# The Impact of Federal Government Business Policy on Minorities and Women Entrepreneurs

**Shelton Rhodes**, Ph.D.
srhodes@bowiestate.edu
Bowie State University

**Abstract**

The federal government purchases over 200 billion dollars worth of goods and services every year. Substantive federal legislation has been passed in an effort to encourage and to develop federal contracting entrepreneurship ventures by minorities, women, and veterans. In FY 2003 the federal government purchased goods and services valued at approximately $100 billion dollars from small businesses. Providing a fair share of government contracting dollars to minorities, women, and veterans is important from an equity and economic perspective. Some of the leading women and minority entrepreneurs in the country focus on selling goods and services to the federal government. This study will examine the effectiveness and implications of select federal business policies to increase federal contracting entrepreneurship opportunities for minorities, women, and veterans. Small Business Administration data and policies provide a wealth of information on the level of federal procurement to minority and female owned business. This research is significant because federal procurement is a significant driver of our national economy. Many personal fortunes in this country can be linked to federal procurement. Providing services and goods to the federal government was a crucial catalyst for the aircraft based fortune of the legendary Howard Hughes. Federal government business policy makes a difference in the extent that minorities and women business can compete for federal contracts in the open market.

## Introduction

The Small Business Act of July 30, 1953 passed by Congress created the Small Business Administration, whose function was to "aid, counsel, assist and protect, insofar as is possible, the interests of small business concerns." The charter also stipulated that the SBA would ensure small businesses a "fair proportion" of government contracts and sales of surplus property. SBA has a long list of accomplishments in aiding small businesses.

> Nearly 20 million small businesses have received direct or indirect help from one or another of those SBA programs since 1953. In fact, SBA's current business loan portfolio of roughly 219,000 loans worth more than $45 billion makes it the largest single financial backer of U.S. businesses in the nation. Since 1958, SBA's venture capital program has put more than $30 billion into the hands of small business owners to finance their growth. In 2004, the SBA backed more than $12.3 billion in loans to small businesses. More than $1 billion was made available for disaster loans and more than $40 billion in federal contracts were secured by small businesses with SBA's help. SBA continues to branch out to increase business participation by women and minorities along new avenues such as the minority small business program, microloans and the publication of Spanish language informational materials.[1]
>
> Providing services and products to the federal government is a crucial catalyst for many successful businesses. Many Fortune 500 companies, such as Lockheed Martin and Boeing, specialize in providing products and services to the federal government. Large companies hire

[1] SBA website, www.sba.gov

former high ranking military officers and former high ranking civil service personnel to lobby Capital Hill to bring in lucrative contracts. A former US Secretary of Defense worked for Halliburton for one of the largest defense contractors in the country. Hurricane Katrina has caused a national disaster but it has also created the opportunity for entrepreneurs and for existing businesses to get wealthy by winning federal contracts to rebuild New Orleans. Also the Iraq War is a bonanza for businesses receiving federal contracts. Federal government business policy makes a difference in who gets a share of the lucrative government contracting pie.

**The 8(a) Small Business Administration Business (SBA) Development Program**

This paper will focus primarily on the 8(a) Small Business Development program which was passed by Congress in 1968. The intent of the program was to level the playing field for minority businesses in competing for federal contracts. The 8(a) Small Business Development program passed under the Nixon administration. Parren Mitchell the first black congressman from the state of Maryland played a critical role in advocating the passage of this landmark legislation. The 8(a) Small Business Development program is an excellent example of federal government business policy that has impacted the growth of small minority and female owned businesses. 8(a) regulations specify SBA business development assistance to 8(a) firms. The most important assistance is contract set-asides that only 8(a) firms can compete for. Other SBA business development assistance to 8(a) firms include contract support, financial, assistance, training in developing business strategies to enhance a firm's ability to compete for contracts, training in transitional business planning, and assistance in forming joint ventures with other firms. Certified 8(a) firms have nine years to participate in the program. The first stage covering years 1 through 4 is a developmental and the second stage covering years 5 through 8 is transitional. During the transitional stage, firms are required to meet non-8(a) business contract levels in an effort to ensure that firms can operate after graduating from the program.

