

# Strengthening Small Business and the Economy Through Procurement Reform

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## KEY TAKEAWAYS

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- Small businesses play a critically important role in helping the federal government procure goods and services. Federal purchasing from small businesses, which totals more than \$130 billion each year, promotes competition, innovation, diversity, supply chain resilience, and national security.
- Federal agencies have met the annual goal of spending 23% of procurement dollars with small businesses for seven consecutive years. The government has also consistently met other small business set-aside goals, such as for small disadvantaged businesses and service-disabled veteran-owned businesses.
- The government has generally failed to meet procurement goals for women-owned small businesses and small businesses located in historically underutilized business zones.
- Recent trends concerning the breadth of small business participation have raised concern among many that opportunities for small and young companies in procurement are diminishing.
- One worrying trend is that the number of small businesses serving as federal contractors has been falling for a decade. Meanwhile, the number of new small business entrants into the federal procurement marketplace has fallen.
- There are several improvements Congress should consider including in an infrastructure package, or other legislation, that would expand contracting opportunities for small businesses. This would not only support small businesses, but also advance other national priorities such as supply chain resilience, job creation, and competition.

Promoting and expanding small business participation in federal procurement has long been a bipartisan priority.

- Rep. Nydia Velázquez (D-NY), Chairwoman of House Committee on Small Business: “When small businesses are awarded federal contracts, the result is a win-win.”
- Sen. Marco Rubio (R-FL), former chairman of Senate Committee on Small Business and Entrepreneurship: “Innovations and unique solutions from small business in the private sector help to support our soldiers, protect national security, enhance government operations and make the federal bureaucracy more efficient. To keep this contracting cycle going, we must reduce fraud, streamline the contracting office at the SBA, and provide more opportunities for small businesses to grow.”
- Former Sen. Olympia Snowe (R-ME), former chairwoman of Senate Committee on Small Business and Entrepreneurship: The small business set-aside target of “23 percent is only a base goal—we must strive to exceed it, not just meet it .... [and] maximize the use of America’s innovative small businesses in the contracting arena.”
- Biden administration:
- White House Fact Sheet, June 2021: “Agencies will assess every available tool to lower barriers to entry and increase opportunities for small businesses and traditionally-underserved entrepreneurs to compete for federal contracts.”

### **Supply chain resilience**

- President Biden made clear, in a February executive order, that small businesses are critical for “resilient, diverse, and secure supply chains to ensure our economic prosperity and national security.”

### **Industrial base vitality**

- “The [Defense] Department’s technological advantage depends on a healthy and secure national security innovation base that includes both traditional and non-traditional defense partners. ... We will continue to streamline processes so that new entrants and small-scale vendors can provide cutting-edge technologies.” Former Secretary of Defense James Mattis, 2018 National Defense Strategy summary

### **Economic development and competition**

- “The government recognizes that without intervention, the federal acquisition marketplace could suffer from inefficiencies such as high concentration and lack of innovative activity.” Center for Strategic and International Studies

A big role for small business in government procurement has other advantages, too. Compared to larger companies, small businesses can be faster and less bureaucratic. They can also be more “accommodating and flexible to incorporate requests that tweak a contract,” one small business contractor told us.

## **TRENDS IN SMALL BUSINESS PROCUREMENT**

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Every year, the federal government must allocate 23% of prime contract spending to small businesses. While definitions of “small business” vary according to employment size, revenue, and sector, this equates to well over \$100 billion in public money going to small businesses annually. The U.S. government has met this 23% goal seven years in a row.

