SAM GRAVES, MISSOURI
CHAIRMAN

NYDIA M. VELAZQUEZ, NEW YORK
RANKING MEMBER

Congress of the United States

U.S. House of Representatives
Committee on Small Business

2361 Rayburn House Office Building
Washington, DC 20515–6315

To: Members, Committee on Small Business
From: Committee Staff
Date: February 22, 2013
Re: Small Business Act Programs for Small Federal Contractors

---

This is one in a series of memorandum prepared by the staff of the Committee on Small Business to explain the key concepts and programs integral to government contracting for small businesses. As such, it is not tied to one particular hearing, but serves as a basis for hearing memoranda related to government contracting.

The federal government routinely spends over half a trillion dollars through prime contracts each year. Given the shear volume of dollars spent, this is a crucial market for small businesses as prime contractors and subcontractors. For example, in Fiscal Year 2010, the federal government obligated approximately $536 billion in prime contracts, which in turn resulted in approximately $210 billion in subcontracts.[1] Small businesses received over $109 billion in prime contracts and over $74 billion in subcontracts.[2]

The Small Business Act (the Act) iterates Congress's belief in the importance of small business participation in federal prime contracts and the resultant subcontracts. Specifically, the Act directs that:

> [t]o effectuate the purposes of this Act, small-business concerns within the meaning of this Act shall receive any award or contract or any part thereof, and be awarded any contract for the sale of Government property, as to which it is determined by the Administration and the contracting procurement or disposal agency (1) to be in the interest of maintaining or mobilizing the Nation's full productive capacity, (2) to be in the interest of war or national defense programs, (3) to be in the interest of assuring that a fair proportion of the total purchases and contracts for property and services for the Government in each industry category are placed with small-business concerns, or (4) to be in the interest of

---

[1] Prime contracting data retrieved from the Federal Procurement Data System *available at* www.fpds.gov; subcontracting data provided by SBA and on file with the Committee.
[2] *Id.*

assuring that a fair proportion of the total sales of Government property be made to small-business concerns;

15 U.S.C. § 644(a).

To effectuate these objectives, Congress has enacted six different contract programs overseen by the Small Business Administration's (SBA's) Office of Government Contracting and Business Development. Each of these programs has a statutory goal associated with it, relating to the percentage of prime contract dollars the government should award qualifying firms each year. These programs are the small business contracting program, Historically Underutilized Business Zone (HUBZone) small business program, Woman-Owned Small Business (WOSB) program, 8(a) Business Development (8(a)) program, Small Disadvantaged Business (SDB) programs, and the Service-Disabled Veteran-Owned Small Business (SDVOSB) programs. This document provides a brief overview of each of the programs.

A. The Small Business Prime Contracting Program and Subcontracting Program.

According to the Act, a small business concern is one that is independently owned and operated, organized for profit, and which is not dominant in its field of operations.[3] SBA creates specific size standards for each industry, and assigns revenue- or employee-based size standards[4] to each of the more than 1,100 North American Industrial Classification System (NAICS) codes.[5] Prime contracts can be set aside for small businesses in two ways. First, all contracts below $150,000 are reserved for small businesses unless the contracting officer (KO) determines there is not a reasonable expectation of obtaining offers from two or more firms.[6] Second, any contract over $150,000 should be set aside for small business if the KO determines that at least two small businesses will make offers, and the award can be made a fair price.[7] The business certifies that it is small at the time of offer[8] through the System for Award Management (SAM).[9] If an offeror or the KO believes that the successful bidder is not actually a small business, SBA's size specialists and Office of Hearings and Appeals (OHA) will adjudicate the firm's size.[10] There is a statutory goal of awarding at least 23 percent of all federal prime contract dollars to small businesses.[11]

For subcontracts, any other-than-small business receiving a prime contract worth more than $650,000 (or $1.5 million in the case of contracts for construction) must negotiate a subcontracting plan with the contracting agency as a material condition of the contract.[12]

---

[3] 15 U.S.C. § 632(a). For further information, please see the Committee Memorandum, "What is a Small Business for Purposes of Federal Contracting?" (2013).
[4] In a few instances, other factors are also considered, such as production or assets. *Id.*
[5] 13 C.F.R. § 121. These regulations also provide SBA's affiliation standards, which address the independence of operations.
[6] 48 C.F.R. § 19.502-2(a).
[7] *Id.* at (b).
[8] 13 C.F.R. § 121.404.
[9] *Available at* www.sam.gov.
[10] 13 C.F.R. § 121.1001.
[11] 15 U.S.C. § 644(g)(1).
[12] 15 U.S.C. § 637(d)(4); 48 C.F.R. § 19.702.

