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## COUNSEL COMMENTARY

# SBIR Phase III Eligibility Clarified

A recent GAO decision provides guidance on when agencies may issue sole-source awards under the SBIR program.

BY STEPHEN L. BACON

The Small Business Innovation Research (SBIR) program is designed to fuel innovation while providing small businesses a pathway to federal contracts. The program also seeks to promote the commercialization of SBIR-derived technologies.

These objectives are advanced through a special acquisition preference that is afforded to SBIR program participants when agencies make “Phase III awards.” The SBIR program’s authorizing statute defines “Phase III” to include any “work that derives from, extends, or completes efforts by the SBIR participant in Phases I and II of the program.”

The law provides that, “[t]o the greatest extent practicable,” agencies “shall...issue, without further justification, Phase III awards relating to technology, including sole source awards, to the

SBIR...award recipients that developed the technology.”<sup>1</sup> This statutory Phase III preference gives agencies a streamlined method to procure SBIR-derived technologies.

In the protest of Digital Force Technologies, Inc., the Government Accountability Office (GAO) clarified the circumstances under which an agency may invoke its authority to award sole-source Phase III contracts.<sup>2</sup> GAO’s decision gives agencies, SBIR participants, and protesters important guidance on when and how this unique contracting preference may be used.

## Background

This protest involved the U.S. Air Force’s requirement for a tactical security system (TSS), which was described as a “modular, scalable, tailorable, lightweight, rapidly

deployable, ground-based security and surveillance system.”<sup>3</sup> The Air Force plans to use the TSS to assist with protecting personnel and assets at remote deployment locations.

After conducting market research, the Air Force decided to fulfill this requirement using a Phase III award to either Clear Align or Anduril Industries, effectively excluding Digital Force from competing for an award.

After its agency-level protest was denied, Digital Force filed a subsequent protest at GAO to challenge the SBIR Phase III solicitations issued to Clear Align and Anduril. In response to that protest, the Air Force took corrective action and canceled those solicitations.

Instead, the Air Force decided to pursue a single Phase III solicitation issued only to Clear Align. The Air



Force's decision was premised on its determination that "Clear Align's proposed solution derives from, extends, and completes work from two prior SBIR phase II awards."<sup>4</sup>

Digital Force challenged the Air Force's decision on several grounds. GAO rejected all the arguments raised by Digital Force and, in doing so, GAO provided three key takeaways for government contractors to understand about Phase III awards.

### **The Work Must Derive From Prior SBIR Efforts**

Digital Force argued that the Air Force's requirement for a tactical security system did not derive from Clear Align's prior SBIR work. According to Digital Force, the procurement did not qualify for Phase III

treatment because the Air Force developed its requirements separately from any of Clear Align's previous SBIR contracts.

GAO disagreed, finding that Digital Force misconstrued the statute. The statute focuses on work that derives from prior SBIR efforts, not requirements that derive from those efforts.

As GAO explained, "the statute and the policy directive each expressly use the word 'work' when explaining SBIR phase III; they do not mention the agency's requirement."<sup>5</sup> Simply put, a proper SBIR phase III award must be for *work* that derives from, extends, or completes a prior SBIR effort.

The Air Force was able to satisfy that requirement by showing that Clear Align's proposed TSS solution derived from work completed on two prior SBIR contracts.

To document this determination, the Air Force prepared a Determination and Finding (D&F) to "memorialize the agency's consideration of the relevant SBIR phase II efforts and explained their relevance to the instant procurement."<sup>6</sup>

Specifically, the Air Force concluded that Clear Align's proposed TSS included a camera that had been developed, in part, under prior SBIR contracts. Indeed, Clear Align's proposal explained that "key design concepts from the prior SBIR efforts have been refined and are embedded into its current generation of cameras."<sup>7</sup>

Moreover, the D&F included copies of the prior SBIR contracts that contained details of the work completed. This was sufficient to establish a connection between the prior SBIR contracts and Clear Align's proposed TSS solution.

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**Key Takeaway:** A contractor's eligibility for a Phase III award does not depend on how the agency writes its requirements. Rather, the agency must reasonably determine that the contractor's proposed solution builds upon its prior research and development efforts under the SBIR program.

Agencies should prepare comprehensive determinations and findings that clearly trace the connection between current work and prior SBIR efforts. Contractors pursuing Phase III opportunities should proactively provide detailed explanations of how their proposed solutions build upon previous research to support the agency's use of an SBIR Phase III award.