## Federal Procurement Spending Has Met or Exceeded Goal 7 Consecutive Years

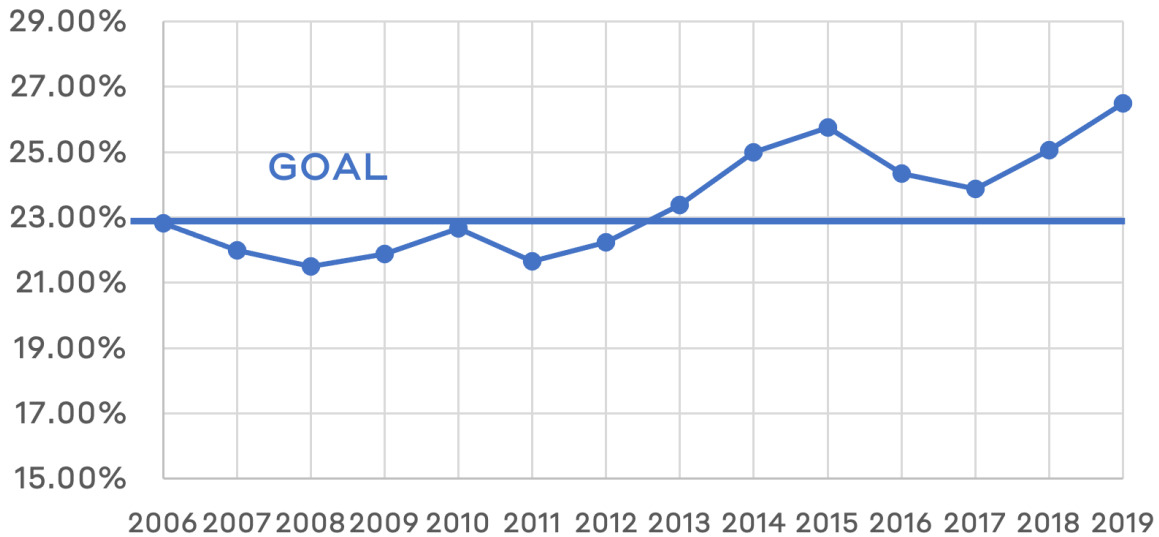


Figure 1. Source: Small Business Administration.

The government has other small business goals to meet as well. Each year, 5% of procurement spending must be allocated to small disadvantaged businesses (SDBs) and women-owned small businesses (WOSBs). Three percent is meant to go to small businesses located in historically underutilized business zones (HUBZones) as well as service-disabled veteran-owned small businesses (SDVOSBs).

The SDB goal has been met consistently for the last 15 years. For eight consecutive years, the SDVOSB goal has been met—and the share achieved rose every single year from 2006 to 2019. (See Figure 4 below.)

### ROOM FOR IMPROVEMENT

There are challenges facing small business procurement. Small businesses and their advocates see ample room for improvement and are optimistic about positive reforms. Yet they also express deep concerns along several fronts.

*Declining Participation.* Even as the government has successfully met the topline 23% goal for several years, the number of small businesses serving as federal contractors has steadily decreased.

### Steady Decrease in Number of Small Businesses Providing Common Products & Services to Federal Government

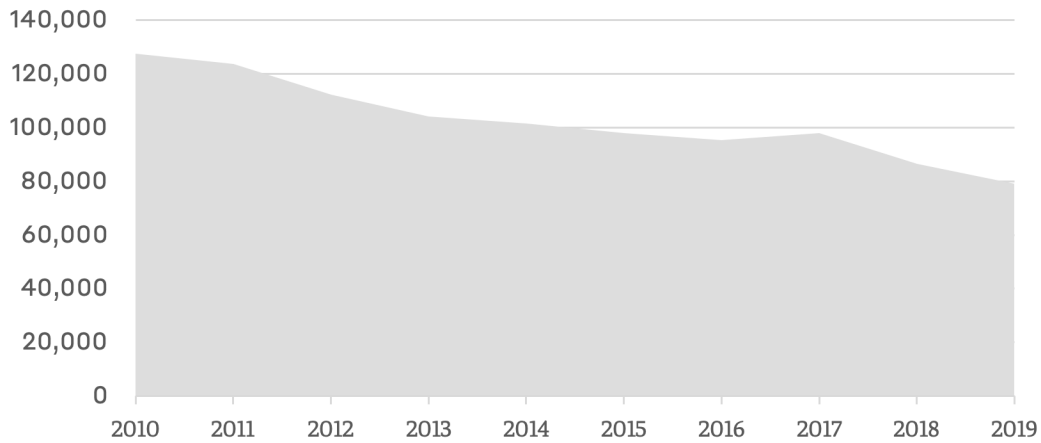


Figure 2. Source: Government Accountability Office.

Small businesses and advocates say this is due to an increased emphasis within the federal government on consolidated, bundled, and government-wide contracts.

### Fewer New Entrants

A big reason for shrinkage in the pool of small business contractors is a sharp drop in the number of small businesses newly entering the procurement space.

