

ALERT

SBA Issues Final Rule Expanding Mentor-Protégé Program to All Small Businesses

July 26, 2016

WHAT: The SBA issued a long-awaited final rule establishing a Government-wide mentor-protégé program for all small businesses. The final rule is largely consistent with the proposed rule, but one underlying theme of many changes was a relaxing of participation and reporting requirements, to both encourage more participation and ease concerns over administrative burdens on participants and the SBA. Get the final rule [here](#).

WHEN: The final rule was issued on July 25, 2016.

WHAT DOES IT MEAN FOR INDUSTRY: Large business will now have a much wider selection of businesses to mentor (SBA anticipates having over 2,000 protégés), and small businesses outside the 8(a) program will have access to the mentor-protégé program's many benefits. Further, once SBA begins approving new mentor-protégé applications, contractors can expect that virtually every significant small business set-aside competition will involve one or more mentor-protégé joint ventures.

EFFECTIVE DATE: August 24, 2016.

OUR ANALYSIS:

On July 25, 2016, the Small Business Administration (SBA) issued a final rule expanding the 8(a) mentor-protégé program to include all businesses designated small, not just 8(a) program participants. All small businesses—women-owned small businesses (WOSB), service-disabled, veteran-owned small businesses (SDVOSB), HUBZone firms, and even “regular” small businesses not part of a designated SBA program—will now be eligible for the many benefits of this critical

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business development tool.

As discussed previously after SBA issued its proposed rule, the purpose of the mentor-protégé program is to encourage approved mentors to provide various forms of business development assistance to protégé firms. For small business, the program provides an opportunity to obtain valuable technical, management, financial and/or contracting assistance from established government contractors. The primary incentive for large businesses to participate as mentors is the ability to form a joint venture with their protégé to pursue small business set-aside contracts. Starting on August 24, 2016, all types of small businesses will be eligible to participate in the mentor-protégé program and pursue small business set-aside contracts with their large business mentors, provided they meet SBA's qualifications and joint venture requirements.

Qualifications of Mentors and Protégés

Consistent with SBA's stated objective, the new Government-wide mentor-protégé program is very similar to the current program for participants in the SBA's 8(a) Business Development program.

The rule retains essentially the same qualification requirements for becoming a mentor that currently apply for the 8(a) mentor-protégé program: a mentor must be a for-profit business that demonstrates a commitment and the ability to assist small business concerns. To meet these requirements, the mentor must possess good character, may not be currently suspended or debarred, and, most importantly, can impart value to a protégé firm due to lessons learned and practical experience. Notably, the final rule removed the requirement in the proposed rule that the mentor "possesses a good financial condition," as SBA agreed with comments that such a requirement was confusing and not directly relevant to whether a firm would be a good mentor. The final rule was changed to require instead that the mentor demonstrate that it can meet its obligations outlined in the mentor-protégé agreement.

Also consistent with the current framework, under the final rule a mentor can have no more than one protégé at a time, but can have up to three protégés if authorized by the SBA. Obtaining SBA approval for an additional protégé requires the mentor to demonstrate that the additional mentor-protégé relationship will not adversely affect the development of either protégé firm. The final rule also permits a small business to be both a protégé and a mentor, with SBA approval.

The rule makes significant changes to the qualification requirements for protégés by opening the mentor-protégé program up to "larger" and more established small businesses. The rule eliminates the current the 8 (a) program protégé qualifications, and would allow firms participating in all SBA programs to qualify as protégés as long as they qualify as small under their primary NAICS code. In a departure from the proposed rule, firms that are not small under their primary NAICS code will be allowed to form mentor-protégé relationships under a secondary NAICS code where they qualify as small, as long as the prospective protégé can demonstrate that such a relationship is a "logical progression for the firm and will further develop current capabilities." SBA warned that the mentor-protégé program was not intended to allow firms that have outgrown their primary NAICS code to enter into a completely new industry, but agreed that a firm already growing into a secondary industry could benefit.

In the final rule, SBA removed the requirement in the proposed rule that that prospective protégé firms obtain formal SBA verification of their small business size status before receiving approval to participate in a mentor-protégé relationship. SBA agreed with comments that argued SBA's size protest mechanism was sufficient to protect the integrity of the program without this extra step. SBA thus clarified that approval of a mentor-protégé agreement would not be a formal determination of size eligibility by the SBA.