Likewise, if the prime contractor is an other-than-small business that in turn subcontracts to an other-than-small business for an amount above the aforementioned dollar thresholds, the subcontractor must negotiate a subcontracting plan with the prime contractor. These subcontracting plans delineate subcontracting opportunities for each of the five categories of small businesses, usually as a percentage of the work that will be subcontracted.[13] Some plans state the goals as a percentage of contract value.[14] Failure to meet the subcontracting goals is reflected in past performance ratings on prime contractors, and if the failure is due to a lack of good faith it can be treated as a material breach of the contract.[15] SBA creates both government-wide and agency goals for subcontracting with small businesses.[16]

B. The Historically Underutilized Business Zone (HUBZone) Program.

A HUBZone is a geographic area with high poverty or high unemployment, as defined through a complicated statutory framework.[17] HUBZone small business concerns are small businesses whose principal office is located in a HUBZone, that are at least 51 percent owned by United States citizens, and which draw at least 35 percent of their employees from HUBZones.[18] These firms can receive set-aside contracts if two or more HUBZone concerns are expected to make a fair and reasonable offer.[19] Sole-source awards are permitted for contracts below $4 million ($6.5 million for manufacturing contracts).[20] A price evaluation adjustment of 10 percent is granted when bidding on contracts offered through full and open competition.[21] To certify as a HUBZone firm, a small business must apply on the SBA website, recertify every three years, certify through SAM, and qualify at the time of offer and the time of award.[22] SBA has the authority to conduct program examinations of firms to verify their continued eligibility[23] or to hear appeals regarding a firm's size[24] or eligibility for the program.[25] There is a statutory goal of

[13] 48 C.F.R. § 19.704.

[14] *See, e.g., FirstLine Transp. Sec., Inc., v. United States*, 12-601C, 2012 WL 5939228 (Fed. Cl. Nov. 19, 2012) (Court of Federal Claims denied a pre-award protest challenging a solicitation's small business subcontracting goal of 40% of the total contract value, holding that this goal was within the high level of discretion afforded to the agency.).

[15] 48 C.F.R. § 19.705-4.

[16] 15 U.S.C. § 644(g)(1).

[17] HUBZone are defined as any area located in a qualified census tract, qualified nonmetropolitan county, within the external boundaries of an Indian reservation or an area subject to the Base Realignment and Closure Act (BRAC). 15 U.S.C. § 632(p). Qualified census tracts are tracts designated by the Department of Housing and Urban Development (HUD) in which either 50 percent or more of the households have an income which is less than 60 percent of the area median gross income for such year or which has a poverty rate of at least 25 percent, but no more than 20 percent of a metropolitan statistical area may qualify. 26 U.S.C. § 42(d)(5)(B)(ii). Qualified nonmetropolitan counties are those in which median household income is at less than 80 percent of the nonmetropolitan State median household income, the unemployment rate at least 140 percent of the average unemployment rate for the United States or for the State in which such county is located, whichever is less, or which is located in a difficult development area, as designated by HUD. 15 U.S.C. § 632(p).

[18] 15 U.S.C. § 632(p)(5).

[19] 48 C.F.R. § 19.1305-1307.

[20] *Id.*

[21] *Id.*

[22] 13 C.F.R. § 126.300.

[23] *Id.* at § 126.401.

[24] *Id.* at § 121.1001.

