ProTorÆ Law PLLC

Small Business Regulatory Update

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AGENDA

- Overview of What's New and What's Not New
- *New* SBA All Small Mentor-Protégé Program
- Affiliation Rules
- SBA Joint Venture Regulations Review
- *New* Limitations on Subcontracting Rules
- 8(a) Business Development Program Review
- Wrap Up and References/Resources

Overview

OVERVIEW

WHAT'S NEW

Two newly-implemented rules that allow small businesses to pursue more small business opportunities when working with other contractors (both large and small):

- All Small Mentor-Protégé Program
- Limitation on Subcontracting Rule

WHAT'S NOT NEW

- Definition of a Small Business
- Joint Ventures (as applied to 8(a) and new All Small Mentor-Protégé Program)

New SBA All Small Mentor-Protégé Program

NEW ALL SMALL MENTOR-PROTÉGÉ REGULATIONS

- Small Business Mentor-Protégé Programs Final Rule (81 Fed. Reg. 48558), published July 25, 2016, *effective August 24, 2016*
- SBA was supposed to begin accepting (electronic) applications October 1, 2016; electronic portal actually went live November 1, 2016
  - certify.sba.gov

ALL SMALL MENTOR-PROTÉGÉ PROGRAM

New All Small Mentor-Protégé Program is distinct from the Section 8(a) Mentor-Protégé Program, although similar requirements

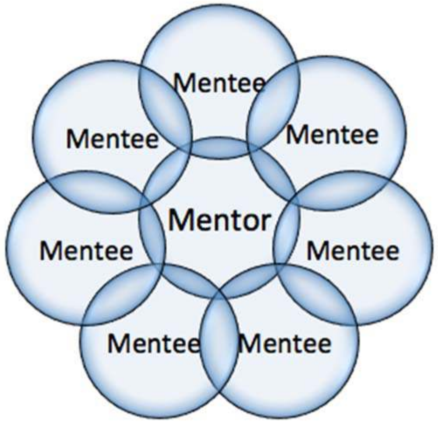
- Mentor must provide tangible financial, technical, or management assistance to Protégé
- Mentor may own up to 40% of Protégé
- Permits joint ventures between small and “other than small” firms
- Exemption from affiliation

INCLUDES SMALL BUSINESSES, SDVOSBs, WOSBs, HUBZone, AND 8(a) CONCERNS

APPLICATION PROCESS

- Applications will be processed by a "unit" in the SBA Office of Business Development
- No "open/closed" periods initially
- Online application process at certify.sba.gov
- Must register in SAM before submitting application
- Both Mentor and Protégé must complete on-line training before submitting application documents
- If SBA rejects application, request for reconsideration must be filed within 45 days
- SBA supposed to issue reconsideration decision within 45 days
- If SBA rejects application, Protégé must wait 60 days before submitting another application with the *same* Mentor

MENTOR



- Must be a for-profit entity
- Can be any size
- Good character/not suspended or debarred
  - Must have financial capacity to fulfill Mentor-Protégé Agreement (MPA) obligations
- May only have 3 Protégés at 1 time
  - Across the 2 programs
  - Must show that multiple MPAs won't hinder the development of any 1 Protégé
- If Mentor experiences a change of control, Mentor must express in writing its commitment to the MPA
- A Mentor can also be a Protégé

PROTÉGÉ

- Must be small under size standard associated with primary NAICS code
- Can get MPA in secondary NAICS code if small under that NAICS code
  - If no longer small under primary NAICS code, Protégé must show prior experience under the secondary NAICS code and that proposed Mentor-Protégé relationship is a logical business progression for the firm
- May have up to 2 Mentors
  - SBA will approve second MPA only if relationship is under different NAICS code and different types of assistance provided
- Protégé may serve as Mentor
- While applicants self-certify, SBA may review SDVOSB and WOSB certifications as part of application process

MENTOR-PROTÉGÉ AGREEMENT (MPA)