**Not a Handout**

Although many of its staunch opponents criticize the program as being a handout designed to award governmental contracts to undeserving businesses, the purpose of the Small Business Administration's 8(a) business-development program is to assist eligible small disadvantaged business concerns to compete in the American economy through business development. Even though the program provides its participants with a unique contracting status, each firm must still compete with and outmaneuver an array of other hungry competitors in order to receive the 8(a) contracts. The intent of the program is not to provide firms with an unfair advantage over other firms; instead it allows them to achieve the footing necessary to compete at an equal level with others in the marketplace. Once firms are on this level playing field, it is up to them to battle for the business they desire.

**Program Eligibility**

Generally speaking, to be eligible for admission to the 8(a) program, an entity must be a small business that is unconditionally owned and controlled by one or more socially and economically disadvantaged individuals who are of good character and are citizens of the United States, and the business must demonstrate the potential for success.

Participants can receive sole-source contracts up to a ceiling of $3 million for goods and services and $5 million for manufacturing. Although the SBA helps 8(a) firms build their competitive and institutional know-how, the agency also encourages them to participate in competitive acquisitions.

Recent changes permit 8(a) firms to form joint ventures and teams to bid on contracts. This approach enhances the ability of 8(a) firms to perform larger prime contracts and overcome the effects of contract bundling – the combining of two or more contracts into one large contract. Used effectively, this new trend could help disadvantaged firms compete in acquisition-funneling environments.

Program goals require 8(a) firms to maintain a balance between their commercial and government business. There is also a limit on the total dollar value of sole-source contracts that an individual participant can receive while in the program: $100 million, or five times the value of its primary SIC code. The overall program goal is to graduate firms that will go on to thrive in a competitive business environment.

To achieve this end, SBA district offices monitor and measure the progress of participants through annual reviews, business planning, and systematic evaluations. Participants in 8(a) may take advantage of specialized business training, counseling, marketing assistance, and high-level executive development provided by the SBA and its resource partners. They may also be eligible for assistance in obtaining access to surplus government property and supplies, SBA-guaranteed loans, and bonding assistance.

***How small is small?***

The SBA defines a small-business concern as one that is independently owned and operated, is organized for profit, and is not dominant in its field. Depending on the industry, eligibility is based on the average number of employees for the preceding 12 months or on sales volume averaged over a three-year period.

A number of stipulations exist that depend on both industry sector and the types of products or services rendered. For manufacturing, the maximum number of employees may range from 500 to 1500. For wholesaling, the maximum number of employees ranges from 100 to 500. In the services industry, annual receipts may not exceed $21.5 million. In the retail market, annual receipts may not exceed $21.0 million. In general and heavy construction, annual receipts may not exceed $17 million. In special trade construction, annual receipts may not exceed $7 million. In agriculture the maximum annual receipts range from $0.5 to $9.0 million, depending on the type of agricultural product.

***When are you at a disadvantage?***

According to the SBA, socially disadvantaged individuals are those who have been subjected to racial or ethnic prejudice or cultural bias because of their identity as members of a group. The social disadvantage must stem from circumstances beyond their control. Currently members of the following ethnic groups are classified as socially disadvantaged: black Americans, Hispanic Americans, Native Americans, and Asian Pacific Americans.

An individual who is not a member of a designated group must establish social disadvantage on the basis of a preponderance of evidence. Generally, preponderance is evidence of quality and quantity which leads the decision maker to conclude that the existence or truth of the fact asserted is more probable than not.

Economically disadvantaged individuals are socially disadvantaged individuals whose ability to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities. The SBA evaluates the economic disadvantage of an individual by looking at the individual's net worth, which, after excluding the individual's equity in the firm and the equity in the primary residence, may not exceed $250,000. In evaluating economic disadvantage, the SBA also considers the individual's average income, the fair market value of all assets, access to credit and capital, and the financial condition of the applicant firm.

***Who is the owner, and who has the power?***

The SBA also requires that at least 51 percent of the firm be directly and unconditionally owned by socially and economically disadvantaged individuals. As a result there are two general ownership restrictions on nondisadvantaged individuals and firms.

First, a nondisadvantaged individual may simultaneously hold up to 10 percent ownership interest in any number of 8(a) firms in the developmental stage of program participation and up to 20 percent interest in any number of 8(a) firms in the transitional stage of program participation.