[25] SBA, the KO, or any other interested party may protest the apparent successful offeror's qualified HUBZone SBC status. 13 C.F.R. § 126.801.

awarding three percent of all prime contract dollars and three percent of all subcontract dollars to HUBZone firms.[26]

C. The Small Disadvantaged Business (SDB) and the 8(a) Business Development (8(a)) Programs.

SDBs are small businesses at least 51 percent unconditionally owned by one or more socially and economically disadvantaged individuals.[27] Social disadvantage is presumed for members of designated groups, or may be established by a preponderance of the evidence for any other individual.[28] Economic disadvantage is defined as a net worth of less than $750,000, after excluding the value of the individual's ownership interest the small business and the value of the individual's equity in a primary personal residence.[29] A firm certifies as an SDB to either the procuring agency or to a third-party certifier, although all 8(a) firms are automatically considered SDBs.[30] There is a statutory goal of awarding five percent of all prime contract and five percent of all subcontract dollars to SDBs. [31]

The 8(a) program is an important subset of the SDB program. 8(a) firms are small businesses owned and controlled by socially and economically disadvantaged individuals who have applied for and been accepted into a nine-year business development program at SBA.[32] While the definition of social disadvantage is the same in the 8(a) program as it is in the SDB program, the definition of economic disadvantage is much stricter, with a $250,000 cap on assets outside of the business and primary residence, and a requirement that the individual demonstrate a limited access to capital.[33] Participation in the 8(a) program provides important contracting preferences – sole-source contracts up to $4 million ($6.5 million for manufacturing contracts) are the preferred contracting method, although competitive 8(a) awards are allowed with the permission of the SBA.[34]

In the 8(a) program, SBA is considered the prime contractor, and the 8(a) firm is its subcontractor, which requires agencies to negotiate awards with SBA.[35] However, since the 1990s, SBA has been entering into Memorandums of Understanding (MOUs) with agencies, allowing agencies to bypass SBA and award contracts directly to the 8(a) firms.[36] The 8(a)

[26] 15 U.S.C. § 644(g)(1).
[27] 13 C.F.R. § 124.1002.
[28] There is a rebuttable presumption that "Black Americans; Hispanic Americans; Native Americans (American Indians, Eskimos, Aleuts, or Native Hawaiians); Asian Pacific Americans (persons with origins from Burma, Thailand, Malaysia, Indonesia, Singapore, Brunei, Japan, China (including Hong Kong), Taiwan, Laos, Cambodia (Kampuchea), Vietnam, Korea, The Philippines, U.S. Trust Territory of the Pacific Islands (Republic of Palau), Republic of the Marshall Islands, Federated States of Micronesia, the Commonwealth of the Northern Mariana Islands, Guam, Samoa, Macao, Fiji, Tonga, Kiribati, Tuvalu, or Nauru); Subcontinent Asian Americans (persons with origins from India, Pakistan, Bangladesh, Sri Lanka, Bhutan, the Maldives Islands or Nepal)" are socially disadvantaged. 13 C.F.R. § 124.103.
[29] 13 C.F.R. § 124.1002(c).
[30] *Id.* at § 124.1003.
[31] 15 U.S.C. § 644(g)(1).
[32] 13 C.F.R. § 124.
[33] *Id.* at § 124.104.
[34] *Id.* at § 124.506.
[35] 15 U.S.C. § 637(a).
[36] 13 C.F.R. § 124.508.

certification is processed by SBA, and annual reviews are required throughout the nine years of program participation to ensure a firm's continued eligibility.[37]

Small business concerns owned by Indian Tribes (ITs) and Alaska Native Corporations (ANCs) may qualify for a modified version of the 8(a) program. ITs and ANCs are not required to be involved in the day-to-day management of the participant.[38] ANCs are presumed economically disadvantaged, whereas ITs look at the economic status of the tribe as a whole is consdered and different thresholds apply.[39] In neither case is the size of other concerns owned by the ANC or IT considered when determining if the firm is small, and ANCs and ITs may have multiple subsidiaries participating in the 8(a) program at the same time. Perhaps the most important distinction is that ANCs and ITs are not subject to any caps on the size of sole-source contracts, although there is a proposed regulation to require that KOs justify sole-source awards above $20 million.[40]

Unlike the HUBZone or small business programs, the eligibility of an 8(a) participant cannot be challenged by another 8(a) firm or any other party.[41] Instead, all OHA protests must focus on whether the firm is indeed a small business, and the protest may only be brought when the contract in question is a set-aside contract rather than a sole source award.[42]

D. <u>The Women-Owned Small Business (WOSB) and Economically Disadvantaged Women-Owned Small Business (EDWOSB) Programs.</u>

