



U.S. Small Business
Administration



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SBA's Small Business Limitations on Subcontracting

Not intended for public distribution

Hosts

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Welcome to “SBA Virtual Learning 2023”

1. Questions answered during the final 10 minutes.
2. Technical problems: Contact your IT admin who manages Teams settings for your organization.
3. Captioning available for this presentation.
4. We cover the “**SBA Quick Reference**” as time allows.
5. For more SBA training visit the SBA Learning Center website <https://www.sba.gov/tools/sba-learning-center/search/training>

Important Announcements

May 1, 2024, First Wednesday

- SBA Learning Series Schedule Revisions
- SBA Learning Series Session 8, scheduled for May 1, 2024, is tentatively revised to Thursday, May 9, 2024, due to a competing scheduled event.

July 3, 2024, First Wednesday

- The July 3 session of First Wednesday is moved to Thursday, July 11, 2024
- This is due to First Wednesday proximity to July 4, 2024 (The Fourth of July Holiday)

The APEX Accelerator Program

The APEX Accelerators are a vital resource partner.

- The APEX Accelerators posts past “First Wednesday” programming at this link: <http://www.aptac-us.org/for-contracting-officers-sba-webinar-library/>
- Contracting Officer Resources: “How APEX Accelerators partner with federal agencies”: <http://www.aptac-us.org/federal-partners/>
- Find your nearest APEX Accelerators/Procurement Technical Assistance Center at <http://www.aptac-us.org>
- APEX Accelerator Information at <https://www.apexaccelerators.us/#/>

Small Business Administration YouTube Page

SBA YouTube page posts past “First Wednesday” programming at links below.

FY2023

- October 5, 2022 – 8(a) Business Development Program Updates: <https://youtu.be/Yl5Sp0dP1aE>
- November 2, 2022 – Surety Bond Guarantee Program: <https://youtu.be/QlZJiMLcc5o>
- December 7, 2022 – Subcontracting Program: <https://youtu.be/gMaaeGl8CBs>
- January 4, 2023 – Surveillance Review Program: <https://youtu.be/euUX4Jv6kRI>
- February 1, 2023 – HUBZone Program: <https://youtu.be/YGnS8e6idCc>
- March 1, 2023 – The Mentor Protégé Program: <https://youtu.be/A9KbCm4FP1c>
- April 5, 2023 – Non-Manufacture Rule (NMR): <https://youtu.be/AqwYMWoe9f0>
- May 3, 2023 – Size Program: https://youtu.be/45WZ_oPb1GY
- Jun 7, 2023 – Legislature and Regulatory Updates: <https://youtu.be/ljx9lajQJNY>
- July 5, 2023 – Market Research: [SBA First Wednesday Market Research - July 13, 2023](https://youtu.be/SBA_First_Wednesday_Market_Research_-_July_13,_2023)
- August 2, 2023 – Service-Disabled Veteran Owned Program (SDVOSB): <https://youtu.be/QxcxJISRhnw>


FY2024

- October 4, 2023 - Certificate Of Competency: <https://youtu.be/VDZ-uuCLIWw>
- November 1, 2023 - 8(a) Program Updates: <https://youtu.be/6fN3dK0EShs>
- December 6, 2023: <https://youtu.be/sa29iONBtfk>
- January 3, 2024 - Compliance Reviews: https://youtu.be/WmZn_oa13-o

FIRST WEDNESDAY VIRTUAL LEARNING SERIES

FY 2024 SCHEDULE

1:00 to 2:00 PM Central Time

FY 2024	Date	Topic
1	October 4, 2023	COC
2	November 1, 2023	8(a) Program Updates
3	December 6, 2023	The Timber Program and SBA POCs
4	January 3, 2024	Compliance Reviews
 5	February 7, 2024	Limitations on Subcontracting
6	March 6, 2024	SBA Mentor Protégé Program and Joint Ventures
7	April 3, 2024	Women Owned Small Business (WOSB)
8	*May 9, 2024	Participation Plans versus Subcontracting Plans
9	June 5, 2024	Legislative Updates
10	*July 11, 2024	HUBZone
11	August 7, 2024	Market Research

* Schedule Revision Due to Holiday or Conflict

The program schedule is for information only and is subject to change.