Second, a nonparticipant concern in the same or similar line of business may own up to 10 percent of an 8(a) firm in the developmental stage and up to 20 percent of an 8(a) firm in the transitional stage. Former 8(a) participants or a principal of a former participant, with the exception of those that have been terminated from the 8(a) program, may own up to 20 percent of an 8(a) firm in the developmental stage and up to 30 percent of an 8(a) firm in the transitional stage.

The SBA is also very clear about the fact that control is not the same as ownership. Although both control and ownership may reside in the same person, control includes both strategic policy setting and the day-to-day management and administration of business operations by disadvantaged individuals. The SBA requires that the disadvantaged individual controlling the firm have management experience necessary to run the firm. The disadvantaged individual must also demonstrate that he or she has the ultimate managerial and supervisory control over those in the firm with the technical or licensing expertise. However, if the critical license is held by a nondisadvantaged individual who has an equity interest in the applicant firm, the SBA may find that the nondisadvantaged individual controls the firm.

There are six situations in which the SBA may determine that disadvantaged individuals control a board of directors:

- If a single disadvantaged individual owns 100 percent of all issued and outstanding voting stock of an applicant firm, regardless of the composition of the board of directors.
- If a single disadvantaged individual owns at least 51 percent of issued and outstanding voting stock of the applicant firm and is a legally elected voting member of the board of directors, and if no super majority voting requirements exist for shareholders to approve corporate actions.
- If a single disadvantaged individual owns at least 51 percent of all issued and outstanding voting stock of the applicant firm, is a legally elected voting member of the board of directors, and owns at least the percentage of voting stock needed to overcome the super majority voting requirements that exist for shareholders to approve corporate actions.
- If more than one disadvantaged individual owns at least 51 percent of all issued and outstanding voting stock of the applicant firm, if they are all legally elected voting members of the board of directors, if no super majority voting requirements exist for shareholders to approve corporate actions, and if the disadvantaged shareholders can demonstrate they have made enforceable arrangements to permit one of them to vote the stock of all as a block to nondisadvantaged shareholders' actions without holding a shareholder meeting.
- If more than one disadvantaged individual owns at least 51 percent of all issued and outstanding voting stock of the applicant firm; if all are legally elected voting members of the board of directors; if, in total, all own at least the percentage of voting stock needed to overcome the super majority voting requirements which exist for shareholders to approve corporate actions; and if the disadvantaged individuals can demonstrate that they have made enforceable arrangements to permit one of them to vote the stock of all as a block to nondisadvantaged shareholders' actions without holding a shareholder meeting.
- If the disadvantaged individuals can control the formation of a quorum for the purpose of holding a board meeting and have a majority vote at board meetings, either through the actual number of voting directors or through weighted voting, where permitted by state law.

Although nondisadvantaged individuals may be involved in the ownership and management of an applicant firm, they may not exercise actual control, be a former employer of the disadvantaged owner, or receive compensation exceeding that of the disadvantaged owner. If one or more of these situations exist, the nondisadvantaged individual will be found to control the firm.

In evaluating the potential for success, the SBA evaluates the technical and managerial experience of the applicant firm's managers, its operating history, its ability to access credit and capital, its financial capacity, its record of performance, and whether or not employees hold the required licenses, when applicable.

***Other limitations***

In order to participate in the program, a firm must routinely be in business two full years prior to applying for admission. However, if a firm has not been in business for two years and still would like to pursue program admission, there is a chance of admittance if it can undoubtedly meet all of the following criteria:

- The individual(s) upon whom eligibility is based must have substantial business management experience.
- The individual(s) must be able to demonstrate the technical experience to carry out the business plan with a substantial likelihood for success.
- The individual(s) must have adequate capital to sustain operations and carry out the business plan.
- The individual(s) must have a record of successful performance on contracts from governmental or nongovernmental sources in its primary industry category.
- The individual(s) must be able to demonstrate the ability to timely obtain the personnel, facilities, and equipment, and to demonstrate any other requirements needed to perform on contracts if admitted.

The SBA determines character by ascertaining that the applicant and its principals have not been engaged in criminal or civil infractions, whether or not they resulted in suspensions, incarcerations, or adverse judgments.

**Program Participation**

If a firm feels that it meets the requirements and is interested in participating in the program, contacting the local SBA district office is the first step. An SBA representative should be able to answer general questions over the telephone, and some district offices also have 8(a) orientation workshops designed to provide additional information regarding the eligibility requirements and to review various SBA forms.