### Dramatic Decline in Number of New Small Business Entrants into Federal Contracting

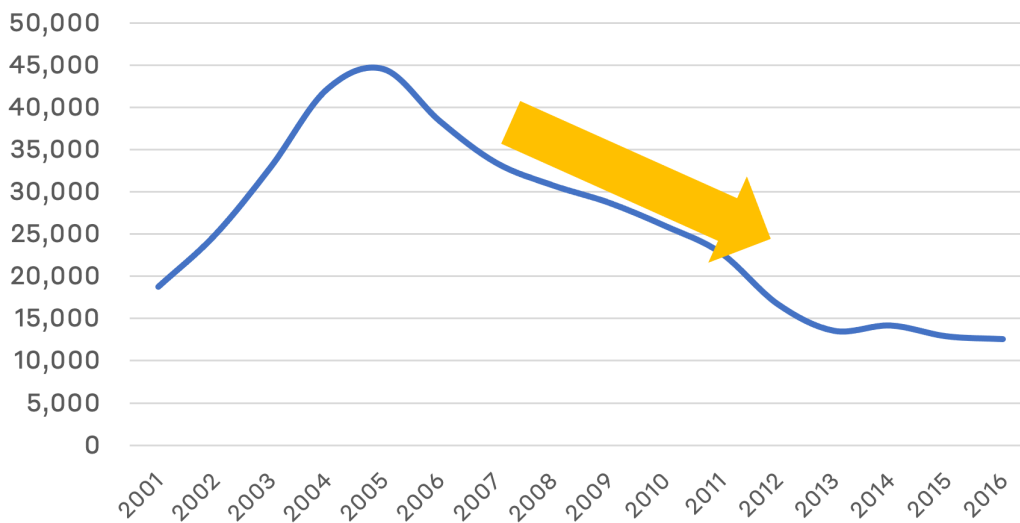


Figure 3. Source: CSIS, based on FPDS data.

Fewer small businesses are even bothering to attempt to serve the federal marketplace. According to the SBA, the number of new small business entrants into federal contracting in 2019 was just 9,400. Putting this figure together with CSIS data, that would represent, since 2005, a **79% decline**

For many small businesses, the process is too daunting to even attempt. A survey conducted for the Goldman Sachs *10,000 Small Businesses Voices* program found that **54% of small businesses had not applied for a federal contract because the “federal procurement process is too time-consuming.”** And this among those who had already applied for state or local government contracts.

## GOALING: MORE THAN MEETS THE EYE

While the federal government has performed well in meeting some specific goals (SDBs, SDVOSBs), it has fallen short in other areas.

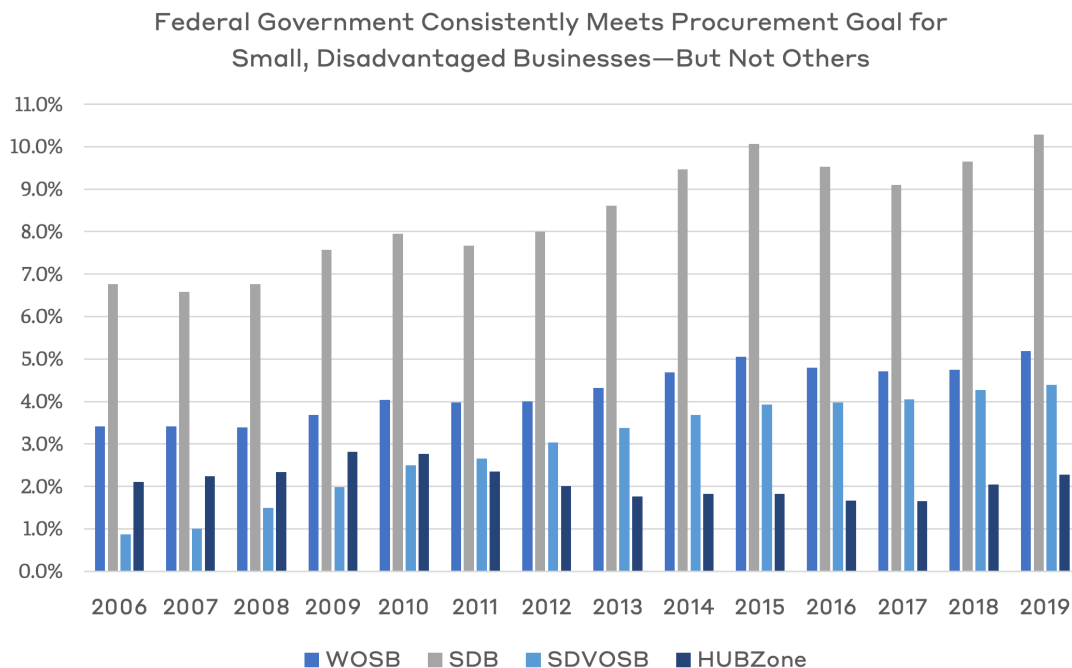


Figure 4. Source: SBA.