One Continuous Learning Point

- Self-service process for one CLP of credit: Many of you want to receive credit for today's training. You will be glad to know that today's training is worth one CLP. The slide presentation will include the training certificate on Slide 10. Fill, download the training certificate, copy and submit it through regular channels.
- If you listen in groups and you want all attendees to be included on the future mailing list, send email addresses of participants in an excel document to sbalearning@sba.gov.

“SBA 1st Wednesday Virtual Learning 2024”

This Certificate is awarded to

Insert Your Name Here

For completion of

Limitations On Subcontracting

This training seminar may be credited towards “Continuous Learning Points” as described in OFPP Policy Letter 05-01. Recommendation of One CLP.



Pamela J. Beavers
Director, Area IV
SBA Office of Government Contracting

02/07/2024

DATE

Today's Speakers

Michael Cecere
Deputy Area Director
Office of Government Contracting, Area I
U.S. Small Business Administration



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Administration



The Limitations on Subcontracting Requirement

1st Wednesday Training
February 7, 2024

Limitations on Subcontracting (LOS) Background

- Many years ago there was no percentage of work requirement in a SB set-aside. SBs had to perform a significant portion of the work.
- When the percentage of work requirements came about, it required the SB prime contractor to perform a minimum percentage of the work, with specific percentages for contracts for supplies, services, special trade construction and general construction.
- Beginning in late 2018, some agencies (e.g., DOD, GSA, VA) issued a class deviation to the FAR based on an SBA regulation effective June 30, 2016 (implementing the NDAA of 2013), that significantly changed the LOS requirement in that the SB could not exceed subcontracting a certain percentage of the contract to any subcontractor that was not a similarly situated entity. The FAR was eventually revised to reflect this change in September 2021.

LOS Applicability

- **SB Set-aside contracts and orders above the SAT**
 - **Applies to partial set-asides where requirement is divided into distinct portions**
- **Sole source or competitive 8(a) strategy (any dollar value)**
- **Sole source or competitive HUBZone SB strategy (any dollar value)**
 - **Also applies where award is based on HUBZone price evaluation preference**
- **Sole source or competitive SDVOSB strategy (any dollar value)**
- **Sole source or competitive WOSB/EDWOSB strategy (any dollar value)**

LOS Applicability cont'd

- The LOS does not apply to:
 - F&OC actions
 - SB reserves at the contract level, but does apply to subsequent orders that are set aside
 - Sole source SB actions using an authority unrelated to FAR Part 19, e.g., establishing or maintaining an alternative source; only one responsible source; urgency; industrial mobilization; international agreement; etc.

The LOS is an Element of Responsibility

- **Upon determining and documenting that an apparently successful SB offeror lacks certain elements of responsibility, including compliance with the LOS, the CO must withhold award and refer the matter to SBA IAW the Certificate of Competency (COC) procedures in FAR subpart 19.6.**
- **A small business that has not agreed to comply with the limitations on subcontracting may be considered nonresponsive. For example, the offeror did not comply with a solicitation requirement that it furnish a formal signed certification with its bid, quotation or proposal that it will comply with the LOS requirement (this is a current VA regulation).**

What is a Similarly Situated Entity (SSE)?

- **Similarly situated entity means a first-tier subcontractor, including an independent contractor, that—**
 - (1) Has the same small business program status as that which qualified the prime contractor for the award; and**
 - (2) Is considered small for the size standard under the NAICS code the prime contractor assigned to the subcontract.**
- **Example: A SDVOSB is awarded a prime contract that was solicited as a 100% SB set-aside. To qualify as a similarly situated entity on this contract, a first-tier subcontractor need only be a SB, not a SDVOSB, because the solicitation was a SB set-aside, not a SDVOSB set-aside.**

Other Notes

- **SBA will exclude a subcontract to a similarly situated entity from consideration under the ostensible subcontractor rule.**
- **A prime contractor may no longer count a similarly situated entity towards compliance with the limitations on subcontracting where the subcontractor ceases to qualify as small or under the relevant socioeconomic status. [not necessarily immediate – see size/status regs]**
- **Any work that a similarly situated entity does not perform with its own employees shall be considered subcontracted.**

What is the Percentage Limitation for Services (except construction)?