- Must be in writing (template available online at Sample Mentor-Protégé Agreement Template)
- Must detail specific assistance (with timeline) to be provided by Mentor to Protégé
- Minimum 1 year commitment
  - After 1 year, may be terminated upon 30 days advance notice
  - Initial term is 3 years; may be extended for additional 3 years
  - SBA may terminate MPA anytime
- Must identify any other Mentor-Protégé relationships
- Must identify Mentor single point of contact for MPA
- Any changes to MPA must be approved by SBA

REPORTING OBLIGATIONS

- Within 1 year of the anniversary date of MPA approval, Protégé must provide exhaustive report to SBA
- Report includes the nature and quantity of the assistance provided by the Mentor
- Includes annual certification from Protégé that the MPA has not changed
- Continued MPA relationship subject to SBA approval

CONSEQUENCES OF SBA DISAPPROVAL

- SBA will first notify Mentor and allow it to respond to SBA concerns
  - If response inadequate, SBA may terminate the MPA
  - Firm cannot be a Mentor again for 2 years
- SBA may also request that agency issue stop work orders on Mentor-Protégé JV contracts
  - SBA may recommend that Protégé be substituted as contract awardee
- Suspension/Debarment possible

MISCELLANEOUS

8(a) can transfer 8(a) Mentor-Protégé relationship to All Small Mentor-Protégé Program upon graduation from the 8(a) Program

- Only need to provide notice to SBA; don't need to go through application process
- Eliminated provision that prohibited 8(a) concern from applying to Mentor-Protégé Program if within 6 months of 8(a) Program graduation

OTHER AGENCY MENTOR-PROTÉGÉ PROGRAMS

- Other agency programs may continue for 1 year
- Agency must seek SBA approval after that year to continue (exception for DoD program, Small Business Innovation Research (SBIR)/Small Business Technology Transfer (STTR) program)
- Authorizes agencies to provide incentives to contractors participating in a Mentor-Protégé program and promising significant subcontracting work

Affiliation

AFFILIATION

- Members of a JV that submit an offer on a procurement are presumed to be **affiliated** with one another for the purposes of that procurement
- If a small business is determined to be “affiliated” with another company, SBA will aggregate the size of the 2 companies in determining the small business’ “size”
- If the aggregate size of the affiliated members exceeds the size standard of the NAICS code for a small business procurement, the JV will not be eligible for the award; there are exceptions

EXCEPTIONS TO AFFILIATION

When ALL members are "small" under the size standard for the NAICS code of the solicitation

≈ *OR* ≈

The members are in an approved SBA Program MPA

- Certain special conditions apply to SBA JV agreements

SBA Joint Venture Requirements/Characteristics

SBA DEFINITION OF JOINT VENTURE

- When 2 or more businesses enter into a temporary partnership, usually associated with a specific contract or series of contracts, that is mutually beneficial to both businesses
  - Association of individuals or companies that come together to combine resources and bid on contract opportunities
- Allowed 3 contract awards per JV within 2 years
  - Known as the "3 in 2" rule
  - Members may form another JV and receive another 3+ contract awards

JOINT VENTURES

- Relationship must be reduced to a written agreement
- Must be unpopulated (i.e., does not use the JV's own employees to perform contracts – serves as a vehicle by which the JV members can collectively serve as the prime contractor, with each JV member performing work with its own employees)
  - If a separate legal entity, Protégé must own 51% of the entity and ***profits must be distributed commensurate with work performed (8(a) and All Small Business Program JVs)***
- Must be separately identified in SAM for tracking purposes
- Written agreement must include specifics
  - Major equipment, facilities, resources
  - Responsibility for source of labor
- Protégé must perform 40% of the work

JOINT VENTURES

- Protégé must be "Managing Member"
- Program Manager must be employed/appointed by the Protégé
  - May be contingent employee
  - Cannot be employee of Mentor
- Mentor cannot exercise "negative control" over Protégé
- Both members required to ensure performance of Government contract; no withdrawal from JV permitted
- Separate bank account for overall JV, *joint signatures required*
- Managing Member must physically maintain JV records
- SBA reporting requirements apply

JOINT VENTURES

- Only 8(a) contracts require prior SBA approval of JV agreements
- 8(a) JV can submit agreement for approval at any time
- HUBZone firms may form a JV with non-HUBZone firms
  - Protégé cannot rely on Mentor's employees to satisfy 35% HUBZone residency or principal office requirement