### **SBIR-Derived Products May Be Only a Component of the System Procured**

Digital Force complained that Clear Align's proposed TSS was made up of many commercial-off-the-shelf (COTS) products and only a single component, the camera, could qualify as SBIR Phase III work. Digital Force contended that the SBIR statute did not authorize agencies to procure a collection of COTS items that were unrelated to Clear Align's prior SBIR efforts.

According to Digital Force, the Air Force's interpretation of the SBIR statute would lead to absurd results. Specifically, Digital Force argued that "a large defense contractor could purchase the rights to Clear Align's Z 320 MWIR camera, install the camera on a C-40 aircraft, and win an SBIR phase III award for the Air Force's C-40 fleet expansion program."<sup>8</sup>

GAO rejected Digital Force's hypothetical scenario. Unlike the "cautionary

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tale involving the Air Force's C-40 fleet expansion," Clear Align's "SBIR-derived component" – the Z 320 MWIR camera – "is reasonably related to the overall objective of the system the agency seeks to procure."<sup>9</sup> GAO noted, for example, that the required TSS needed "surveillance capability, motion detection, video assessment, and sensing technologies, and Clear Align is providing within its overall system, an SBIR-derived camera."<sup>10</sup>

**Key Takeaway:** Companies with SBIR-derived technology can potentially leverage Phase III authority for larger systems that incorporate their innovations, provided the SBIR component serves a meaningful role in the overall solution. Future cases are likely to test how close of a nexus is required between the SBIR-derived technology and the objective of the system procured by the agency.

### **Document Status as a Successor-in-Interest Entity**

Digital Force also challenged whether Clear Align qualified as a "successor-in-interest" to Computer Optics, the company that performed the original SBIR Phase II work. This argument highlights a common complication in the SBIR ecosystem: small companies frequently merge, acquire assets, or undergo corporate changes between Phase II completion and Phase III opportunities.

The SBIR/STTR Policy Directive allows Phase III awards to entities that are successors-in-interest to the original SBIR participants. But what constitutes sufficient evidence of succession to qualify for a Phase III award?

In this case, Clear Align acquired the assets of Computer Optics through a detailed purchase agreement that transferred "all intellectual property used or usable in connection with the business, including, without limitation, patents, computer software and

data, trademarks, trade styles, trade secrets, know-how, processes, formulae, designs, drawings, [and] technical data.”<sup>11</sup>

GAO found this sufficient to demonstrate that Clear Align qualified as a “successor-in-interest.” The agency had reasonably concluded that Clear Align acquired the relevant intellectual property and could legitimately claim successor status.

**Key Takeaway:** Companies acquiring or merging with SBIR participants should document transactions thoroughly. The asset purchase agreement should explicitly address intellectual property transfers, including SBIR-derived technology. This is critical to ensure that the resulting entity is eligible for Phase III awards as a “successor-in-interest” to the acquired entity.

### Looking Forward

The *Digital Force* decision provides valuable clarity for the government contracting community. SBIR Phase III authority remains a powerful tool for agencies seeking to leverage successful research investments, even when that research represents only part of a larger system solution.

For SBIR companies, the decision confirms that Phase III opportunities can extend beyond narrow technical applications to broader system integrations. Success requires clear documentation of the connection between past research and current proposals, along with proper handling of any corporate succession issues.

For competitors considering protests, *Digital Force* demonstrates the high bar for challenging Phase III awards. If the agency’s Phase III determination is adequately documented, technical disagreements about connections between

SBIR phases are unlikely to succeed. Challenges should focus instead on clear procedural violations or obvious misapplications of Phase III authority.

Most importantly, the decision underscores that SBIR Phase III procurement operates under different rules than traditional competitive acquisitions. Understanding these distinctions and planning accordingly remains essential for success in this unique corner of the federal marketplace. **CM**

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*The views expressed in this article are those of the author and do not necessarily reflect the views of Rogers Joseph O’Donnell or its clients. This article is for general information purposes and is not intended to be and should not be construed as legal advice.*

### ENDNOTES

- 1 15 U.S.C. § 638(r)(4).
- 2 Digital Force Technologies, Inc., B-423319, May 19, 2025, 2025 CPD ¶ 114.
- 3 Id. at 2.
- 4 Id. at 4.
- 5 Id. at 7 (citing 15 U.S.C. § 638(e)(4)(C); SBIR/STTR Policy Directive (May 2023) § 4(c).
- 6 Id. at 13.
- 7 Id. at 9.
- 8 Id. at 10.
- 9 Id. at 14.
- 10 Id.
- 11 Id. at 16.

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