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U.S. House of Representatives Committee on Small Business

"Beyond the Size Standards: Sustainability of Small Business Graduates"

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I. Introduction to GWU Law School's Government Procurement Law Program

Established in 1960, the Government Procurement Law Program at The George Washington University Law School is the only one of its kind in the United States. A broad range of faculty teach, speak and write on federal contract formations and administration, anti-corruption issues, bid protests, claims, cost and pricing, small business programs, procurement reform initiatives, and international and comparative law. The procurement law program at GWU Law School offers unparalleled faculty resources, course offerings, and professional development opportunities. The program's faculty bring with them years of experience in the federal government and in the private sector. In addition to our classes, a sponsored moot court competition and the *Public Contract Law Journal*, the program also hosts colloquia and symposia addressing evolving issues in procurement reform, and presenting esteemed speakers from government, industry, academia and private practice.

II. The Competitive Problem for Mid-Sized Firms in the Procurement Market

The problem the Committee is addressing today -- the problem of mid-sized firms in the government marketplace -- really has two aspects. First, there is the problem of "graduating" small businesses, which grow up under the protection of various small business preference programs and then must compete as mid-sized firms, without any preferences or protections. Second, and more broadly, mid-sized firms face special competitive obstacles in the federal procurement market, a market which sometimes favors the largest firms, in part because of its steep barriers to entry.

Sustaining Small Businesses That Grow Beyond Preference Programs: A key problem that has emerged in the U.S. small business program is how to sustain growth in those small businesses, nurtured by the U.S. small business preferences in procurement, which grow into "medium"-sized firms and so are no longer eligible for small business preferences. This issue has been an open one for many years. *See, e.g.*, N. Eric Weiss, *Possible Small Business Issues in the 110th Congress*, Congressional Research Service (CRS) Report No. RS22589, at 4 (Feb. 27, 2008).[1]

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[1] This issue of constrictive size standards is not new to the 112th Congress. For example, the Congressional Research Service reported, in 2008:

> Revisions to the Definition of Small. There is no uniform definition of "small" business. The SBA determines a *size standard* on an industry-by-industry basis, weighing the number and size of firms in an industry, the degree of competition, barriers to entry, and start up costs. The size standard must be small enough exclude any dominant firms in the industry. Depending on the industry, the SBA sets the size standard based on a firm's number of employees or revenues. For example, the size standard for new single family home construction businesses is $31 million of annual revenue, and for iron and steel mills the standard is 1,000 employees.5
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> **There have been proposals to increase the size standard to make larger businesses eligible for small business programs.** For example, the Department of Defense (DOD) has suggested increasing the size standards because defense contracts frequently push the winning small business over the size standard. This limits a small business to one DOD contract, and the Pentagon would like the flexibility to award additional relatively large contracts to a firm. Many small business advocacy groups have opposed this. On the other

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General Competitive Problems for Mid-Sized Firms: There is also a perception that mid-sized firms in general face special difficulties in the government procurement marketplace, because those mid-sized firms do not have access to the preferences enjoyed by small businesses and because the mid-sized firms lack the economies of scale, and sheer economic muscle, of the largest prime contractors.

To even the competitive playing field for those mid-sized firms, the Obama administration launched the **"Business Breakthrough Program"** in March 2011, through the U.S. General Services Administration (GSA). *See* Press Release: *White House and GSA Launch New Program to Give Companies a Leg Up in Federal Contracting: New GSA Program to Help Companies Secure and Keep Government Contracts*, GSA No. 10780, Mar. 10, 2011, http://www.gsa.gov/portal/content/241485. The program is to provide training and outreach, but *not* any special preferences. The "Business Breakthrough Program" targets "midsize firms that can get lost in the shuffle between industry goliaths and undersized firms that qualify for Small Business Administration socioeconomic set-aside contract opportunities," according to GSA. *See* Robert Brodsky, *GSA Launches Program To Educate New and Emerging Contractors*, Gov. Exec., Mar. 10, 2011, http://www.govexec.com/dailyfed/0311/031011rb2.htm. According to one White House adviser involved with the program, "'We have heard from medium-sized businesses that they are falling through the cracks here. They did not fit the SBA programs, which are geared toward how to get certified as an 8(a) [small business contractor] or as service disabled or women-owned.'" *Id. (*quoting Ginger Lew, senior adviser to the White House National Economic Council). According to GSA Associate Administrator Jiyoung Park, the goal of the program is "'to increase competition in contracting governmentwide,'" though without any new preference for mid-sized firms. *Id.* The Business Breakthrough Program, which is essentially an intensive training program, emphasizes GSA's "Mentor-Protégé" Program, and is described at http://www.gsa.gov/portal/content/239329.

