

RULES and REGULATIONS

SMALL BUSINESS ADMINISTRATION

13 CFR Part 121

Small Business Size Standards

Thursday, February 20, 1986

*6099 AGENCY: Small Business Administration.

ACTION: Statement of General Policy, SBA Size Policy Statement No. 1.

SUMMARY: The Small Business Administration (SBA) hereby gives notice of its intended application and interpretation of the definition of "number of employees," at 13 CFR 121.2(b). This Agency regulation has for a number of years provided for the calculation of the number of employees of a business for size standard purposes on several alternative bases, including employees retained on a ". . . full-time, part-time, temporary or other basis . . ." The Agency has examined its administrative precedents interpreting 13 CFR 121.2(b) as it applies to the treatment of employees not clearly full-time, part-time or temporary employees of a business, and finds that a line of cases exists which deal with employees provided by temporary employment agencies and other employment contractors (hereafter jointly referred to as employment contractors) in a way which is overly mechanical and has the potential for subjecting SBA size determinations to abuse. In these cases, the Agency has merely applied the common law indicia of an employee/employer relationship, i.e., who hires, fires, pays and withholds taxes and provides benefits, to determine whether such individuals should be treated as employees of the business or not. This approach creates a potential for firms to avoid the consequences of their true size by imaginative use of employment contractors. Recognizing this potential for abuse and seeking a way to fairly ascertain which businesses are truly small and which are truly large, the Agency hereby announces that it shall examine the totality of the circumstances under which businesses have obtained employees from employment contractors to determine whether such employees should be considered employees of the subject business on some "other basis," under the existing regulatory language even if not temporary employees of the business under the common law. This general statement of policy also provides specific guidelines as to how the Agency intends to apply the language "other basis" contained in 13 CFR 121.2(b).

EFFECTIVE DATE: February 20, 1986.

*6100 ADDRESS: Written comments should be addressed to Robert J. Moffitt, Chairman, Size Policy Board, U.S. Small Business Administration, 1441 L Street, N.W., Washington, D.C. 20416.

FOR FURTHER INFORMATION CONTACT: David R. Kohler, Associate General Counsel, Office of General Law, (202) 653-6660.

SUPPLEMENTARY INFORMATION: The Small Business Administration (SBA) has determined that the definition of "number of employees" at 13 CFR 121.2(b) requires clarification in light of the decisions issued to date by the former Size Appeals Board (Board) and the current Office of Hearings and Appeals (OHA). This determination is based on the Agency's conclusion that certain size appeal determinations could be read to necessarily exclude em-

ployees obtained through employment contractors from the number of employees of a business considered in determining such business' size status. Two cases have directly addressed this particular issue: Appeal of Marinette Marine Corporation and Marine Power Equipment Co., No. 1495, September 28, 1981, [affirmed, 527 F. Supp. 587 (D.D.C. 1981)], and Size Appeal of Aeromech Industries, Inc., No. 1979, June 22, 1984. The purpose of this statement of general policy is to clarify the approach the Agency intends to take in the future for resolving questions arising under 13 CFR 121.2(b) and involving employment contractors.

Before discussing the specific question of whether individuals whose services are procured through an employment contractor should be counted as employees of a business for size determination purposes, a brief review of the Agency's interpretation of the language "number of employees" is in order. Two general principles have governed size determinations where the number of employees of the business has been in issue. Foremost of these is that all employees of a business, including those of its affiliates, whether full-time, part-time, temporary or otherwise (including floaters), and regardless of whether they are engaged in industries related to the procurement involved in the size protest, count as employees of the business for size status purposes. Second, individuals who are clearly employees of bona fide independent contractors/consultants of the business whose size is in question have not been generally considered as temporary employees of that business.