- **The SB prime contractor will not pay more than 50% of the amount paid by the government to it to firms that are not similarly situated. Any work that a similarly situated subcontractor further subcontracts will count towards the 50% subcontract amount that cannot be exceeded.**
- **Cost of materials are excluded and not considered to be subcontracted.**
- **Other direct costs may be excluded to the extent they are not the principal purpose of the acquisition and small business concerns do not provide the service, such as airline travel, work performed by a transportation or disposal entity for environmental remediation, cloud computing services, mass media purchases or certain work performed overseas.**
- **Example: A \$5M contract is assigned a services NAICS code. The cost of materials is \$1M. Excluding the cost of materials, the work requirement is \$4M, so the prime may not subcontract more than \$2M (50%) to non-similarly situated entities, and the prime and/or similarly situated entities must perform at least \$2M (50%).**

What is the Percentage Limitation for Supplies or Products (other than from a nonmanufacturer of such supplies)?

- **The SB prime contractor will not pay more than 50% of the amount paid by the government to it to firms that are not similarly situated. Any work that a similarly situated subcontractor further subcontracts will count towards the 50% subcontract amount that cannot be exceeded.**
- **Cost of materials are excluded and not considered to be subcontracted.**
- **Example: A \$4M contract is assigned a supply NAICS code. The cost of materials is \$1M. Excluding the cost of materials, the work requirement is \$3M, so the prime may not subcontract more than \$1.5M (50%) to non-similarly situated entities, and the prime and/or similarly situated entities must perform at least \$1.5M (50%).**

The Nonmanufacturer Rule (NMR) for Supplies

- **The LOS clause provides that a nonmanufacturer of supplies may provide the product of any SB manufacturer. The similarly situated entity concept does not apply to the NMR. For example, on a supply contract set aside for SDVOSB, a SDVOSB that is a nonmanufacturer can provide the product of any SB.**
- **Conditions: SB cannot exceed 500 employees; must be primarily engaged in retail or wholesale and normally sells type of product being supplied; must take ownership or possession of the item(s) in a manner consistent with industry practice; and must supply the end product of a small business manufacturer or processor made in U.S.**
- **If there is a class waiver to the NMR or the CO obtains an individual waiver to the NMR, a SB can provide the product of a LB on any type of set-aside and the LOS requirement does not apply.**

What are the Percentage Limitations for Construction?

- **For general construction, the SB prime contractor will not pay more than 85% of the amount paid by the government to it to firms that are not similarly situated. Any work that a similarly situated subcontractor further subcontracts will count towards the 85% subcontract amount that cannot be exceeded.**
- **For a contract involving special trade contractors, the applicable percentage is 75%.**
- **Cost of materials are excluded and not considered to be subcontracted.**
- **Example: A \$10M contract with a \$2M services portion is assigned a general construction NAICS code. The cost of materials is \$1M. Excluding the services and cost of materials, the work requirement is \$7M, so the prime may not subcontract more than \$5.95M (85%) to non-similarly situated entities, and the prime and/or similarly situated entities must perform at least \$1.05M (15%).**

Mixed Contracts

- **Where a contract integrates any combination of services, supplies or construction, the CO shall select the appropriate NAICS code which then determines which LOS requirement applies. The relevant LOS requirement will apply only to that portion of the contract award amount. In no case shall more than one limitation on subcontracting requirement apply to the same contract.**
- **Example: A \$3M contract with a \$2.5M supply portion and a \$500K services portion is assigned a supply NAICS code. The cost of materials is \$500K. Excluding the services and cost of materials, the work requirement is \$2M, so the prime may not subcontract more than \$1M (50%) to non-similarly situated entities, and the prime and/or similarly situated entities must perform at least \$1M (50%) .**

Joint Ventures

- **A joint venture agrees that, in the performance of the contract, the applicable percentage specified in the clause will be performed by the aggregate of the joint venture participants and any similarly situated entities.**
- **In an 8(a), HUBZone SB, SDVOSB or WOSB joint venture or a joint venture comprised of a small business protégé and its mentor approved by the SBA, the SB participants or small business protégé shall perform at least 40 percent of the work performed by the joint venture. Work performed by the SB participants or the small business protégé in the joint venture must be more than administrative functions.**

Compliance Period

- **For contracts that are awarded under any FAR Part 19 SB Program, the default period is generally by the end of the base term and then by the end of each subsequent option period unless the CO specifically requires compliance at the end of each order issued under the contract.**
- **However, for a multi-agency set-aside contract where more than one agency can issue orders under the contract, the ordering agency must use the period of performance for each order to determine compliance. [new SBA regulation effective May 30, 2023]**
- **For orders that are awarded under any FAR Part 19 SB Program where the base contract is not set aside, the SB must be compliant by the end of the performance period for the order.**