Although consultants are available to help complete the 8(a) application, there is no need to pay anyone to prepare it. The SBA intentionally designed the application forms so the applicant can complete it, and the application process is intended to assure that each applicant receives a fair review.

Like any governmental program, the firm must agree to comply with the regulations once it is admitted. All 8(a) participants receive a program term of nine years from the date of the SBA's approval letter certifying the concern's admission to the program.

The participant must maintain its program eligibility during its tenure in the program and must inform the SBA of any changes that would adversely affect its program eligibility. A firm that completes its nine-year term is deemed to have graduated from the program.

The nine-year program term may be shortened only by termination, early graduation, or voluntary graduation. The nine years are divided into two stages: a four-year developmental stage and a five-year transitional stage. The developmental stage is designed to help 8(a)-certified firms overcome their economic disadvantage by providing business-development assistance. The transitional stage is designed to help participants overcome the remaining elements of economic disadvantage and to prepare them for leaving the 8(a) program.

Participants must also agree to actively participate in an annual review. As part of this review, each firm must submit the following to the servicing district office, along with any other information the SBA office requests:

- A certification that it meets the 8(a) program eligibility requirements;
- A certification that there have been no changed circumstances which could adversely affect the participant's program eligibility;
- Personal financial information for each disadvantaged owner;
- A record from each individual claiming disadvantaged status regarding the transfer of any assets for less than fair market value to any immediate family member, or to a trust of which an immediate family member is a beneficiary, within two years of the date of the annual review;
- A record of all payments, compensation, and distributions, including loans, advances, salaries, and dividends made by the participant to each of its owners, officers, and directors, or to any person or entity affiliated with such individuals;
- IRS Form 4506 (Request for Copy or Transcript of Tax Form).

When a participant fails to provide documentation for its annual review, the SBA may elect to terminate a firm from the program.

**Giving Back**

Upon graduation, firms are routinely asked to serve as mentors to 8(a) participants currently in the development stage. The mentor-protégé program enhances the capability of 8(a) participants to compete more successfully for federal government contracts. The program encourages private-sector relationships and expands the SBA's efforts to identify and respond to the developmental needs of 8(a) clients.

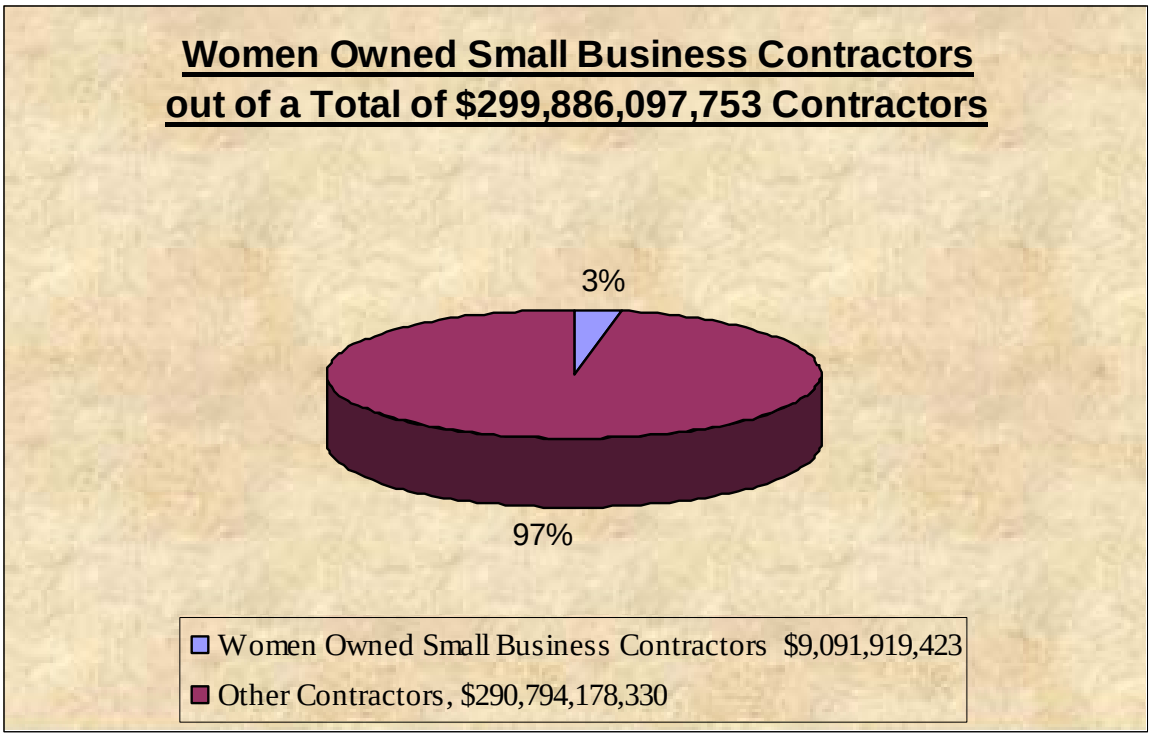
Like any mentor-protégé business relationship, mentors are expected to provide technical and management assistance, financial assistance in the form of equity investments and/or loans, subcontract support, and assistance in performing prime contracts through joint-venture arrangements with 8(a) firms.

