SBA 8(a) Contractors Must Prepare To Reestablish Eligibility

By **Edward DeLisle and Andrés Vera** (August 29, 2023)

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On July 19, the U.S. District Court for the Eastern District of Tennessee issued an unprecedented decision with massive implications for the Small Business Administration's 8(a) Business Development Program.

In Ultima Services Corp. v. U.S. Department of Agriculture, the plaintiff challenged the constitutionality of the rebuttable presumption of social disadvantage afforded to individuals who are members of certain racial and ethnic groups.

The court ultimately agreed that the presumption is unconstitutional. The effect of this decision on current and future 8(a) program participants cannot be understated.

The SBA has already suspended new 8(a) program applications, and we believe all participating businesses that were certified based on this rebuttable presumption will soon need to reestablish their status as socially disadvantaged.

Rebuttable Presumption and Social Disadvantage Narratives

One of the primary requirements for participation in the 8(a) program is that the business must be owned and controlled by a socially and economically disadvantaged individual.[1]

The SBA defines socially disadvantaged individuals as "those who have been subjected to racial or ethnic prejudice or cultural bias within American society because of their identity as a member of a group without regard to their individual qualities" and that this disadvantage is a result of "circumstances beyond their control."[2]

Under Title 13 of the Code of Federal Regulations, Section 124.103(b)(1), members of certain racial and ethnic groups, including African Americans, Hispanic Americans, Native Americans, Asian Americans, Pacific Islander Americans and Subcontinent Asian Americans, are deemed to satisfy the socially disadvantaged requirement by use of a rebuttable presumption.

Thus, if a business owner is a member of one of those groups, they are not required to submit additional evidence of social disadvantage to successfully apply for the 8(a) program.

Owners who are not members of these racial and ethnic groups may qualify for the 8(a) program, but they must satisfy the social disadvantage requirement "by a preponderance of the evidence,"[3] which is generally accomplished by submitting a social disadvantage narrative along with corroborating evidence.

The narrative must include information to satisfy the following requirements: at least one objective distinguishing feature contributing to social disadvantage; the social disadvantage is rooted in treatment experienced in American society; the social disadvantage is chronic and substantial; and, most importantly, the social disadvantage negatively affected the owner's entry into or advancement in the business world.[4]

The SBA views these narratives quite critically, so they must be highly detailed and carefully constructed to ensure admission to the 8(a) program.

The Court's Decision

The plaintiff, Ultima Services, is a small business owned by a woman who is not a member of the racial and ethnic groups listed in Title 13 of the Code of Federal Regulations, Section 124.103(b)(1).

In 2017, Ultima was awarded four regional indefinite delivery, indefinite quantity contracts to provide services to the USDA. Each indefinite delivery, indefinite quantity contract included one base year with an option to renew annually over the four years following the base year.

But in 2018, the USDA informed Ultima that it was declining to exercise options under the indefinite delivery, indefinite quantity contracts and subsequently migrated the services Ultima was providing to contracts that were set aside for 8(a) program participants.

Ultima is not a participant in the 8(a) program, and thus was ineligible to compete for the award. To prevent this result, it filed a complaint alleging that the USDA and SBA engaged in racially discriminatory conduct in violation of its Fifth Amendment rights. Ultima alleged that the SBA's use of the 8(a) program's rebuttable presumption of social disadvantage discriminates on the basis of race.

In analyzing the alleged conduct, the court applied a strict scrutiny standard of review, meaning the use of the rebuttable presumption would be constitutional only if it is narrowly tailored and furthers a compelling governmental interest.

The court found that the rebuttable presumption does not serve a compelling government interest and is not narrowly tailored enough to survive the strict scrutiny standard.

Consequently, it held that the USDA and SBA violated Ultima's Fifth Amendment rights and enjoined the SBA from using the rebuttable presumption of social disadvantage in administering the 8(a) program.

Takeaways

In effect, this decision means that the SBA's rebuttable presumption of social disadvantage is unconstitutional and can no longer be used to qualify applicants for the 8(a) program. And because a business must maintain eligibility throughout its participation in the program, the prohibition on the rebuttal presumption is likely to be given retroactive effect.

Barring an appeal by the SBA, this will give rise to major changes in the 8(a) program application and annual review processes. It is also likely to result in protests challenging 8(a) set-aside awards on the basis that the awardee has not affirmatively established its owner's status as socially disadvantaged.

Most importantly, our expectation is that both applicants and current 8(a) program participants who satisfied the social disadvantage requirement by using the rebuttable presumption must reestablish that they are socially disadvantaged.

They will likely be required to submit social disadvantage narratives satisfying the requirements outlined above. While the SBA has yet to comment on the Ultima holding, we expect it to do so soon and that its response will be to require all 8(a) program participants to promptly submit these narratives and other evidence of social disadvantage.

Thus, we strongly recommend that all 8(a) program participants prepare a social disadvantage narrative and gather corroborating evidence as soon as possible.

The SBA's regulations set forth what is required as part of a social disadvantage narrative. Specifically, an 8(a) applicant must identify his or her personal experiences that demonstrate substantial and chronic prejudice or bias.[5]

The more specific an applicant can be, the better, because the regulations impose a "preponderance of the evidence" standard in evaluating whether the instances set forth in the narrative are sufficient to prove substantial, chronic prejudice or bias.[6]

The SBA will consider barriers experienced in accessing employment and/or business opportunities, among other things, as part of its assessment, and those barriers must be premised upon cultural, ethnic, racial, gender, handicap or residential prejudice of some kind.[7]

In terms of tying all this information together, it is important for the applicant to cite to corroborating evidence that shows how these prejudices manifested themselves and created barriers to employment, business opportunities and the like.

Given these regulatory-driven requirements, the multitude of them and the standard of review, this is not an easy endeavor. But, based upon the holding in Ultima, it may be a necessary one.

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[1] 13 CFR § 124.105.

[2] 13 CFR § 124.103(a).

[3] 13 CFR § 124.103(c)(1).

[4] 13 CFR § 124.103(c)(2).

[5] Id.

[6] 13 CFR § 124.103(c)(1).

[7] 13 CFR § 124.103(c)(2)(iv).