Determining Compliance with the LOS

- **FAR 1.602-2 states that Contracting Officers are responsible for ensuring performance of all necessary actions for effective contracting, including compliance with the terms and conditions of the contract.**
- **Specifically addressed in SBA 8(a) Partnership Agreements.**
- **Paragraph (e) of FAR clause 52.219-14, Limitations on Subcontracting stipulates, by submission of an offer and execution of a contract, the contractor agrees that in performance of a contract it will comply with the limitations on subcontracting set forth in the clause.**

Issues Regarding Monitoring LOS Compliance

- The FAR does not currently include specific procedures for contracting personnel to track and monitor a SB prime contractor's compliance with the LOS.
- Recent reports and findings:
 - DOD IG Audit of Department of Defense Small Business Subcontracting Requirements (DODIG-2022-069), dated 7 March 2022, reported that CO actions to ensure compliance with the LOS requirements were not effective.
 - SBA surveillance reviews of federal contracting activities reveal that COs were not always monitoring contractor compliance with the LOS.
 - Internal Program Management Reviews also reveal that COs were not adequately monitoring the LOS requirement.

Issues Regarding Monitoring LOS Compliance cont'd

- **Relying on an offeror's signed proposal that they will comply with the LOS requirement is rather weak. Contracting activities should develop a minimal process/standard procedure to ensure monitoring and compliance of SB subcontracting requirements.**
- **SBA regulations clarify that COs may, at their discretion, require the contractor to demonstrate its compliance with the LOS at any time during performance and upon completion of a contract if the information regarding such compliance is not already available to the CO. Evidence of compliance includes, but is not limited to, invoices, copies of subcontracts, or a list of the value of tasks performed.**
- **Although COs are not required to request evidence of compliance, they should take positive action to determine whether or not a contractor complied with the LOS requirement.**

Benefits

- **According to the U.S. Army Corps of Engineers, an effective LOS monitoring program will achieve multiple objectives. Ensuring SB compliance will:**
 - **promote a level-playing field and support the integrity of the SB program**
 - **continue to grow, develop and maintain a competent SB industrial base to meet the government's requirements**

Past Performance Evaluation

- **New SBA regulation effective May 30, 2023, requires the CO to determine at conclusion of contract/order performance whether the SB satisfied the LOS requirement. If not compliant, CO must provide SB the opportunity to explain extenuating circumstances and determine whether or not the mitigating factors were beyond the control of the SB.**
- **Where a small business does not provide any extenuating or mitigating circumstances or the agency determines that the concern's failure to meet the applicable LOS requirement was not beyond the concern's control, the agency may not give a satisfactory or higher past performance rating for the appropriate factor or subfactor in accordance with FAR 42.1503.**
- **Where a contracting officer determines that extenuating circumstances warrant a satisfactory/positive past performance evaluation for the appropriate evaluation factor or subfactor and the individual at least one level above the CO concurs with that determination, a satisfactory or higher past performance rating may be given.**

Past Performance Evaluation cont'd

Extenuating or mitigating circumstances that could lead to a satisfactory/positive rating include, but are not limited to, unforeseen labor shortages, modifications to the contract's scope of work which were requested or directed by the Government, emergency or rapid response requirements that demand immediate subcontracting actions by the prime small business concern, unexpected changes to a subcontractor's designation as a similarly situated entity, differing site or environmental conditions which arose during the course of performance, force majeure events, and the contractor's good faith reliance upon a similarly situated subcontractor's representation of size or relevant socioeconomic status.

An agency cannot rely on any circumstances that were within the contractor's control, or those which could have been mitigated without imposing an undue cost or burden on the contractor.

Some Best Practices to Consider*

- **Require offerors to acknowledge the LOS requirement with offer**
- **Address offeror's ability to comply with LOS in your responsibility determination**
- **Include the LOS requirement in your post-award meeting agenda**
- **Include a special contract report deliverable**
- **Use a LOS calculations template**
- **COR/ACO check construction payrolls and provide report to the CO regarding amount paid to subcontractors**

*** reference VA regulations and U.S. Army Corps of Engineers guidance**

Noncompliance

- **Civil/criminal penalties (15 USC 645(d)), including:**
 - **Fines – the greater of \$500,000 or amount expended on subcontractors in excess of allowed amount**
 - **Suspension and debarment**
 - **Imprisonment up to 10 years**

Thank You for Your Support of Small Business!