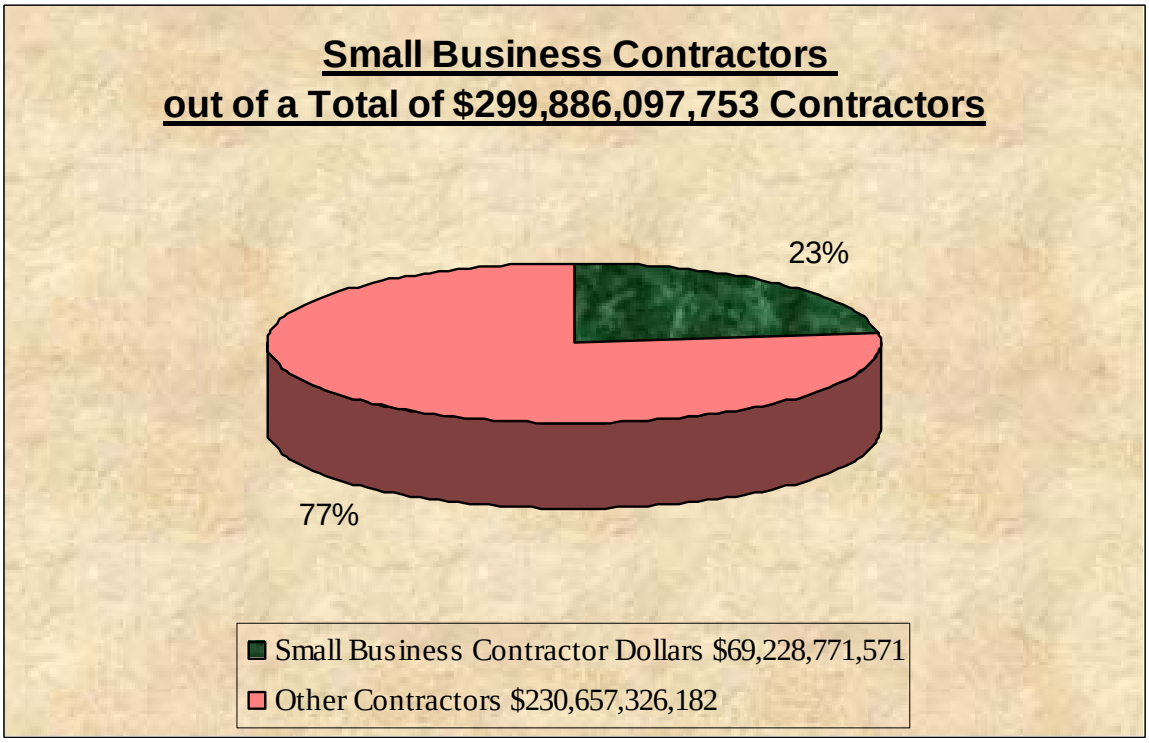
The mentor can be a business that has graduated from the 8(a) BD program, a firm in the transitional stage of the program, or a small or large business. A mentor must have the capability to assist the protégé and must make a commitment for at least a year. In addition, it must demonstrate that it enjoys favorable financial health, including profitability for at least the last two years; it must be a federal contractor in good standing; and it must be able to provide valuable support to a protégé through lessons learned and practical experience gained from the 8(a) program or its general knowledge of government contracting**.**