While the WOSB goal was met in fiscal year 2019, it has only been met one other time (2015) since it was established in 1994. The HUBZone goal of 3% has never been met. That, says Delali Dzirasa, president of a small business contractor, “equates to well over \$7-8 billion in spending that was not making it into communities most in need.”

More problematically, across the small business set-aside programs, the dollar value of contracts awarded is often counted against more than one program. It’s “double dipping” for federal agencies and prime contractors,

one small business owner told us. If an award is granted, or a subcontract given, to, say, a woman-owned small business in a HUBZone, it is counted toward both goals. This, says Dzirasa, “inflates the data reported on small business contracting awards.”

## OMINOUS OMENS

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In 2015, Section 809 of the FY2016 National Defense Authorization Act created a panel of experts to explore ways to streamline and codify acquisition policy for the Department of Defense. Included in a voluminous set of reports was a recommendation, released in 2019, that small business set-asides for “readily available products and services” be ended and replaced with a 5% price preference for small businesses.

“Small business policies, which are focused on meeting quotas through indiscriminate set-asides and reservations, are not benefiting DoD or small businesses in a way that ensures DoD has access to a robust, innovative, and globally competitive small business vendor-base.” — Section 809 Panel

This and other recommendations conveyed the sense to many that the federal government is not interested in making things easier for small businesses or expanding their participation. It reinforced a feeling among small businesses that they are an afterthought or, worse, nuisance to federal agencies. The Goldman Sachs 10,000 Small Businesses Voices survey found that, among small businesses that have applied for state or local government contracts, **four in 10** have declined to apply for federal contracts because:

**“success is unlikely because small businesses are not adequately prioritized”**

The House Small Business Committee concluded that the Section 809 Panel recommendations “would cause great harm to small firms and weaken the pool of contractors performing work for DOD.” The Section 809 Panel reports and recommendations are related to the institution of category management across the federal government (see sidebar).

### Overview: Category Management

What is it?

- A method of procurement that seeks efficiency and cost-savings through reduction of duplicative contracts, multiple purchase orders of similar goods and services, and coordination across contracting agencies.

How does it work?

- Category management relies on the use of tools such as “best-in-class” contracts to standardize and reduce the overall number of govern-

mentwide contracts.

#### What does it achieve?

- It saves taxpayers money: \$27 billion in first three years for federal government.

#### How does it affect small businesses?

- GAO calculated that, of those contracts eliminated due to category management since 2016, 53% had previously been won by small businesses.
- “The government-wide push to increase the use of category management leaves small businesses shut out of opportunities to contract across the government.” — Dzirasa

#### **BUT:**

- Category management is not incompatible with small business participation and its benefits.
- The United Kingdom adopted category management in its public procurement four years before the United States. There, category management was seen both as a way to cut costs and increase small business participation.
- An IBM study found that, in the UK, **category management “helped attain the governmentwide procurement goal of increasing spending with small and medium-size businesses.”**

### **IN THEIR OWN WORDS: WHAT SMALL BUSINESSES SAY**

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Together with Goldman Sachs 10,000 Small Businesses Voices and Center Forward, we convened two roundtables of small businesses that have been or currently are government contractors.

#### **On category management, best-in-class contracts**

These require “new strategies for small businesses and changes to SBA contracting programs to increase small business participation.” Vicki Marino, Testimony, Senate Committee on Small Business and Entrepreneurship

“They’ve made clear that they feel small businesses are a hindrance to their category management model.” Roundtable participant.



## **On SBA and procurement monitoring resources**

“We complain [about abuses and violations] but nothing seems to change. The government tells us they don’t have the funding to monitor and that we small businesses need to be the police and tell them.” Roundtable participant.

“It’s not a question of over- or under-regulation. It’s a matter of having the resources to regulate the way the system was designed.” Roundtable participant.