In the proposed rule, the SBA proposed to limit the duration of mentor-protégé agreement to three years, and to permit a protégé to have one three-year mentor protégé agreement with one entity and one three-year mentor protégé agreement with another entity. Because of concerns that three years was too short to form a meaningful relationship, the final rule continues to authorize two three-year mentor-protégé agreements with different mentors, but will allow each to be extended for a second three years provided the protégé has received the agreed-upon business development assistance and will continue to receive additional assistance.

Joint Venture Requirements

The rule also makes a number of changes to the rules governing the formation and approval of joint ventures. The rule clarifies that the joint venture must be created through a formal written document setting forth all of the responsibilities of the parties as a partnership, regardless of whether a new legal entity, such as a limited liability company, is formed or not. The SBA had considered requiring the creation of a new legal entity for the joint venture, but the final rule continues to allow informal joint ventures. However, the final rule clarifies the potential consequences of an informal joint venture, such as the joint venture being considered a partnership under state law, with the attendant fiduciary duties imposed upon the partners.

Consistent with the proposed rule, the final rule eliminates the option to create a joint venture entity populated with employees who will be performing the contract. Instead, the joint venture entity must be unpopulated or populated only with administrative personnel. The SBA's concern is that the large business mentor would populate the joint venture with its own employees, and it would be too difficult to determine what benefits the protégé is receiving from the relationship.

The final rule allows mentors to own up to 40% of their small business protégés. The final rule does not adopt the proposal to require mentors to divest this ownership interest once the mentor-protégé agreement expires. SBA agreed with many comments that argued the SBA's affiliation regulations were sufficient. The final rule also recognizes that having the mentor serve as a subcontractor to the protégé is a recognized form of assistance under the program.

Consistent with the proposed rule, the final rule states that contracting agencies must consider the past performance of the members of a joint venture when considering the past performance of an entity submitting an offer as a joint venture. This was in recognition of the difficulty newly established joint ventures have in demonstrating positive past performance where the agency requires the specific joint venture entity itself to have the experience and past performance, rather than the individual joint venture partners.

Other changes to the joint venture rules also signify SBA's concern that this expansion of the program could create opportunities for abuse. The rule requires all joint venture partners participating in a small business set-aside contract to certify to the contracting officer and to the SBA prior to performing the contract that they will perform the contract in compliance with the joint venture regulations. The joint venture must also submit annual reports to the contracting officer and SBA certifying compliance with joint venture requirements and explaining how the performance of work requirements are met.

Although SBA was not willing to eliminate the annual reporting requirement for joint ventures that was included in the proposed rule, the final rule does not require firms outside the 8(a) program to report on joint venture awards received and how they are meeting the limitations on subcontracting requirements. Instead, to enable SBA to track joint venture awards, the final rule requires joint ventures under the mentor-protégé program to register in SAM, with separate DUNS and CAGE numbers, listing the joint venture partners.

The final rule eliminates one concern that many large businesses had with the proposed rule with regard to access to records. The proposed rule seemingly allowed SBA unfettered access to the records of not only the joint venture, but to the records of each member of the joint venture. The final rule clarifies that access is limited to documents relevant to the joint venture. The final rule also requires contractors to certify that SBA representatives will have access to files and records of the joint venture itself when necessary.

Submission of Applications

In anticipation of the thousands of new mentor-protégé applications that will be submitted to SBA under the new program, the final rule gives the SBA the discretion to decide that if the number of mentor-protégé applications becomes "unwieldy," SBA can institute "open" and "closed" periods for the receipt of mentor-protégé applications. SBA would then accept applications only during "open" periods. The final rule establishes a dedicated office within the SBA's Office of Business Development to oversee the mentor-protégé program, which SBA believes should decrease the likelihood that it will need to institute a "closed" period.

If contractors have not already lined up partners for the newly expanded mentor-protégé program, now is the time. Once the SBA begins approving new mentor-protégé applications next month, virtually every significant small business set-aside competition will likely involve one or more mentor-protégé joint ventures.