August 23, 2019

Via Regulatory Portal

Mr. Khem R. Sharma
U.S. Small Business Administration
Chief, Office of Size Standards
409 Third Street SW, 8th Floor
Washington, DC 20416

Re: Comments on SBA Proposed Rule, Small Business Size Standards:
Calculation of Annual Receipts, 84 Fed. Reg. 29,399 (June 24, 2019);
RIN 3245-AH16

Dear Mr. Sharma,

On behalf of the American Bar Association (“ABA”) Section of Public Contract Law (“Section”), I am submitting comments on the proposed rule cited above. The Section consists of attorneys and associated professionals in private practice, industry, and government service. The Section’s governing Council and substantive committees include members representing these three segments to ensure that all points of view are considered. By presenting their consensus view, the Section seeks to improve the process of public contracting for needed supplies, services, and public works.

The views expressed herein are presented on behalf of the Section. They have not been approved by the House of Delegates or the Board of Governors of the ABA and, therefore, should not be construed as representing the position of the ABA.

Mary Ellen Coster Williams, Section Delegate to the ABA House of Delegates, and Scott Flesch and Douglas Mickle, members of the Section’s Council, did not participate in the Section’s consideration of these comments and abstained from the voting to approve and send this letter.

This letter is available in pdf format at http://www.americanbar.org/groups/public_contract_law/resources/prior_section_comments.html under the topic “Small Business and Socioeconomic Issues.”
I. BRIEF SUMMARY OF THE PROPOSED ANNUAL RECEIPTS RULE

The Small Business Runway Extension Act of 2018 ("SBREA") amended the Small Business Act by changing the requirements for small business size standards prescribed by agencies without their own statutory authority to issue size standards. Under 15 U.S.C. § 632(a)(2)(C), as amended, the following requirements now apply:

Requirements. Unless specifically authorized by statute, no Federal department or agency may prescribe a size standard for categorizing a business concern as a small business concern, unless such proposed size standard—

(i) is proposed after an opportunity for public notice and comment;

(ii) provides for determining—

(I) the size of a manufacturing concern as measured by the manufacturing concern’s average employment based upon employment during each of the manufacturing concern’s pay periods for the preceding 12 months;

(II) the size of a business concern providing services on the basis of the annual average gross receipts of the business concern over a period of not less than 5 years;

(III) the size of other business concerns on the basis of data over a period of not less than 3 years; or

(IV) other appropriate factors; and

(iii) is approved by the [SBA] Administrator.

According to the Small Business Administration ("SBA"), the agency is not subject to the amendments to Section 632(a)(2)(C) because SBA has its own statutory authority to prescribe size standards. Nevertheless, to promote government-wide consistency and avoid confusion, the proposed rule would change SBA’s size standards by adopting a 5-year averaging period for calculating annual average receipts for all receipts-based size standards.

In addition, the proposed rule contains changes intended to clarify how SBA calculates annual receipts in connection with the acquisition or sale of a division of a concern.

Specifically, the proposed rule would provide that the annual receipts of a concern would not be adjusted where the concern sells or acquires a segregable division during the applicable period of measurement or before the date on which it self-certified as small. This would be different from how SBA treats the sale or acquisition of a subsidiary. In the case of a subsidiary, SBA’s regulations provide that “[t]he annual receipts of a former affiliate are not included if affiliation ceased before the date used for determining size. This exclusion of annual receipts of a former affiliate applies during the entire period of measurement, rather than only for the period after which affiliation ceased.” 13 CFR 121.104(d)(4).
II. COMMENTS

The Section is pleased to offer comments on SBA’s proposed rule for calculating annual receipts. The Section believes that the Proposed Rule should be implemented quickly to provide certainty to the contractor community with respect to size status.

A. Section’s Response to Specific SBA Requests for Comments.

1. The Section supports applying the 5-year lookback average to all industries subject to receipts-based size standards.

SBA requested feedback, along with supporting facts and analyses, on whether the Agency should calculate annual average receipts over 5 years for all industries subject to receipts-based size standards or on whether it should use a 5-year annual receipts average for businesses in services industries only and continue using a 3-year annual average for other businesses. SBA is concerned that the latter option may create confusion both for businesses in reporting their size based on annual average receipts and for contracting personnel in verifying the size of bidders to federal contracts.

The Section supports SBA’s intent to apply the same rule—the 5-year lookback average—to all industries subject to receipts-based size standards. The Section concurs with SBA’s concern that using different formulas for calculating size in different industries could create confusion. Also, using different formulas could incentivize NAICS appeals as contractors jockey for a code that not only uses their preferred size standard, but also their preferred number of years in the calculation of size.

While the Section understands that the “mid-tier desert” problem, which Congress cited as one reason for passing the SBREA, appears to be more acutely affecting services industries than other industries, the Section is not aware of any data showing that problem does not exist within the retail trade or construction industries, for example.

Thus, the Section supports uniformity in size calculation methodology, and is not aware of any compelling rationale for not expanding application of the 5-year lookback to all receipts-based size standards.

2. The Section supports continued monitoring with respect to how the 5-year lookback impacts smaller and larger small businesses.

SBA invited input on how the use of annual average receipts over 5 years instead of 3 years would impact both smaller small businesses and more advanced (larger) small businesses in terms of getting access to federal opportunities for small businesses.

The Section recognizes that SBA’s own data, as presented in the proposed rule, appears to show that the change to a 5-year lookback will arguably benefit (i.e., keep small) more than 7% of small firms, while arguably harming (i.e., keeping large) less than 1%. The Section observes that a rule leaving a 7 to 1 rate of return, so to speak, might be reasonably viewed as benefiting the
small-business community as a whole. The Section also observes that, to the extent the change in formula does ameliorate the perceived “mid-tier desert” problem highlighted by Congress, that improvement would help not only smaller firms but also the procurement system as a whole. Government customers and large businesses should be able to maintain relationships with trusted small-business suppliers for longer (and continue to receive small-business credit for doing so), and small businesses should become more competitive with the largest firms in the country, potentially fostering greater price competition and innovation at the top of the market.

However, in any case, the Section recommends that SBA closely monitor whether the rule achieves the above objectives, or those stated by Congress in passing the SBREA. For example, SBA should monitor increases or decreases in the number of mid-tier firms participating in the federal contracts marketplace, year over year, in order to assess the proposed rule’s impact.

3. The Section supports SBA’s proposed clarification to require the sale or acquisition of an actual subsidiary before allowing a contractor to utilize the former affiliate rule.

SBA is changing its receipts calculation rules to distinguish between the sale of a division from that of a subsidiary. SBA specifically requested comments on this issue.

The Section supports SBA’s clarification because it provides clarity to the community with regard to the application of the former affiliate rule. The Section suggests that SBA expand the scope of this clarification to segregable divisions and “other assets not held as a separate legal entity,” to ensure that SBA’s clarification applies to the sale or purchase of non-segregable assets as well, e.g., when an entity acquires the assets performing a specific contract.

The Section appreciates the opportunity to provide these comments and is available to provide additional information or assistance as you may require.

Sincerely,
/s Linda Maramba
Chair, Section of Public Contract Law

cc: Susan Warshaw Ebner
Jennifer L. Dauer
Annejanette Heckman Pickens
Patricia H. Becker
Amy Conant Hoang
Council Members, Section of Public Contract Law
Chairs and Vice Chairs, Small Business & Other Socioeconomic Programs Committee
Craig Smith
Samantha S. Lee