JV WORK PERFORMANCE REQUIREMENTS

- JV must comply with FAR Clause 52.219-14, Limitations on Subcontracting
  - For services, the JV must perform 51% of the cost of labor; work of both JV members included in 51% calculation (revised in SBA regulations – not yet in FAR)
- Protégé must perform at least 40% of the total work performed by the JV members (at any tier)

UNPOPULATED SBA MENTOR-PROTÉGÉ JOINT VENTURE

JOINT VENTURE
Unpopulated

- Acts as a pass-through
- JV must perform at least 51% of the cost of the JV contract incurred for personnel

PROTÉGÉ

- *De facto* subcontractor
- Must perform at least 40% of JV contract

MENTOR

- *De facto* subcontractor
- Can perform up to 60% of JV contract

SUBCONTRACTORS

Can only perform up to 49% of cost of JV contract incurred for personnel

JV CERTIFICATES OF COMPLIANCE

- Applies to all types of JVs
- Prior to a set-aside contract or contract with reserve, each member of JV must certify that the JV:
  - Fully complies with regulatory requirements
  - Will perform the contract in compliance with the JV agreement
  - Will perform the contract in compliance with work performance requirements

JV CERTIFICATES OF COMPLIANCE

- Report detailing compliance with work performance requirements must be submitted annually
- At contract completion, another Certificate of Compliance must be submitted wherein each party:
  - Details how work performance requirements were met
  - Certifies that work performance requirements were met
  - Certifies that the contract was performed in compliance with the JV regulatory requirements
- Failure to submit Certificate of Compliance may be grounds for suspension/debarment

SBA Mentor-Protégé Joint Ventures Advantages/Disadvantages

JV ADVANTAGES

- Provides "one-stop shopping" to the Government for the combined resources of the members (technical and other)
- Has performance history that combines the history of each member
  - Government now required to consider past performance history of each JV member
  - Advantageous when solicitation says past performance of subcontractors will not be considered
- Allows each member to cite the contract as past performance in future proposals

JV ADVANTAGES TO PROTÉGÉ

- Allows a small business to be competitive as a prime contractor
  - Small business may pursue opportunities broader than it would otherwise qualify for
- Small businesses qualify as "small" longer
  - Small businesses must include in receipts or headcount its proportionate share of joint receipts or joint employees

JV ADVANTAGES TO MENTOR

- Large business may pursue set-aside opportunities for which it is otherwise ineligible
  - Large business can perform up to 60% of the work, as opposed to 49% as a subcontractor to a small business prime contractor
- Large business may have more control over contract performance than if it were a subcontractor
  - For JVs under SBA-approved MPAs, control over performance will not lead to "affiliation"
- Large business can gain entry to new agency or program where small business has history

JV DISADVANTAGES

- Some Government officials are not familiar with the model; concerns arise about responsibility for contract performance or non-performance
- Can be a challenge for JV members to “speak with one voice”
- Depending on the JV structure, a member may receive less work than it would as a subcontractor or a single prime contractor
- Large contractor must give up control

JV DISADVANTAGES

- More paperwork and more complicated to set up a JV; can be more expensive
- All the liabilities are shared by all JV members
- JV relationships are harder to exit if they do not work

New Limitations on Subcontracting Rules

NEW REGULATIONS: LIMITATIONS ON SUBCONTRACTING (LOS)

- Proposed Rule issued December 29, 2014
- Final Rule issued May 31, 2016 (81 Fed. Reg. 34243)
  - Effective June 30, 2016
- Standard is now % of amount Government ***paid*** to prime contractor rather than cost of contract
- Cannot pay subcontractor more than certain percentage of amount paid to prime contractor
  - Services (50%), supplies (50%), construction (85%), special trades (75%)

NOT YET IMPLEMENTED IN FAR

NEW REGULATIONS: LOS

- Does not apply to small business set-asides valued between $3,500 and $150,000
- Excludes "similarly situated entity"
  - Subcontractor that has the same small business program status as the prime contractor that made prime contractor eligible for award
  - Already the case for HUBZone and SDVOSB programs
- The subcontractor/entity must also be small under the NAICS code applicable to the *subcontract*

