TESTIMONY OF
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"INCREASING GOVERNMENT ACCOUNTABILITY AND ENSURING FAIRNESS IN SMALL BUSINESS CONTRACTING"

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Chairman Kerry, Ranking Member Snowe, and members of the committee, my name is Todd McCracken, and I am the president of the National Small Business Association (NSBA), the oldest small-business advocacy organization in the United States. On behalf of NSBA, I would like to thank you for inviting me to testify today on small-business federal contracting.

Federal procurement is not just of singular importance to many small businesses—small-business participation is crucial to a healthy and competitive federal procurement process. Small businesses provide high-quality goods and services to federal-contracting agencies and infuse the federal procurement system with much-needed competition. In turn, the federal government invests in the most-dynamic and innovative sector of the U.S. economy. America's small businesses annually have generated 60 to 80 percent of the country's net new jobs over the last decade. Small businesses also "produce 13 to 14 times more patents per employee than their larger counterparts, and... these patents are more likely to be cited in other patenting applications," according to a recent Small Business Administration Office of Advocacy working paper.

This unrivaled success has been achieved with less than adequate governmental support, however. In FY 2006, for instance, small companies received 19 percent of federal contracting dollars, according to data compiled by the respected research firm Eagle Eye Publishers. Even governmental statistics regarding small-business federal contracting—while more optimistic than those independently compiled—are underwhelming considering the huge and integral role small businesses play in the U.S. economy. The federal research and development numbers are even more disheartening. Despite employing more scientists and engineers than large businesses (32 percent vs. 27 percent) and generating five times more

patents per research and development dollar than large companies, America's small businesses receive only 4.3 percent of federal research and development funds.

Small Business Contracting Goal

The *Small Business Reauthorization Act of 1997* established a government-wide goal of 23 percent of prime, federal contracts to be awarded to small firms. While this was a welcome initial step, it is time to enhance it. America's small businesses—which comprise 99.7 percent of all employer firms in the U.S., employ half of all private sector employees, and are responsible for more than 50 percent of the country's private, non-farm gross domestic product—deserve their fair share of federal contracting dollars. NSBA supports increasing the government's small-business procurement goal to at least a third of all federal contracts. This does not seem an overly ambitious goal, when one considers that small business comprises half of the U.S. economy. NSBA also supports legislation that would stipulating that each federal agency have an annual small-business procurement goal not lower than the government-wide goal.

Furthermore, NSBA strongly believes that the calculation of agencies small-business contracting numbers should incorporate ALL of an agency's contracts, including those carried out abroad. The inexplicable exclusion of various kinds of contracts, such as those carried out overseas, has distorted the reality of federal small-business procurement for too long. The continued omission of certain types of contracts from the government's small-business procurement calculations too frequently has resulted in escalating exclusions and creative bookkeeping rather than increased small-business contracting or even accurate data collection.

Since 1984, the Competition in Contracting Act (CICA) has prohibited the bundling of contract requirements in a way that unreasonably restrains competition beyond the government's minimum needs. Twenty years ago, in 1987, the Comptroller General issued an advisory ruling in the *Pacific Sky Supply* case which prohibited contract bundling for reasons of administrative, bureaucratic convenience. Unfortunately, federal agencies routinely have ignored this, and the CICA does not set clear standards on the issue. It is therefore not surprising that, according to the White House Acquisition Advisory Panel, about one third of the federal contracts awarded in FY 2004, totaling $108 billion, were awarded without competition. Congress should consider directing the SBA to issue binding regulations prohibiting anti-

competitive bundling in violation of the Competition in Contracting Act. Congress also should direct agencies to set a portion of requirements rolled together under various strategic sourcing initiatives for award to small businesses.

Reliable and Accurate Data

The previously-alluded-to discrepancies between the small-business contracting statistics compiled by the government and outside experts demonstrate the absence of reliable and accurate small-business federal procurement data. Time and again, it has been demonstrated that a large number of contracts ostensibly awarded to small businesses actually have been awarded to and carried out by large firms. A FY 2005 Office of Advocacy-sponsored study found that 44 of the top 1,000 small business contractors in FY 2002 were not, in fact, small businesses—and the small-business coded contracts they received totaled $2 billion. The aforementioned exclusion of various kinds of contracts, such as those carried out abroad, also dilutes the accuracy of federal procurement data. NSBA continues to support efforts to improve the accuracy and reliability of federal procurement data.

NSBA supports the new SBA regulation regarding small-business size-standard recertification following mergers, acquisitions, novation requests, and prior to any option being exercised. Agencies must not receive credit for small-business contracting when none actually has occurred, and contracts purportedly awarded to small businesses actually should be carried out by them.

