

SBA Is Wrong To Delay Runway Extension Act

By **Deborah Rodin and Jeffery Chiow** (January 11, 2019, 2:59 PM EST)

Amid the ongoing government shutdown drama, you may have missed a recent two-word change to the Small Business Act with huge consequences for calculating small business program eligibility. The new law should allow growing small businesses to maintain their “small” status for longer. Consistent with settled U.S. Supreme Court law, the change to this basic standard for size eligibility ought to have instant effect on companies’ size representations for the new year in the System for Award Management, or SAM, and on proposals for various contracting opportunities.

But small businesses expecting to benefit from the change cannot celebrate yet. The U.S. Small Business Administration disagrees that the change is immediately effective and instead has delayed indefinitely its implementation of the new law. The SBA’s policy position poses a conundrum for contractors looking to benefit from the new law and appears to thwart the will of Congress.

The New Law

The Small Business Runway Extension Act of 2018, signed into law on Dec. 17, extends the period for determining a company’s size based on annual receipts from three to five years.[1] Previously, companies seeking small business eligibility were required to meet size standards based on average gross revenue over three years. The new law changes this look-back period to five years, allowing a longer “runway” for growing small businesses to prepare for graduation from the set-aside world. For small businesses with steady strong growth, the rule change should ease their transition to other-than-small status, enabling some such businesses to better compete in full and open competitions.

Effective Date

On its face, the law makes the change in look-back period effective immediately. It is an established principle of statutory interpretation, under enduring Supreme Court law, that a law takes effect on the date it is enacted unless Congress clearly specifies a different effective date.[2] Here, the law does not include an effective date, meaning that it should have become effective upon signing by the president.

The SBA sees it differently. In an information notice issued on Dec. 21 by SBA’s associate administrator



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for the Office of Government Contracting and Business Development — which has yet to be posted on its website due to the government shutdown — the SBA notes that the law does not include an effective date. However, the SBA concludes that the change to calculating small business size status “is not presently effective and is therefore not applicable to present contracts, offers, or bids until implemented through the standard rulemaking process.”

It is unclear how the SBA arrived at this conclusion as the information notice fails to explain the SBA’s rationale. Although it states that the SBA is drafting regulations to implement the change in the law, it fails to offer any timeframe or even any indication that the SBA is prioritizing this rule change. Instead, the SBA advises that businesses must still report their receipts based on a three-year average “[u]ntil SBA changes its regulations.”

Implementation Delay Seems Likely

There is cause to worry that the SBA will not be in a hurry to make the simple change that would be necessary to update its regulations, i.e., substituting the word “five” for the word “three”. In April of last year, the SBA issued a proposed rule concerning revisions to its size standards methodology.[3] A commenter recommended calculating average annual receipts over the preceding five years, rather than three, contending that “this would allow small businesses to plan and increase capacity before entering full and open competition and provide longer transition time from small business status to other than small business status.”[4] The SBA rejected the suggestion, saying it “would allow a business to greatly exceed the size standard for some years and still be eligible for Federal assistance, perhaps at the expense of other small businesses.” The SBA added that a change to five years “is more likely to benefit successful small business graduates by allowing them to prolong their small business status, thereby reducing opportunities for [other] small businesses.”[5]

The SBA’s track record for timely rulemaking is another cause for concern. The 2013 National Defense Authorization Act, or NDAA, made major changes to the “limitations on subcontracting,” including changing the methods of calculating compliance for service and supply contracts and allowing small prime contractors to claim performance credit for “similarly situated entities.”[6] Although the NDAA was signed into law in January 2013, the SBA implemented the changes three and a half years later in a final rule effective June 30, 2016.[7] Further compounding the SBA’s delay, it took another two years for the Federal Acquisition Regulation Council to update the FAR to conform to the SBA rule.[8]

The SBA also took more than three years to implement significant regulatory changes required by the Small Business Jobs Act of 2010, which Former President Barack Obama signed into law in September 2010.[9] The SBA published a final rule implementing the changes three years later on Oct. 2, 2013.[10] If SBA follows this pattern, we may not see a final rule extending the runway for small business eligibility until the end of 2021!

Consequences of Implementation Delay

Delayed implementation will have profound consequences for at least some small businesses and will present a quandary for others. For example, a business that has just graduated out of its small business status under the current three-year look-back period — let’s call it OnTheUp Inc. — may still qualify as small if it was measured under the new law’s five-year period. Since it would benefit OnTheUp Inc. to continue to qualify for set-aside contracts, should it rely on the law’s five-year calculation and risk an agency rejecting its proposal based on SBA’s current policy stance? If it wins, will its award be upset by a size challenge? As the SBA is among the federal agencies shuttered by the partial government

shutdown, neither contractors nor contracting officers can seek answers from the agency.

On the other hand, a business that has recently experienced declining revenue — let's call it Downward LLC — may now qualify as small under the three-year calculation but would not under a five-year average. If Downward LLC bids on set-aside contracts based on the current SBA guidance, it risks challenges to its size eligibility based on the five-year formula of the new law. Challenges might be resolved at the SBA Office of Hearings and Appeals or before the U.S. Court of Federal Claims, depending on the individual circumstances.

Additionally, if either OnTheUp Inc. or Downward LLC is entertaining offers to acquire its business, the timing and value of any such sale would likely be significantly affected by the change to the law.

Tension with Congressional Intent

The SBA's stated policy of continuing to apply the three-year average for the foreseeable future sits in direct tension with the legislative intent of the recently ended Republican Congress. It also does not bode well for the new Democrat-controlled House, which could find its legislative intent frustrated by, or held hostage to, seemingly arbitrary rule-making processes. The SBA may disagree with the wisdom of the change, but that is mostly irrelevant. As far as courts are concerned, changing a look-back period from three to five years would not seem to be the sort of area where agency discretion is even implicated, much less owed any deference.

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[1] H.R. 6330, now Pub. L. 115–324 (Dec. 17, 2018).

[2] See, e.g., *Johnson v. United States*, 529 U.S. 694, 702 (2000).

[3] Small Business Size Standards: Revised Size Standards Methodology, 83 Fed. Reg. 18,468 (Apr. 27, 2018) at 18,473-74.

[4] *Id.* at 18,473.

[5] *Id.* at 18,474.

[6] Section 1651 of the National Defense Authorization Act of 2013, Pub. L. 112–239, 126 Stat. 1632 (Jan. 2, 2013).

[7] Small Business Government Contracting and National Defense Authorization Act of 2013 Amendments, 81 Fed. Reg. 34,243 (May 31, 2016), now codified at 13 C.F.R. § 125.6.

[8] See Federal Acquisition Regulation: Revision of Limitations on Subcontracting, 83 Fed. Reg. 62,540 (Dec. 4, 2018).

[9] Small Business Jobs Act of 2010, Pub. L. 111–240 (Sept. 27, 2010).

[10] Acquisition Process: Task and Delivery Order Contracts, Bundling, Consolidation, 78 Fed. Reg. 61,114 (Oct. 2, 2013).