WOSB are small businesses that are at least 51 percent owned and controlled by women who are United States citizens.[43] EDWOSBs must meet the same eligibility requirements, and demonstrate that they have a personal net worth of less than $750,000, exclusive of a primary residence, the ownership share in the business, and any retirement accounts that have penalties for early withdrawal.[44] To certify as a WOSB or EDWOSB, the firm must register and certify as such in SAM, and provide the KO with supporting documents .[45] Additionally, the firm must either be certified by an SBA-approved third party certifier or provide supporting documentation to the Program Repository.[46] Contracts may be set aside for EDWOSBs if: (1) the contract requirement is in an industry designated by SBA as one where WOSBs are underrepresented; (2) two or more EDWOSBs will submit offers for the contract; and (3) award of the contract may be made at a fair and reasonable price that is less than $5 million if the contract is for

---

[37] *Id.* at § 124.201, 124.601.
[38] *Id.* at § 124.109.
[39] *Id.*
[40] Federal Acquisition Regulation; Justification and Approval of Sole-Source 8(a) Contracts, 76 Fed. Reg. 14,559 (Mar. 16, 2011) (to be codified at 48 C.F.R. § 6, § 8, and § 19).
[41] 13 C.F.R. § 124.517.
[42] *Id.*
[43] *Id.* at § 127.200.
[44] *Id.* at § 127.203.
[45] *Id.* at § 127.300. The supporting documents include (1) proof of citizenship; (2) joint venture agreements; (3) Articles of Organization and operating agreements for Limited Liability Companies; (4) Articles of Incorporation, By-Laws, stock certificates, stock ledger and voting agreements for corporations; (5) for partnerships, the partnership agreement and any amendments; (6) any assumed/fictitious name certificate(s); (7) a signed copy WOSB/EDWOSB program certification; and (8) for EDWOSBs, personal financial statements.
[46] *Id.*

manufacturing, or less than $3 million in all other cases.[47] This third requirement was removed by the National Defense Authorization Act of 2013, but will continue to apply until such time as the SBA and the Federal Acquisition Council issue new regulations.[48] Contracts may be set aside for WOSBs in the same manner, except that the contract requirement must be for an industry designated by SBA as one where WOSBs are substantially underrepresented.[49] Status as an EDVOSB or a WOSB may be protested by another EDVOSB or WOSB bidding on a specific requirement, by the KO, or by SBA.[50] There is a statutory goal of awarding five percent of all prime contract dollars and five percent of all subcontract dollars to WOSBs.[51]

E. The Service-Disabled Veteran-Owned Small Business (SDVOSB) Program.

SDVOSBs are small businesses that are at least 51 percent owned and controlled by service-disabled veterans, or the spouse or caregiver of a service-disabled veteran with a permanent and severe disability.[52] Contracts may be set aside for SDVOSB if there are two or more SDVOSBs who will submit offers and the award can be made at a fair and reasonable price.[53] SDVOSB may receive sole-source contracts if there is only one SDBVOSB who can meet the requirements at a fair and reasonable price, and the contract will not exceed $6 million for a manufacturing contract or $3.5 million for any other contract.[54] For purposes of contracting with any agency other than the Department of Veterans Affairs (VA), a concern must self-certify its status in SAM, and is subject to protest by other interested parties, the KO, or the SBA.[55] If the firm wishes to contract with VA, it must have its eligibility verified by VA.[56] There is a statutory goal of awarding three percent of all prime contract dollars and three percent of all subcontract dollars to SDVOSBs.[57]

---

[47] *Id.* at § 127.503(a).
[48] Pub. L. No. 112-238 § 1697, __ Stat. ___ at ___ (2013).
[49] *Id.* at. § 127.503(b).
[50] *Id.* at § 121.1001(a)(9).
[51] 15 U.S.C. § 644(g)(1).
[52] 13 C.F.R. § 1215.8.
[53] 48 C.F.R. § 19.1405(b).
[54] *Id.* at § 19.1406(a).
[55] 13 C.F.R. § 125.25.
[56] 38 C.F.R. § 74. Interestingly, this has led to cases where VA and SBA have conflicting determinations regarding who controls the business.
[57] 15 U.S.C. § 644(g)(1).