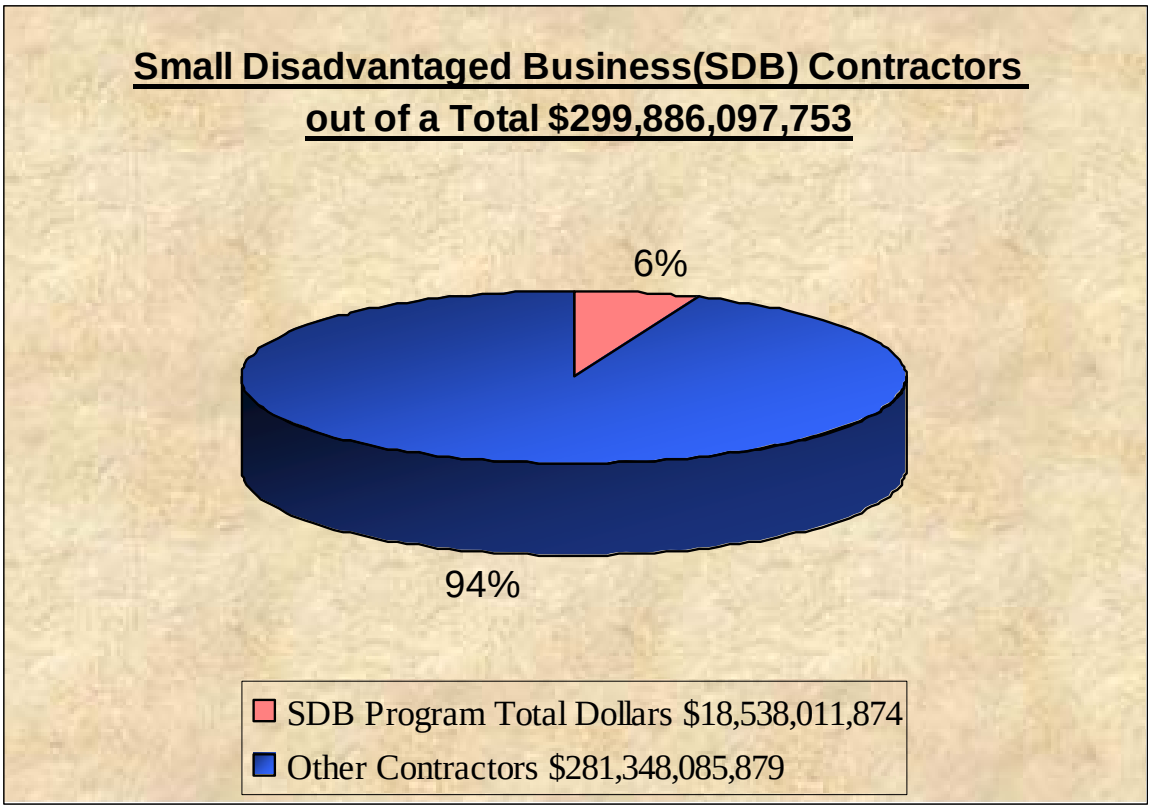
**Data Summary Federal Procurement Data System Small Business Goal Report Actions Reported Between Fiscal Year 2004(Q1) and Fiscal Year 2004(Q4)**

