

**UNDERSTANDING SBA'S PROPOSED  
RULE CHANGES FOR  
THE MENTOR-PROTÉGÉ PROGRAM  
AND LIMITATIONS ON SUBCONTRACTING**



**A PilieroMazza Webinar**  
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# PRESENTED BY

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PilieroMazza PLLC is a full-service law firm located in Washington, D.C. We are most well known as a government contracting firm and for 25 years we have helped our clients navigate the complexities of doing business with the federal government. We also provide a full range of legal services including advice on corporate, labor and employment, SBA procurement programs, and litigation matters. Our clients value the diverse array of legal guidance they receive from us and our responsiveness as we guide their growth and secure their success.

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***Legal Advisor Newsletter*** – our quarterly publication which addresses current issues that are of concern to federal government contractors and commercial businesses nationwide. The Legal Advisor articles focus on recent legal trends, court decision, legislative and regulatory rule-making as well as other newsworthy events.

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## OVERVIEW

- ❖ Two new proposed rules from SBA:
  - Mentor-protégé program for all small businesses
  - Limitations on subcontracting
- ❖ Both rulemakings contain many other proposals that will impact SBA's rules pertaining to:
  - Joint ventures
  - The 8(a) and HUBZone programs
  - Affiliation
  - Size recertification
  - And more



**THE PROPOSED RULE TO CREATE A NEW  
MENTOR-PROTÉGÉ PROGRAM AVAILABLE TO  
ALL SMALL BUSINESSES**



## **TIMELINE**

- ❖ **Proposed rule would implement 2010 Small Business Jobs Act and 2013 National Defense Authorization Act (“NDAA”)**
- ❖ **Proposed rule issued February 5, 2015**
- ❖ **Comments currently due April 6, 2015**
- ❖ **Target date for final rule?**



# PROPOSED MENTOR PROTÉGÉ PROGRAM

- ❖ One new program available to all small businesses
- ❖ Patterned on existing 8(a) Mentor-Protégé Program
  - Designed as a business development tool to enhance protégé's capabilities
  - Financial, technical, and/or management assistance
  - Would allow all small business protégés to joint venture with their large business mentors
  - Mentor could own up to 40% of the protégé
  - Also envisions assistance through loans, financing, prime contracts, and subcontracts



## PROTÉGÉ ELIGIBILITY

- ❖ Must be small under its primary NAICS code and in need of mentoring
  - For 8(a), protégé must also show positive impact on its business plan
- ❖ Must undergo a formal SBA size determination (either in the past or as part of the mentor-protégé application)
- ❖ Must identify mentors for other agency mentor-protégé programs
- ❖ Generally, may not have more than one mentor at a time
  - SBA may permit a second mentor if the second mentor brings different expertise from the first mentor or if they can assist the protégé in an unrelated, secondary NAICS code





## MENTOR ELIGIBILITY

- ❖ Must possess good financial condition, commitment to mentoring, and good character
- ❖ Only for-profit firms
- ❖ Generally, no more than one protégé at a time
  - However, SBA may approve up to three protégés for the same mentor if there is no adverse impact on any protégé
- ❖ A protégé cannot also be a mentor



## HOW TO APPLY

- ❖ SBA is proposing one office to receive applications from all small businesses except 8(a) firms; separate SBA office would continue processing 8(a) MP applications
  - SBA envisions that 8(a) firms could apply to either office
  - SBA is seeking comment on whether to consolidate the applications into one office
- ❖ SBA may utilize “open” and “closed” application periods
  - Unclear how many applications will be filed and how SBA will keep up
  - No details provided on thresholds for or timing of open and closed periods
  - This did not work well for VA's mentor-protégé program, which was closed more than open



## PARTICIPATION PERIOD

- ❖ **Proposed participation period: up to three years in one agreement, maximum of six years overall**
  - **Protégé may have two three-year agreements with two different mentors, or two three-year agreements with the same mentor**
  - **Only for-profit firms**
  - **SBA will review agreements annually**



## IMPACT ON OTHER MENTOR-PROTÉGÉ PROGRAMS

- ❖ Agencies without statutorily-authorized programs will need to seek SBA approval of their program within one year
- ❖ DoD's mentor-protégé program is not affected
- ❖ May signal end of other mentor-protégé programs
  - Some are likely to remain, but SBA questions utility of these programs once it has a government-wide program up-and-running for all small businesses



## PROPOSALS FOR JOINT VENTURES

- ❖ SBA is attempting to clarify what it means by “informal” joint ventures – i.e., a joint venture not formed as a separate legal entity
- ❖ Would eliminate populated joint ventures for “formal” joint ventures
  - Why not for “informal” joint ventures as well?
- ❖ Will all joint ventures need to be formed as a separate legal entity?
- ❖ Annual certifications of compliance from joint ventures, with possibility of suspension/debarment for noncompliance
- ❖ What is the best way for SBA to track JV awards?