“It comes down to the resource and staffing issue at SBA. We need more PCRs [procurement center representatives] that really have authority. They have overwhelming caseloads but no teeth in enforcing. We have got to find a way to strengthen SBA and give them teeth.” Roundtable participant.

## **On the relationship between large prime contractors and small business subcontractors**

“A lot of them are squeezing their small business subs.” Roundtable participant.

“Squeezing is an issue, but there’s also just bad treatment by the primes.” Roundtable participant.

“Primes underbid a contract to get their foot in the door, and then small businesses pay the price, but they bake that into their strategy from the beginning.” Roundtable participant.

## **On the overall orientation of government toward small businesses**

“It is tougher for a small business because we do get scrutinized much more closely than a larger business.” Roundtable participant.

“Some agencies are forcing small business to work through only a few vehicles, essentially telling small businesses you shouldn’t be in business. They’re crunching and crunching down the small business numbers.” Roundtable participant

## SPOTLIGHT: 8(A) BUSINESS DEVELOPMENT PROGRAM

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One expert we spoke to described this as the “anchor program” in efforts to expand and strengthen small business participation in procurement. As the name implies, the 8(a) program is intended to help businesses grow and compete.

- Eligibility: businesses owned by socially and economically disadvantaged individuals
- Duration: 9 years
- Benefits: contracting preferences such as set-aside and sole-source awards

As with other areas of federal procurement, the 8(a) program is not without room for improvement. The SBA has worked for the last several years to increase 8(a) participation after declines in the number of certified firms. Experts we spoke to also cited “unreasonable” regulatory restrictions around what 8(a)-certified small businesses are able to do in terms of growth and acquisitions.

### Opportunity for Reforms That Advance Public Priorities

Congress and the Administration have two major opportunities to enact reforms that, while maintaining a focus on efficient use of taxpayer dollars, promote greater small business participation in federal contracting. Such expansion will strengthen supply chains, contribute to industrial base vitality, enhance competition, and boost local economies. Those opportunities are (1) a potential infrastructure package this year, and (2) SBA reauthorization, potentially in 2022.

“Infrastructure investment represents an investment in all those small businesses that one way or another support the U.S. infrastructure.” — Kweisi Mfume (D-MD), Chairman, Subcommittee on Contracting and Infrastructure, House Small Business Committee.

**88%** of small business owners support Congress making changes to the federal procurement process to ensure small businesses are able to receive more federal contracts. That’s according to the Goldman Sachs 10,000 Small Businesses Voices survey.

### What Actions Can Be Taken?

There are number of different national objectives and public priorities that can be advanced through small business procurement reforms. With bipartisan support, Congress could consider such actions in forthcoming legislation.

## **Objective: Expand the breadth of small business participation and reduce entry barriers**

### **Actions:**

- Raise the simplified acquisition threshold
- Expand what is considered as part of “past performance”
- Establish specific annual goals for new small business entrants

## **Objective: Enhance assistance for small businesses to increase competition**

### **Actions:**

- Lower specific bonding thresholds or strengthen the SBA’s Surety Bond Guarantee Program
- Incentivize and assist utilization of training ahead of certification for programs such as 8(a)
- Create dedicated on (new entry) and off (established larger small businesses) ramps

## **Objective: Improve transparency, accountability, and oversight**

### **Actions:**

- Increase staffing and resources at SBA and for contracting officers across agencies
- Improve data collection in the electronic subcontracting reporting system (eSRS) regarding prime contractors and subcontractors
- Monitor and enforce payment timeline reforms for prime contractors and their subcontractors

## **Objective: Modernize the 8(a) program**

### **Actions:**

- Streamline the certification process at the beginning and for annual renewal
- Remove the limitation on mergers and acquisitions—or at least the requirement of SBA Administrator approval
- Increase the sole-source thresholds

## CONCLUDING THOUGHTS

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Small businesses play a crucial role in the economy and are a critical element of the federal procurement system, providing vital goods and services to the federal government each year. Supporting small businesses' involvement in government contracting promotes competition, diversity, job creation, free and open markets, and innovation. Small business contractors also support local communities and help ensure that the country's national security industrial base is vibrant and robust. Taking action to improve the ability of small businesses to participate in federal procurement would strengthen small businesses, communities, and the broader economy.

# Sources

Non-attributed small business owner comments are from two roundtables with small business contractors hosted by BPC and Goldman Sachs 10,000 Small Business Voices

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