THOMPSON HINE

Government Contracts Update

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Key Takeaways in SBA's Final Rule: 8(a) Business Development Program

Key Notes:

- SBA attempts to reduce potential barriers to program entry in final rule.
- SBA loosens ownership restrictions by increasing the allowable ownership interest a non-disadvantaged individual or non-8(a) business may own in an 8(a) program participant.

The U.S. Small Business Administration's (SBA) December 17, 2024 final rule incorporates the 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 January 16, 2025, applies to existing contracts but will not be applied retroactively. In this third and final installment in our series of updates analyzing the final rule, we examine notable changes to the 8(a) Business Development Program.

Application Requirements: Operating Revenue

Under 13 C.F.R. § 124.107, SBA requires applicants to establish their "potential for success," which includes submitting income tax returns demonstrating operating revenue for the two years immediately prior to application submission. Previously, the income tax returns had to reflect operating revenue in the primary industry for which the applicant was seeking certification. In its final rule, SBA modified this requirement to allow income tax returns that show operating revenues *generally* rather than in the applicant's primary industry. While a seemingly minor adjustment, this change provides greater flexibility for businesses that have recently expanded or transitioned into a different industry and may not yet have significant operating revenue in that specific sector. By removing this restriction, SBA has reduced potential barriers to program entry and made the program more accessible.

Ownership and Control

Ownership Interest Restrictions

Under 13 C.F.R. § 124.105(h), SBA sets forth restrictions applicable to non-disadvantaged individuals and non-8(a) businesses with ownership interests in 8(a) program participants. These restrictions limit the ownership percentage a non-disadvantaged owner or non-8(a) business may have in an 8(a) participant if the owner already has an interest in another 8(a) participant or a business in the same or a similar line of business. In its final rule, SBA increased the allowable ownership percentage from 10% to 20% during a participant's developmental stage (years 1-4 in the program) and from 20% to 30% in a participant's transitional stage (years 5-8 in the program).

Approval of Changes in Ownership

Previously, 13 C.F.R. § 124.105(i)(2) outlined three exceptions to the rule that requires SBA's prior approval when a participant firm has a change in ownership. In the final rule, SBA made minor changes to the exceptions and added a fourth. Now, prior SBA approval is not required if:

- All non-disadvantaged owners involved in a transaction own no more than a **30% interest** in the participant concern both before and after the transaction.
- The transfer results from a disadvantaged principal's death or incapacity due to a serious long-term illness or injury.
- The disadvantaged owner(s) in control of the participant firm will increase their ownership interest.

- The 8(a) participant has never received an 8(a) contract *and* the owner(s) upon whom initial eligibility was based continues to own more than 50% of the participant firm.

The final rule also clarifies that even if prior approval is not required, SBA must be notified of any changes within 60 days of the transaction or before the firm submits an offer for an 8(a) contract, whichever occurs *first*.

Program Compliance: Non-8(a) Business Activity Target

To help ensure that 8(a) program graduates continue their success after exiting the program, SBA requires participants to gradually increase their non-8(a) revenues in the program's latter stages. Participants are required to demonstrate good faith efforts to meet a certain percentage of non-8(a) business activity to enhance their likelihood of success once they exit the program. 13 C.F.R. § 124.509. If a firm fails to engage in a good faith effort to meet its non-8(a) business activity target, SBA may restrict its ability to receive 8(a) sole-source contracts.

What SBA meant by "good faith efforts" was murky, so it provides some guidance and clarification on this requirement in its final rule. For example, SBA previously considered unsuccessful offers a firm made on contracts as good faith efforts, but arguably, this applied even if the participant had little or no chance of receiving an award. The final rule clarifies that SBA will only consider unsuccessful offers on contracts where the firm had a reasonable prospect of success. As an example, SBA explains that if a firm has never received a contract in excess of $5 million, an unsuccessful offer on a contract for $100 million will not be considered a good faith effort because the firm was unlikely to receive this award based on prior contract awards.

SBA also clarifies that only the value of the base year of the contract for which the firm submitted an unsuccessful offer will be included as part the firm's good faith effort to meet the business activity percentage. Notably, while several commenters reasoned that projected revenue under the contract should be considered, SBA declined.

Our Government Contracts group will monitor the regulations governing SBA programs as they continue to evolve and provide relevant updates.

FOR MORE INFORMATION

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