LOS: SIMILARLY SITUATED ENTITY

- First-tier subcontractor (similarly situated entity) must perform work with its own employees; any work subcontracted by the first-tier subcontractor is considered subcontracted work
- Independent contractors are considered subcontractors and can be "similarly situated entities"
- Similarly situated entities exempt from "ostensible contractor" rule
  - A small business that relies too heavily on another business for subcontracting may trigger affiliation under the Ostensible Subcontractor Doctrine, which holds that a small business that "is unusually reliant" on a subcontractor may be deemed affiliated for size determination purposes. This occurs if the subcontractor performs the primary and vital requirements of the prime contract.

LOS: MIXED SERVICE/SUPPLY CONTRACTS

- CO to determine primary purpose of contract and assign corresponding NAICS code
- LOS percentages apply only to that portion considered the primary purpose of the contract
- Includes any overhead or indirect costs associated with primary purpose, but does not include "cost of materials"

LOS: COMPLIANCE

- Period of time to determine compliance in set-aside contract is usually the base term and each subsequent option period
- For an order set aside under a full and open contract with a reserve, period of compliance is period of performance for each order
- CO has discretion under set-aside contract to make compliance correlate to task order period of performance

LOS: PENALTIES FOR NON-COMPLIANCE

- Fine of the greater of $500,000 or the amount spent on subcontracts above the permitted percentage
- Basis for debarment
  - Unless firm made good faith representation that it would use similarly situated entities and meet the LOS requirements, but through “unforeseen circumstances” was unable to do so

Wrap Up

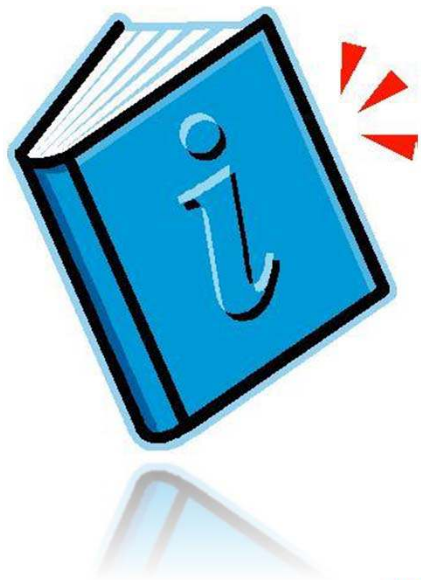
WRAP UP

- Mentor-Protégé JV is a win/win for small and other than small businesses
  - Small businesses can bid on larger contracts
  - Small businesses can get prime past performance
  - Large businesses can perform up to 60% of work set-aside for small businesses
- Mentor-Protégé JV is a win for the Government
  - One-stop shopping
  - Get small business credit, but performance of sophisticated, large business
- Mentor-Protégé JV must follow strict guidelines

References/Resources

REFERENCES/RESOURCES

- SBA Getting Started: SBA Getting Started Home Page
- SBA Blogs: Venturing into a Joint Venture - Need-to-Know Basics
- SBA Mentor-Protégé Program: SBA Mentor-Protégé Program Home Page
- SBA 8(a) Business Development Program: SBA 8(a) Business Development Program Home Page
- SBA All Small Mentor-Protégé Program: SBA All Small Mentor-Protégé Program Home Page
- SBA NAICS Codes: SBA NAICS Codes Home Page



WHAT'S NOT NEW

WHAT IS A SMALL BUSINESS?

- A business that meets certain SBA "size standards"
- Size standards correspond to "codes" published by the North American Industrial Classification System (NAICS) (Census Bureau NAICS Home Page)
- For most industries, SBA defines a "small business" either in terms of average number of employees or average annual receipts over the past 3 years
- Additionally, a small business must:
  - Be organized for profit
  - Have a place of business in the U.S.
  - Operate primarily within the U.S. or make a significant contribution to the U.S. economy
  - Be independently owned and operated
  - Not be dominant in its field on a national basis

WHAT'S NOT NEW

WHAT IS A JOINT VENTURE (JV)?

