

ALERT

Multi-Faceted SBA Final Rule Clarifies Existing Regulations and Brings Long-Awaited Changes

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WHAT: The U.S. Small Business Administration (SBA) published a sweeping final rule implementing several provisions of the National Defense Authorization Acts of 2016 and 2017 and the Recovery Improvements for Small Entities After Disaster Act of 2015 (RISE Act), as well as clarifying existing regulations. The new rule addresses contracting preferences for small businesses in disaster areas; SBA Procurement Center Representative (PCR) reviews; contracting officer oversight of subcontracting restrictions; limitations on subcontracting exclusions; indirect costs in commercial subcontracting plans; material breach of subcontracting plans; size and status recertifications; and the kit assembly exclusion to the non-manufacturer rule (NMR).

WHEN: The SBA published the rule on November 29, 2019, effective December 30, 2019.

WHAT DOES IT MEAN FOR INDUSTRY: SBA's new rule touches on many different areas, from oversight to contract administration. While some of these changes will have minimal direct effect on contractors, others could significantly impact the way small and large businesses seek opportunities and structure their agreements and proposals.

- Contracting Preferences in Disaster Areas: Pursuant to the RISE Act, the final rule creates a new preference program for small businesses located in "major disaster" areas. Under this provision, contracting officers may set aside solicitations for emergency response contracts to allow only small businesses located in the disaster area to compete. Additionally, if an agency awards an emergency response contract to a local

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small business that also has a socioeconomic certification (e.g., 8(a), HUBZone, veteran-owned, or woman-owned), the agency will receive double credit towards its small business goals. (13 C.F.R. § 129)

- PCR Reviews: The final rule clarifies that SBA PCRs may review any acquisition and make recommendations to the contracting officer, even those where the acquisition has already been totally or partially set aside for small business. Absent a specific request by the contracting agency, however, PCRs will not review the following types of acquisitions: those for foreign military sales by or on behalf of the Department of Defense if conducted for a foreign government under 22 U.S.C. § 2762 (the Arms Control Export Act); those for humanitarian or civic assistance provided in conjunction with U.S. military operations under 10 U.S.C. § 401(e); those for a contingency operation under 10 U.S.C. § 101(a)(13); those for awards under an agreement with a foreign government in which U.S. armed forces are deployed; or, those where both the place of award **and** the place of performance are entirely outside of the United States and its territories. (13 C.F.R. § 125.2(b)(1)(i))
- Contracting Officer Oversight of Subcontracting Restrictions: The final rule clarifies that contracting officers have the discretion to request that prime contractors demonstrate compliance with the limitations on subcontracting requirements at any point during performance or upon completion of a contract. SBA provided a non-exhaustive list of documentation that contracting officers could request, such as copies of subcontracts, or a list of subcontractor payments from the prime contractor for a particular procurement and whether those subcontractors are similarly situated entities. (13 C.F.R. § 125.6(e)(4)).
- Exclusions from the Limitations on Subcontracting: The final rule provides that certain types of other direct costs may be excluded from the limitations on subcontracting rule to the extent they are not the “principal purpose of the acquisition” and are not provided by small businesses. The rule provides a list of industries as examples of potentially excluded costs: (1) airline travel; (2) work performed by a transportation or disposal entity under a contract assigned the environmental remediation North American Industry Classification System (NAICS) code 562910; (3) cloud computing services; and (4) mass media services. The list of industries is not meant to be all inclusive, and small businesses can argue that other direct costs similar to the four identified industries should be excluded if they meet the other criteria. The rule also exempts work performed overseas on awards made pursuant to the Foreign Assistance Act of 1961 or work required to be performed by a local foreign contractor. (13 C.F.R. § 125.6(a)(1))
- Indirect Costs in Commercial Subcontracting Plans: The final rule requires that prime contractors with commercial small business subcontracting plans include indirect costs in their commercial subcontracting plan goals rather than make such inclusion optional. This rule will align the plans with the summary subcontract report requirements which already require indirect cost reporting. This rule is expected to somewhat increase the amount of subcontracting goal dollars for small businesses, but most commercial subcontracting plans already included indirect costs according to eSRS data. (13 C.F.R. § 125.3(c)(1)(iv))
- Material Breach of Subcontracting Plans: The final rule provides that it shall be a material breach of contract to fail to make a good faith effort to comply with a small business subcontracting plan or

provide timely subcontracting reports. Such a breach would expose the contractor to liquidated damages, in addition to the remedies already available in FAR 52.219-9. (13 C.F.R. § 125.3(d))

- Size and Status Recertification: The final rule clarifies that the requirement that small businesses recertify their size and status for long-term (over 5 years) contracts includes long-term contracts awarded to small businesses through full and open competition. To promote consistency across SBA's contracting programs, the rule also adds language to harmonize the recertification requirements of 8(a) participants with the requirements already present in the service-disabled veteran owned small business, HUBZone, and woman-owned small business regulations. (13 C.F.R. §§ 124.521, 124.1015, 125.18(f), 126.601(i), & 127.503(h))
- Kit Assemblers & Non-Manufacturer Rule: The final rule removes the kit assembler exception to the NMR. Small business prime contractors who are not manufacturers may nevertheless supply products if those products are acquired from another small business. If SBA determines that there are no small business manufacturers available to supply a product, it may waive the NMR for the specific acquisition or for an entire product class. Under the kit assembler exception to the NMR, only 50 percent of the total value of the kit had to be supplied by a small business. This led to confusion about the kit value and whether the contracting officer was required, or even could, seek a NMR waiver for the excluded items. The final rule removes the kit assembler exception, and instead applies the existing multi-item acquisition rule at 13 C.F.R. § 403(e) to kit assemblers. Under the multi-item rule, if at least 50 percent of the estimated contract value is composed of items manufactured by small businesses then the acquisition can be set aside for small business without the need to request a waiver, even if not all items are manufactured by small businesses. If not, a waiver is required for sufficient items to reach the 50 percent estimated contract value threshold. (13 C.F.R. § 121.406)

Wiley Rein stands ready to assist businesses of all sizes to navigate this complex area of government contracts regulations.

Nicholas Perry, a Law Clerk in the Government Contracts practice, contributed to this alert.