## JOINT VENTURES (CONTINUED)

- ❖ Uniform requirements for all small business programs regarding size and content of JV agreement
  - Comparable to existing 8(a) JV requirements (e.g., small business must perform at least 40% of the work)
  - HUBZone firms may JV with non-HUBZone firms
  - Size protests permitted, including for 8(a) JVs



## JOINT VENTURED (CONTINUED)

- ❖ Despite many similarities, there are some differences:
  - Proposal would require joint venture partners to share profit commensurate with their ownership interests in a separate legal entity joint venture
  - Mentor-protégé proposed rule retains existing rules that determine the size of a joint venture based on the size of the procurement
    - SBA proposed to eliminate this in the limitation on subcontracting rulemaking
  - No prior approval of joint venture agreement by SBA except for 8(a) contracts
  - 8(a) firms would be allowed to submit a joint venture to SBA for approval at any time



## PROPOSALS FOR THE 8(A) PROGRAM

- ❖ **New rule would change how SBA assesses an applicant's claim of social disadvantage**
  - **Would permit SBA to disregard an applicant's claim if the applicant does not provide sufficient evidence to make his/her claim any more likely than a legitimate alternate reason for adversity the applicant has faced**
  - **Designed to alter recent OHA case law favorable to applicants**
  - **Does this proposed rule raise the evidentiary burden on applicants above the current preponderance of the evidence standard?**





## **8(A) PROGRAM (CONTINUED)**

- ❖ SBA would have discretion to change a participant's primary NAICS code based on plurality of firm's revenues over the most recent three years
- ❖ 8(a) firms could elect to suspend their program term if they are located in a declared major disaster area or if subject to a lapse in federal appropriations



## 8(A) PROGRAM (CONTINUED)

### ❖ Tribally-owned 8(a)s:

- No one individual could be responsible for the management or daily operations of more than two such firms at the same time
- Tribally-owned concerns and NHOs generally maintain a broad exemption from affiliation with the Tribe/NHO or related entities unless SBA determines the concern has or is likely to gain a substantial unfair competitive advantage
  - SBA will examine the firm's participation in the relevant NAICS code nationally as compared to the overall small business share



# **THE PROPOSED RULE FOR THE LIMITATIONS ON SUBCONTRACTING**



## TIMELINE

- ❖ Proposal would implement the 2013 NDAA
- ❖ Released December 29, 2014
- ❖ Comments were originally due February 27, 2015; comment period extended to April 6, 2015
- ❖ Final rule may be issued by the end of 2015, but more likely in 2016



## PROPOSED NEW SUBCONTRACTING LIMITS

- ❖ Proposed rule keeps the same subcontracting limits as are found in the existing rule:
  - 50% for services
  - 50% for supplies
    - Statute provides an exclusion for the cost of materials on supply contracts, but SBA left this out of the proposed rule
  - 15% for general construction
  - 25% for specialty trade construction
- ❖ However, rather than base the percentage off of the contract's labor costs like the existing rule, the proposed rule would shift the focus to the total contract value



## MIXED SERVICE AND SUPPLY CONTRACTS

- ❖ **NAICS code assigned to the contract will determine applicable subcontracting limit – services or supplies**
  - **In no case would the subcontracting limits for services and supplies apply to the same contract**
- ❖ **The applicable limitation on subcontracting (either for services or supplies) “shall apply only to that portion of the contract award amount”**
  - **This should mean that, on a contract primarily for services, you can exclude any supplies and apply the “50% of the total cost of the contract” subcontracting limitation to only the services portion of the contract**



## **SBA EXAMPLE FOR MIXED SUPPLIES AND SERVICES CONTRACT**

“A procuring agency is acquiring both services and supplies through a small business set aside. The total value of the requirement is \$3,000,000, with the supply portion comprising \$2,500,000, and the services portion comprising \$500,000. The contracting officer appropriately assigns a manufacturing NAICS code to the requirement. Because the services portion of the contract is excluded from consideration, a small business manufacturer, together with one or more similarly situated small business manufacturers, must perform at least 50% of the cost of manufacturing the supplies or products, or at least 50% of the \$2,500,000 supply portion of the requirement (not including the costs of materials).” (Emphasis added)



## CONSTRUCTION CONTRACTS

- ❖ Proposed rule does not exclude cost of supplies or materials for construction contracts, meaning such costs would be included in the total contract value
- ❖ If the proposed rule is adopted, the existing percentages of 15% and 25% will be unworkable for many small business construction projects
- ❖ Why not keep the exclusion for the cost of materials found in the existing construction rule?
  - 2013 NDAA gave SBA freedom to implement rules for construction, so it does not have to change the existing rule
  - 2013 NDAA includes an exclusion for the cost of materials on supply contracts, so why not for construction as well?