The Agency's decisions in Marinette Marine and Aeromech follow these general principles. In Marinette Marine, the Board held that employees retained for a short period of time through an employment contractor were not "temporary" employees of the protested concern since they were bona fide employees of the employment contractor, an unaffiliated business. In that case, the protested concern had utilized replacement workers for the completion of a Navy Contract. While the protested concern maintained supervision and control over the worker's performance, all other incidents of employment were supplied by the employment contractor. The Board held that the term "temporary" employee in the size regulations does not include employees of other concerns, even if they are performing work on the premises of the prime contractor and subject to its supervision. See Also Marinette Marine Corp. v. Department of Navy, 527 F. Supp. 587, 590-92 (D.D.C. 1981). The Board appeared to draw on the precedent it established in Size Appeal of Newton Lumber Co., Ltd., No. 502, July 14, 1971, where the status of certain logging contractors was in issue. There, the Size Appeals Board expressly applied the common law test for finding a master/servant relationship, i.e., who hires, fires, pays and withholds taxes, provides benefits and supervises performance. In Aeromech, where the status of certain consultants was in issue, OHA referred without further discussion to Marinette Marine as standing for the proposition that "persons on the payroll of a temporary personnel agency are not treated as employees of the firm whose small business size status is under consideration." Aeromech, supra, p. 6. The decisions in both of these cases follow the reasoning first applied in the context of the independent contractor/consultant cases not involving temporary personnel agencies. The rationale used was that where an individual was either self-employed or employed in the traditional sense by an independent company, i.e., such company selected him or her, paid his or her wages, withheld and paid employment taxes and benefits, etc., he or she could not be considered as also being an employee of the concern whose size was in question. While the Agency does not dispute the general wisdom of this rationale, it is concerned that mechanical application of this rationale ignoring the "other basis" portion of its regulations will result in decisions at variance with the spirit of the Small Business Act and the small business size standards promulgated pursuant thereto.

This concern is based, in part, on the manner in which the Board, and later OHA, analyzed the cases presenting the issue. In the decisions discussed above, the Board and OHA focused on only the common law indicia of an employer/employee relationship, without addressing the totality of the circumstances under which the individuals in question came to labor for the business whose size was in issue.

The mechanical exclusion of employees retained through an employment contractor from the number of employees counted in determining a business' size status would encourage circumvention of the size standards by means of creative employment practices. Therefore, in order to preserve the integrity of its size regulations, the SBA has determined that in appropriate cases individuals whose services have been procured through an employment contractor should be considered "individuals employed on . . . [an] other basis," under 13 CFR 121.2(b) and be counted as part of that business' "number of employees" even if technically the employees of the contractor under common law prin-

principles. To do otherwise would be to permit form to prevail over substance. The Agency will not condone the use of employment practices that allow a business to create the facial appearance of being small under the size standards while at the same time deriving the usual benefits from the services of individuals in excess of those standards.

Agency officials charged with the responsibility of making size determinations shall take special care in such cases to determine whether any "other basis," aside from whether a full-time, part-time or temporary employee/employer relationship exists, to properly treat such employees as employees of the subject firm. In doing so, they should consider any information or data relevant to the question of whether an employer is deriving the usual benefits incident to employment of such individuals, and the circumstances under which the situation came to exist. The totality of the circumstances should be considered in order to prevent circumvention of SBA's size regulations, including, but not limited to:

1. Did the company engage and select the employees?
2. Does the company pay the employees wages and/or withhold employment taxes and/or provide employment benefits?
3. Does the company have the power to dismiss the employees?
- *6101 4. Does the company have the power to control and supervise the employees' performance of their duties?
5. Did the company procure the services of the employees from any employment contractor involved in close proximity to the date of self-certification as a small business?
6. Did the company dismiss employees from its own payroll and replace them with the employees from any employment contractor involved? Were they replaced soon after their dismissal?
7. Are the individual employees supplied by any employment contractor involved the same individuals that were dismissed by the company?
8. Do the employees possess a type of expertise or skill that other companies in the same or similar lines of business normally employ in-house (as opposed to procuring by sub-contract or through an employment contractor)?
9. Do the employees perform tasks normally performed by the regular employees of the business or which were previously performed by the company's own employees?
10. Were the employees procured through an employment contractor to do other than fill in for regular employees of the company who are temporarily absent?
11. Does the contract with the independent contractor have a term based on the term of an existing Government contract?

The presence of one or more single factors on the list in a particular case may but will not necessarily support a finding that the employees should be attributed to the business whose size is in issue. This listing is not meant to be exhaustive, and other factors not listed that demonstrate an effort on the part of the firm to satisfy the SBA size standard in form, while deriving the benefits of a much larger number of employees in fact, must be considered.

In announcing this policy, the Agency recognizes that in the normal course of business operations there are legitimate business reasons in some cases for procuring employees through employment contractors or other kinds of indepen-

dent contractors. The policy expressed herein should not be construed so as to penalize a business engaging in legitimate business arrangements to adversely affect its size status. The Agency believes that the regulatory language "other basis" was intended to reach situations where the number of employees is artificially reduced to meet particular size standards for the purpose of becoming eligible for a particular procurement or for receipt of some other SBA program benefit, while the firm continues to operate or be capable of operating for all intents and purposes as though it employed a larger number of individuals.

Dated: February 10, 1986.

Robert A. Turnbull,

Acting Administrator.

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