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Government Contracts Update

March 2025

Key Takeaways in SBA's Final Rule: HUBZone Program

Key Notes:

- SBA implements updates in its final rule to ensure that HUBZone program participants remain compliant with relevant regulations beyond initial certification.
- The final rule clarifies the definition of HUBZone "employee."

On December 17, 2024, the U.S. Small Business Administration (SBA) issued its highly anticipated final rule incorporating comments addressed and changes adopted from its proposed rule, "HUBZone Program Updates and Clarifications, and Clarifications to Other Small Business Programs," which we explored in a prior update. The final rule, which became effective on January 16, 2025, applies to existing contracts but will not be applied retroactively. In this second installment in our series of updates analyzing the final rule, we examine crucial changes to the Historically Underutilized Business Zone (HUBZone) Program.

HUBZone Contract Eligibility

In its proposed rule, SBA expressed concern that participants were not remaining fully compliant with the requirement for 35% of the firm's employees to reside in a HUBZone. Under the prior regulations, firms were required to meet the 35% residency requirement during the initial certification and annual recertification; however, SBA did not have measures in place to determine whether firms remained compliant throughout the year. Thus, as long as they received their annual certification, firms were able to submit offers on HUBZone set-asides even if they could not meet the 35% threshold or other program requirements. SBA noted that this structure created the potential for program abuses and did not align with the program's intended purpose.

To address this, the final rule mandates at 13 C.F.R. § 126.601(a) that a firm must comply with *all* HUBZone program requirements as of the date it submits an offer on a HUBZone contract. This aligns the HUBZone Program with the Women-Owned Small Business Program, 8(a) Program, and other SBA government contracting programs. With this change, a firm must be compliant at initial certification, recertification, and any time in between recertification when the firm plans to submit an offer on a HUBZone contract. However, for competitive HUBZone contracts, if a firm is eligible when it submits its offer but is no longer eligible when the award is made (e.g., if a HUBZone employee necessary for eligibility leaves the firm after the offer is submitted), then it remains eligible for the award. This is not the case for sole-source contracts where the firm must be HUBZone eligible at the time of the award.

Given the new requirement for a firm to be HUBZone eligible as of the date of an offer submission, SBA also proposed eliminating annual recertification and instead requiring recertification every three years. To the relief of HUBZone contractors, this proposed change was adopted in the final rule and is reflected at 13 C.F.R. § 126.500(a).

Attempt to Maintain 35% HUBZone Residency Requirement

SBA made several clarifications in the final rule regarding the "attempt to maintain" compliance with the 35% residency requirement. First, SBA provides that a firm must certify that it will attempt to maintain the 35% residency requirement at the time of an offer submission for a HUBZone contract, which was not required under the prior regulations.

Second, SBA clarifies that when a firm is actively performing a HUBZone contract, it must only demonstrate that it is attempting to meet the 35% residency requirement. A firm demonstrates this by "making substantive and documented efforts, such as written offers of employment, published advertisements seeking employees, and attendance at job fairs." 13 C.F.R. § 126.103. If a firm cannot make this demonstration, it fails to meet the requirement. Conversely, when a firm is not performing a HUBZone contract, the firm *must meet the 35% residency requirement*. Put another way, an attempt to maintain the residency requirement is not sufficient when a firm is not actively performing a HUBZone contract.

Finally, SBA adopted in the final rule a 12-month "grace period" after a contract award for program participants to meet the 35% residency requirement. As mentioned above, a firm can certify that it is attempting to maintain the residency requirement when performing a HUBZone contract. However, in SBA's view, if a firm is always performing a HUBZone contract, it essentially never has to demonstrate that it is meeting the residency requirement. To avoid this, SBA now offers firms a 12-month grace period after receiving a HUBZone contract to ensure enough employees are hired to remain compliant with the program regulations. Interestingly, this is not limited to a firm's first HUBZone award. So ostensibly, every HUBZone award triggers a new 12-month grace period. But once the grace period ends, a firm must meet the residency requirement.

HUBZone Employee Hours

SBA proposed doubling the minimum required work hours for a HUBZone "employee" from 40 to 80 hours during the four-week period preceding HUBZone certification or contract offer submission. According to SBA, many firms were adding individuals to their payroll without actually employing them or providing meaningful work for them to perform in a last-minute attempt to meet program requirements. SBA was also concerned that many employees would perform 40 hours of work in one week rather than working regularly throughout the four-week period. Despite its concerns, SBA did not adopt the 80-hour requirement after commenters overwhelmingly opposed it. Thus, the 40-hour requirement remains at 13 C.F.R. § 126.103. However, the final rule requires that an individual *must* work at least 10 hours per week during the four-week period to meet the criteria of being a HUBZone employee.

The final rule also addresses several important updates to other SBA programs that we will examine in future updates.

FOR MORE INFORMATION

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