## **SIMILARLY SITUATED ENTITIES**

- ❖ Any work done by a similarly situated small business will not constitute “subcontracting”
- ❖ A similarly situated entity is a firm that meets the same size/status requirements as the prime contractor for the project in question
- ❖ Prime contractor and its similarly situated subcontractors must perform the required amount of work “themselves” – cannot flow down to large business subcontractors
- ❖ Percentage of the prime contract award amount that will be spent on each similarly situated entity must be identified in a written agreement with the similarly situated entity
  - Written agreement must be attached to the prime contractor’s proposal



## COMPLIANCE

- ❖ Compliance will be an element of responsibility and not a component of size eligibility (i.e., no size protests)
- ❖ Prime contractor must certify its compliance in its proposal
- ❖ Time period used to determine compliance for a total or partial set-aside would be the base term and then each subsequent option period
  - Contracting Officer (“CO”) would have discretion to require compliance for each order
  - For an order under a full and open contract, the time period will typically be the period of performance for each order
- ❖ Potential monetary penalties of \$500,000 or more



## **PROCEDURES FOR CHANGING THE LIMITATION FOR A SPECIFIC NAICS CODE**

- ❖ SBA is proposing procedures for industry groups or interested small businesses to request the SBA Administrator to change the subcontracting limitation for a specific six-digit NAICS code
- ❖ The request must demonstrate that the change is necessary to reflect industry practices among small businesses in that NAICS code
- ❖ For SBA to grant such a request, it must go through a rulemaking process (i.e., public notice and opportunity for comment)



## AFFILIATION

- ❖ Two proposed changes for identity of interest affiliation:
  - Rebuttable presumption of identity of interest affiliation through family relationships exists for firms that conduct business with each other and are owned and controlled by persons who are married, parties to a civil union, parents and children, or siblings
  - Rebuttable presumption of affiliation through economic dependence when one firm derives 70% or more of its revenue from another firm over the previous completed fiscal year
    - May be rebutted when a firm is new or a start-up and has only received a few contracts or subcontracts
    - Why only one fiscal year when current measurement is based on three?



## JOINT VENTURES

- ❖ Currently, SBA looks at the aggregate size of both joint venture partners to determine if the joint venture is small, except for bundled contracts or larger procurements (i.e., those exceeding one-half the size standard for the contract or \$10 million)
- ❖ SBA is proposing to permit two or more small businesses to joint venture for any procurement, regardless of the size of the procurement, as long as each firm is considered to be small for the procurement
  - This is a favorable proposal and will allow more small businesses to joint venture



## SIZE RECERTIFICATION

- ❖ **Existing rule:** small businesses must recertify their size to the CO on existing set-aside contracts when they undergo a merger or acquisition
- ❖ **Proposed rule:** small businesses would have to recertify size to the CO on pending proposals where a merger or acquisition occurs after proposal submission but prior to award
  - How will recertification in this circumstance affect the agency's willingness to award the contract to that firm?
  - Is SBA moving toward requiring all small businesses to be eligible at the time of proposal submission and the time of award?



## NAICS CODE APPEALS

- ❖ An interested party may challenge the NAICS code assigned to a solicitation by filing an appeal with SBA's Office of Hearings and Appeals
  - Currently, an appeal must be filed within 10 calendar days after issuance of the solicitation or amendment affecting the NAICS code
  - SBA is seeking comment on whether 10 days is the appropriate timeline, in light of the fact that many procurements close in less than 30 days
- ❖ SBA is also assessing the impact a NAICS code appeal should have on the solicitation in question
  - SBA is seeking comments on whether its rules should provide that the CO should not award the contract or delay the offeror or bid response date (Yes!)



## NONMANUFACTURER RULE

- ❖ SBA is proposing to clarify that the limitations on subcontracting and the nonmanufacturer rule do NOT apply to small business set-aside contracts between \$3,000 and \$150,000
  - This means a small business can supply the product of a large business on small business set-asides in this dollar range
  - Expected to spur more small business set-asides and help small businesses fulfill acquisitions of products manufactured by large businesses (such as computers and other “name brand items”)
- ❖ However, the limitations on subcontracting and nonmanufacturer rule would continue to apply to 8(a), HUBZone, SDVOSB, and WOSB/EDWOSB set-asides between \$3,000 and \$150,000





## NONMANUFACTURER RULE (CONT'D)

- ❖ Proposed changes to nonmanufacturer rule waivers:
  - COs would be required to notify potential offerors in the solicitation if a class or individual waiver applies
  - SBA would be authorized to grant a waiver for an individual contract award after the solicitation has been issued, as long as the CO gives all potential offerors additional time to respond
  - SBA would also be authorized to grant waivers after contract award when additional items that are waiver-eligible are sought through an in-scope modification
- ❖ SBA is clarifying that waiver of the nonmanufacturer rule does not exempt other requirements pertaining to the supplied item, such as the Buy American Act and the Trade Agreements Act



## SOFTWARE PURCHASES

- ❖ **Nonmanufacturer rule would apply to software that is generally available to both the public and private sector unmodified**
  - Change would allow SBA to grant waivers of the nonmanufacturer rule for such software, permitting small businesses to supply software made by large businesses on set-aside contracts
  - Agencies would use NAICS code 511210 when purchasing software eligible for a waiver
- ❖ **Change would not affect contracts for the creation or modification of custom-design software**
  - SBA will continue to treat such software as a service, requiring small businesses (together with similarly situated entities) to perform the required percentage of the work



# Any Questions?

Thank you for joining us today.

If you would like to speak with Pam or Jon about the proposed rule changes, please contact them at:

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