- A JV is a business agreement in which the parties agree to develop, for a finite time, a new entity and new assets by contributing equity. The parties control the enterprise and, consequently, share revenues, expenses, and assets.
- Key Characteristics:
  - A separate legal entity
    - Usually a partnership (informal) or Limited Liability Company (formal)
  - Includes "members" with proportional interests in the entity
  - Limited in duration
  - Special purpose (i.e., pursuit of contract award)
  - Sharing of profits and losses among members

QUESTIONS/COMMENTS

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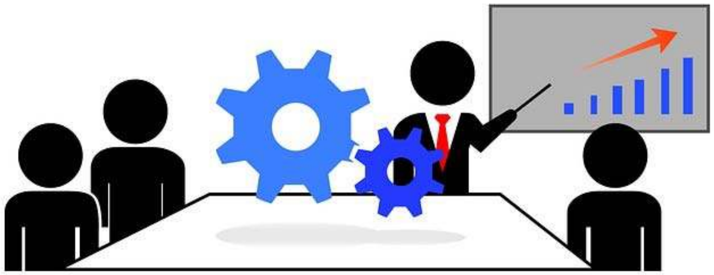
SBA 8(a) Business Development and Mentor-Protégé Program

8(a) BUSINESS DEVELOPMENT PROGRAM

- To help small disadvantaged businesses (SDBs) compete in the marketplace
- The 8(a) Business Development Program is a business assistance program for SDBs to firms that are at least 51% owned and controlled by socially and economically disadvantaged individuals
- Program is divided into 2 phases over 9 years: a 4 year developmental stage and a 5 year transition stage
- Participants can receive sole-source contracts up to ceiling values of \$4M for goods and services and \$6.5M for manufacturing
- 8(a) firms are also able to participate in Mentor-Protégé programs and form JVs with "other than small businesses" to bid on contracts

8(a) BUSINESS DEVELOPMENT PROGRAM

- The overall goal is to develop and graduate 8(a) firms that will go on to thrive in a competitive business environment
- Primary requirements:
  - Maintain a balance between commercial and Government business
  - Limit the total dollar value of sole-source contracts that an individual 8(a) participant can receive while in the program: $100M or 5 times the value of its primary NAICS code



8(a) MENTOR-PROTÉGÉ PROGRAM

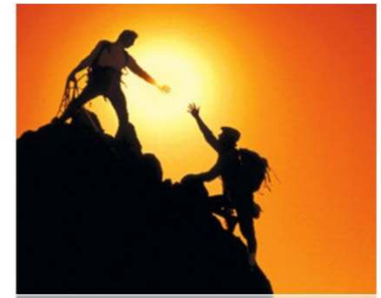
- Alliance between an 8(a) Program participant (Protégé) and typically an "other than small" business as defined by NAICS (Mentor) (although any business can be a Mentor)
- Protégé has identified needs for business development and the Mentor has the capacity to address those needs
- A Mentor can have no more than 3 Protégés at 1 time
- A Protégé generally has 1 Mentor, but can get a second in limited circumstances

8(a) MENTOR-PROTÉGÉ PROGRAM

THE PURPOSE OF THE 8(a) MENTOR-PROTÉGÉ RELATIONSHIP IS TO:

- Enhance the capabilities of the Protégé (an 8(a) Program participant)
- Assist the Protégé with meeting the goals established in its SBA-approved business plan
- Improve the Protégé's ability to successfully compete for Government contracts

8(a) MENTOR-PROTÉGÉ PROGRAM



BENEFITS

- Mentor's expertise, resources, and capabilities are made available to the Protégé
- Mentors can provide assistance relevant to performance of non-8(a) contracts so that Protégé firms more fully develop their competitive abilities
- "Other than small" Mentors can enter into JV arrangements with Protégés to compete for and perform on Government contracts set aside for small businesses without regard to "affiliation"
  - A Mentor-Protégé relationship must be approved by SBA *before a JV: 1) is created, and 2) submits an offer/proposal to the Government*
- Mentors can own up to 40% of the Protégé to help it raise capital