

# SBA rule allows small business subcontracting plans to take credit for lower-tier subcontractors

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On Oct. 11, 2023, the Small Business Administration (SBA) issued a final rule revising its regulations to implement changes resulting from § 870 of the National Defense Authorization Act of 2020.<sup>1</sup> The rule permits prime contractors with individual subcontracting plans applicable to a sole contract with a single federal agency, to receive credit for subcontracts to small businesses at lower tiers.

To streamline the process, prime contractors will incorporate lower-tier subcontracting performance into their overall subcontracting-plan goals.

## Background

Federal contracts exceeding \$750,000 — or \$1.5 million for construction — require the awardee to have a small business subcontracting plan, which includes percentage goals for using small businesses and subcategories of small businesses as subcontractors in the performance of the contract.

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Awardees are only exempt from this requirement if the awardee is a small business, the contract does not offer subcontracting opportunities, or the contract will be performed entirely outside the United States and its outlying areas.

This topic has undergone several changes in the past decade. Prior to 2016, the SBA permitted a prime contractor to count only its first-tier subcontracts toward its subcontracting plan goals. In December of 2016, the SBA published a final rule mandating that prime contractors receive credit for lower-tier subcontracts when certain criteria are met. This 2023 final rule implements changes and departs from the 2016 rule in various ways.

## Changes

First, the rule changes the threshold for a required subcontracting plan. The threshold at 13 CFR § 125.3(a) will increase from \$650,000 to \$750,000, resolving inconsistencies between it and FAR 52.219-9, Small Business Subcontracting Plan.

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The main focal point of the rule, however, is the change that allows prime contractors to elect whether to receive credit toward their subcontracting plans for lower-tier subcontracts to small businesses when the subcontracting plan applies to a single contract with one federal agency.

Contractors with commercial plans, comprehensive subcontracting plans, plans that apply to multiple contracts, plans that apply to single contracts with multiple agencies, government-wide contracts, and multi-agency contracts may not use lower-tier subcontracts. Instead, contractors with those types of plans must rely solely on first-tier subcontracts to meet their subcontracting goals.

The rule does not require prime contractors to submit additional reports. Lower-tier awards will be reported by the subcontractors that award them; prime contractors who elect to use lower-tier subcontracts in meeting their plan goals will only be responsible for reporting their own first-tier awards.

Further, the rule prohibits agencies from setting tier-specific goals for prime contractors. Prime contractors may only have one set of goals, which includes both first- and lower-tier subcontracts. This is a departure from the previous rule, which required two sets of subcontracting goals.

Lastly, the rule implements a new recordkeeping requirement. Prime contractors must now maintain records of the procedures

they used to substantiate the credit they elect to receive for any lower-tier subcontracting.

### Implications for contractors

The applicability of the rule is very limited. For example, contractors pursuing a single contract that applies to more than one military department would not be able to take advantage of these changes because each military department is considered a separate federal agency for the purposes of the rule.

Still, the rule resolves inconsistencies and simplifies the process for prime contractors electing to receive credit toward their goals

when using lower-tier subcontracts. The elective nature of the rule allows eligible prime contractors to consider their business needs when determining whether to take credit for lower-tier subcontracts. Various supporters of the rule believe it will increase small business participation in federal government contracting.

The final rule was effective Nov. 13, 2023, but the Federal Acquisition Regulation (FAR) Council's lag behind SBA's rule changes will likely extend the time period for regulatory consistency between the rule and the FAR on lower tier subcontracting rules.

### Notes

<sup>1</sup> 3 CFR 125.3

### About the author



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