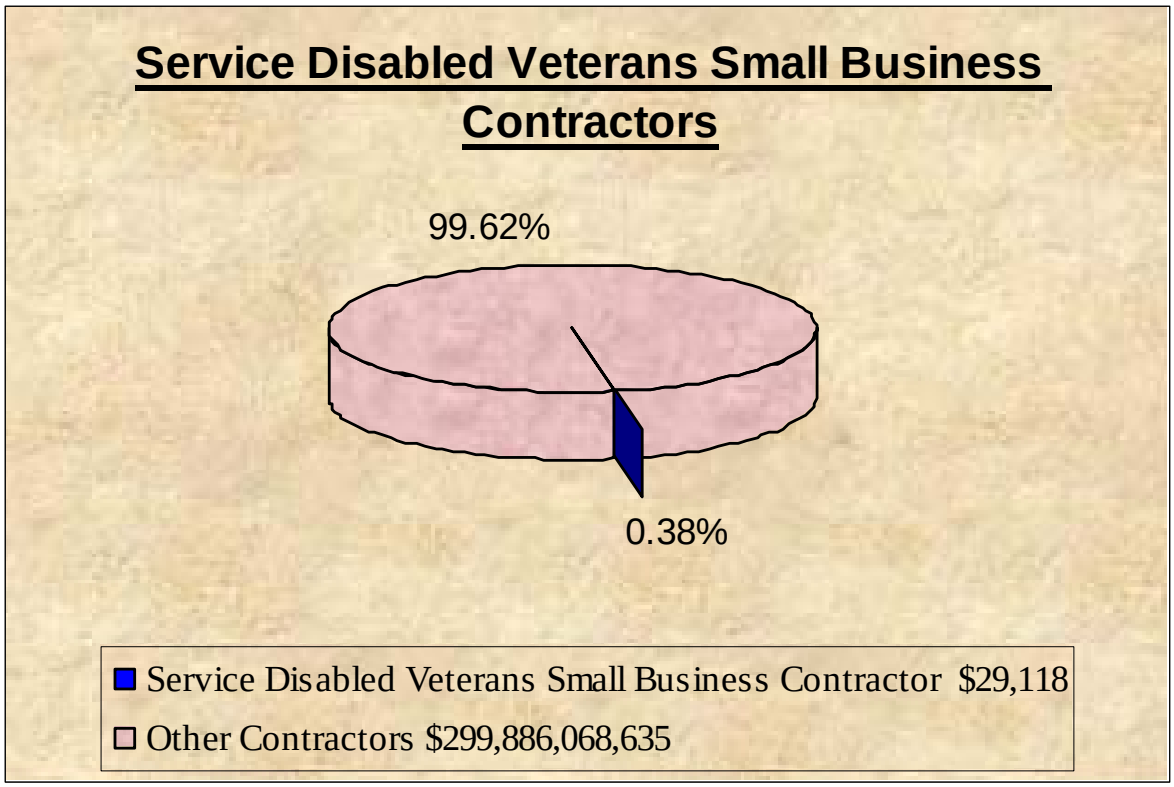
Federal business policy requires that federal contracting dollars be set-aside for a small business. The Small Business Administration defines business size. A size standard is the largest that a for-profit concern can be and still qualify as a small business for federal government programs. In general, size standards are the average annual receipts or the average employment of the firms. The U.S. government is the world's largest buyer of products and services. Purchases by military and civilian installations amount to nearly $200 billion a year, and include everything from complex space vehicles to janitorial services to cancer research. In short, the government buys just about every category of commodity and service available.

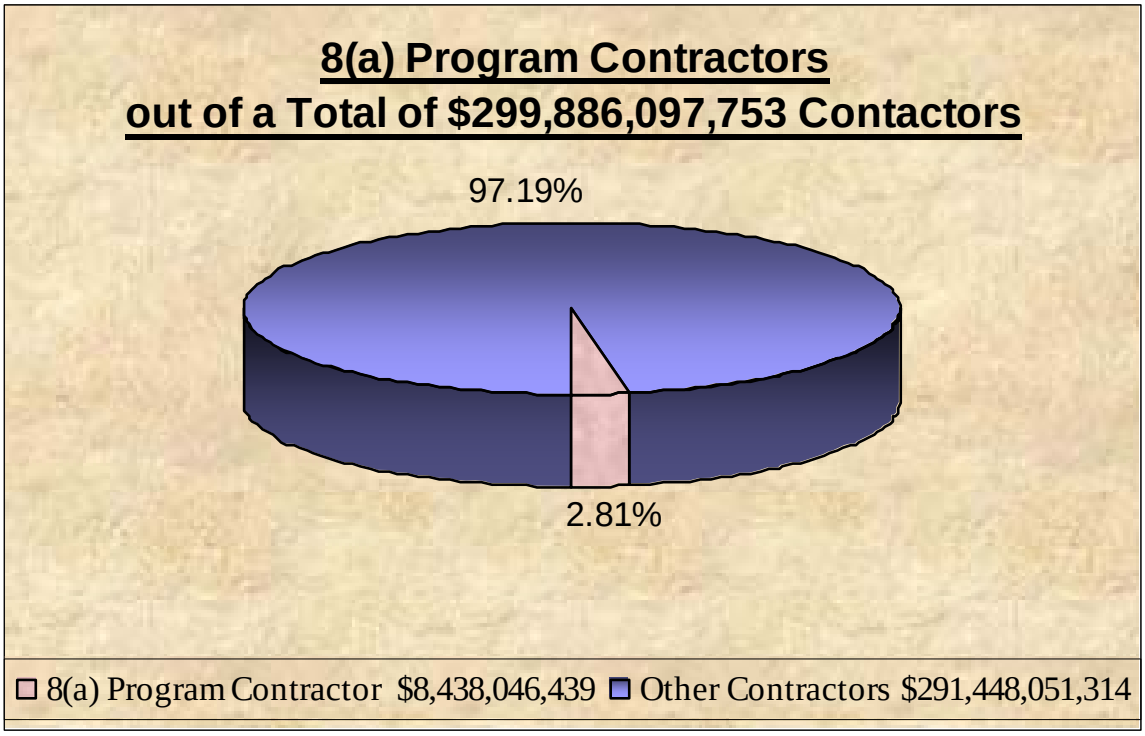
By law, federal agencies are required to establish contracting goals, such that 23% of all government buys are intended to go to small businesses. In addition, contract goals are established for women-owned businesses, small disadvantaged businesses, firms located in HUBZones and service disabled veteran-owned businesses.