It is equally vital that these firms not be penalized for their growth. NSBA opposes any effort to change the terms and conditions of contracts awarded to actual small businesses that grew beyond their small-business status during the duration of their contract. Small-business growth should not be penalized, especially if the growth is transitory and related only to the duration of a contract. Small businesses also must not be further saddled with onerous regulatory requirements, as they already disproportionably bear the burden of federal regulations and paperwork. Accordingly, NSBA recommends requiring small-business contractors to recertify their size status every three years, and using a rolling average of their size during this time. This approach will not overly burden small-business contractors with recertification requirements, nor will it unduly punish small-businesses that briefly surpass their size status.

Todd McCracken
National Small Business Association

Elimination of Fraud

Large businesses are far too frequently the real recipients and executors of federal contracts ostensibly awarded to small businesses. Up to a third of the SBA's list of top 100 small business contractors in 2005 were actually large businesses, according to a report from Eagle Eye Publishers. More than 20 percent of the respondents to an NSBA survey reported losing out on a federal procurement opportunity that instead went to a large firm identified as a small business.

Since 1988, the *Small Business Act* provided for felony convictions up to 10 years, criminal fines of $500,000, mandatory 3-year debarments, and forfeitures for companies which are determined by the SBA to misrepresent their small business status in seeking government contracts. Prosecutions under these provisions have been lacking, and the SBA rarely rules on whether companies misrepresent their small business status. This should change. To combat fraud, NSBA urges prompt prosecution for companies found to have fraudulently claimed small-business status. NSBA also continues to advocate for increased authority for the SBA to disbar large contractors that fraudulently identified themselves as small businesses.

Contract Bundling

Small-business concerns about contract bundling are not new. Unfortunately, they are persistent—as the love affair between federal procurement agents and bundled contracts continues unabated. This dalliance perseveres despite repeated governmental denouncements of its economic unseemliness. No less than the president himself has called for a reduction in contract bundling, saying "I believe the best way to help our small businesses is not only through small-business loans. . . but to unbundle government contracts so people have a chance to be able to bid and receive a contract to help get their business going." NSBA agrees.

The exceptional growth witnessed in the last 15 years in the size, breadth of work, and number of work locations of prime contracts has been to the detriment of America's small businesses. According to a report sponsored by the Office of Advocacy, by FY 2001, "an average bundled contract was over three times larger than an average contract and over five times larger than an average unbundled contract."

According to the same report, federal agencies reporting to the U.S. General Services Administration's Federal Procurement Data Center issued a combined 1.24 million prime contracts worth $1.89 trillion between FY 1992 and FY 2001. The report determined that 8.6 percent of these contracts were bundled and that they accounted for $840.3 billion, or 44.5 percent, of all reported prime contract dollars during this period. The more frequently contracts are bundled and the larger the average bundled contract becomes, the more small businesses are going to be excluded from competing in the federal procurement system. In fact, nearly a third of the respondents to an NSBA procurement survey reported first-hand experience of losing out on a federal contract because of contract bundling.

The previously-referenced bundling statistics are based on a more broad definition of contract bundling than currently used by the federal government, which relies on a limited definition focused exclusively on whether one of the contracts was previously performed by a small business. This overly-narrow definition warps the government's calculations on the prevalence of contract bundling in the federal procurement arena. NSBA advocates expanding the definition of contract bundling to include any instance where two or more individual contracts are combined.

In order to break-up bundled contracts and ensure agency compliance with existing contracting rules, NSBA supports increased oversight authority for the Office of Management and Budget. NSBA also supports an increased level of authority for the Office of Small and Disadvantaged Business Utilization or the establishment of a similar small-business-focused contracting office within each agency.

Subcontracting

Federal subcontracting is greatly important to small businesses as well. From FY 1985 to FY 2004, small firms received between 34 and 42 percent of all federal subcontracting, according to a recent working paper produced by the Office of Advocacy. The enactment of a government-wide subcontracting goal would help improve these numbers. NSBA also supports including the entire contract award when calculating the percentage of small-business subcontracts awarded and not just those dollars that are subcontracted.

Simply increasing small-business opportunities for federal subcontracting is not sufficient. The federal government must do more to protect small-business subcontractors and to ensure that they are being paid in a timely matter. In fact, 70 percent of the respondents to an NSBA procurement survey expressed the belief that the federal government should provide more oversight and protection for federal subcontractors. This may not be surprising when one considers that nearly a quarter of the respondents said that their small business had been included, as a subcontractor, in a multi-year contract for which the prime contactor has yet to provide any work or payment—and in almost 70 percent of the contracts in question work had commenced over 12 months ago.

Additionally, almost 30 percent of the respondents reported personally experiencing "extreme delays" for subcontracting services they had provided. Accordingly, NSBA continues to advocate for the codification of payment history in the federal evaluation of all prime federal contractors. NSBA also supports proposal to grant prime contractors bonus credits for their next bids upon for achieving their subcontracting goals.

Conclusion

As the members of this committee well know, small business is the engine of the U.S. economy. America's small businesses lead the nation in net new job creation and innovation. Small businesses also can infuse the federal procurement system with much-needed competition—but only if they allowed to compete on an even slightly-level playing field. Achieving such a playing field will benefit both the small-business community and the country.