Women Owned Small Business Contractors
out of a Total of $299,886,097,753 Contractors
3%
97%
Women Owned Small Business Contractors $9,091,919,423
Other Contractors, $290,794,178,330


Small Business Contractors
out of a Total of $299,886,097,753 Contractors
23%
77%
Small Business Contractor Dollars $69,228,771,571
Other Contractors $230,657,326,182


Small Disadvantaged Business(SDB) Contractors
out of a Total $299,886,097,753
6%
94%
SDB Program Total Dollars $18,538,011,874
Other Contractors $281,348,085,879


Service Disabled Veterans Small Business Contractors
99.62%
0.38%
Service Disabled Veterans Small Business Contractor $29,118
Other Contractors $299,886,068,635


8(a) Program Contractors
out of a Total of $299,886,097,753 Contactors
97.19%
2.81%
8(a) Program Contractor $8,438,046,439
Other Contractors $291,448,051,314

**Conclusion**

The Data Summary Federal Procurement Data System Small Business Goal Report Actions Reported Between Fiscal Year 2004(Q1) and Fiscal Year 2004(Q4) information indicates while federal policy has an impact on the amount of federal dollars going to small business, minority, female, and veteran owned business are reaping only a small slice of the billion dollar government contracting pie. However, without proactive federal business policy the share would be even smaller if not non existent. The benefits of the 8(a) Program were summarized in the 2000 U.S. Small Business Administration report to the U.S. Congress. The long term business development efforts of the 8(a) program since its 1968 inception include contract actions worth $88.4 billion dollars. Employment by 8(a) firms was estimated at 140,659 persons during fiscal year 2000. The 8(a) program has many shortcomings in spite of its success. Many 8(a) companies were formed to be past through contract vehicles for large companies. A July 2000 GAO report found that over 48 percent of the firms in the 8(a) program for at least 2 years had obtained at least one 8(a) contract. Fifty eight percent of surveyed firms indicated that they were dissatisfied with the amount of contracting opportunities afforded by the program.

References

Carvin, M, Clegg, R. and Ryland, W., (1993) Racial Preferences in Government Contracting, Washington, D.C. : National Legal Center for the Public Interest.

Clark, M and Moutray, C., (2004, October 21-23). *The Future of Small Businesses in the U. S. Federal Government Marketplace,* presented at the International Public Procurement Conference, Ft. Lauderdale, FL.

Fretty, P. and Rhodes, S. (August 2004) A Piece of the Pie, Outskirts Press Inc., Denver, CO.

Joel Popkin and Company. (2001 December 14). Small Business Share of Economic Growth. Washington, DC: Office of Advocacy, U.S. Small Business Administration.

Nagle, James F., (1999) A History of Government Contracting, 2nd ed. Washington D.C. George Washington University Law School, Government Contracts Program.

U.S. General Accounting Office. (2000) Small Business Expectations of Firsm in SBA's 8(a) Program Are Not Being Met, (GAO/T-RCED-00-261), Washington DC

U.S. Small Business Administration. (2000) The Report to The U.S. Congress on Minority Small Business and Capital Ownership Development For Fiscal Year 2000, Small Business Administration, Washington, DC.