Mentor-protégé programs, which are sponsored in different forms by different agencies, are generally designed to accommodate both small businesses (the "protégés") and the larger firms that enter into formal agreements to assist those small businesses (the "mentors"). The General Services Administration notes that its mentor-protégé program seeks "to assist small business, including small disadvantaged business, veteran-owned, service-disabled veteran-owned, HUBZone, and women-owned small business in enhancing their capabilities to perform contracts and subcontracts for GSA and other Federal agencies." Successful mentor-protégé arrangements, GSA has said, "represent opportunities for creating access for small business to GSA contracts and awards." 74 Fed. Reg. 41060, 41061 (Aug. 14, 2009).

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> hand, there are also proposals to reduce the size standard, in order to eliminate larger small businesses from small business programs.
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> H.R. 1332, as reported out of committee on May 25, 2007, would direct the SBA to create a size standard based on maximum tangible net worth and average net income in addition to the current standard based on either revenue or number of employees.

Id. at 4 (emphasis added).

GSA's mentor-protégé program has been criticized for offering too few incentives for larger businesses to join the program. 74 Fed. Reg. at 41061; *see also* General Services Acquisition Manual (GSAM) 519.7004 (discussing incentives for prime contractors to join mentor-protégé program); Anthony Eiland, GSA, Presentation: *The GSA Mentor-Protégé Program*, http://www.gsaopeningdoors.com/pdfs/Eiland,%20Tony%20GSA.pdf (discussing practical and legal benefits of joining program). The Department of Defense's mentor-protégé program, which is statutorily authorized, in contrast provides greater incentives for mentor firms to join. *See generally* U.S. Government Accountability Office, Report No. GAO-11-548R *Federal Mentor-Protégé Programs* (June 15, 2011) (discussing various agencies' programs); *GSA Mentor-Protégé Master Participation List*, http://contacts.gsa.gov/graphics/staffoffices/Mentor-ProtegeParticipationList_10AUG11-EXTERNAL.doc (GSA reports 76 mentor-protégé agreements);. The legislative proposals the Committee is discussing today, which would create special procurement preferences for participants in mentor-protégé programs, would offer strong new incentives to join those programs.

III. The Proposed Legislation

The Committee's hearing today will examine proposals for a medium-sized business program, with a specific focus on H.R. 1812, the Small Business Growth Act, and other legislative proposals. According to the Committee's hearing notice, the hearing is to analyze the desirability of a medium-sized business program, the effect of such a program on current small firms, and the fundamental issues any such program must address.

Today's hearing focuses, as noted, on H.R. 1812, introduced by Congressman Gerry Connolly (D-VA), which would address the problem as follows:

- H.R. 1812 would direct the Administrator of General Services to establish a five-year **small business growth pilot program**.
- **To be eligible to participate in the program**, an entity would have to:
    - be **enrolled as a mentor or participating in the GSA's Mentor-Protege program**;
    - **if participating as a mentor**,[2] have at least one protege that was a small business;
    - have **fewer than 1,500** employees; and
    - **not be a small business**.

[2] While technically a protégé would also qualify for the program, because mentor-protégé programs typically accommodate small businesses as protégés, and small businesses could *not* qualify for the preference under H.R. 1812, the discussion below will assume that *mentors*, not protégés, would take benefit from the program in the first instance.

- **Competitions for GSA contracts could be limited to entities eligible** for the program **if**:
    - The anticipated award price of the contract (including options) was reasonably expected to **exceed the simplified acquisition threshold** (currently generally $150,000, per FAR 2.101, 48 CFR § 2.101);
    - The contract would **otherwise likely be awarded to other than a small business**;
    - There was a reasonable expectation that **at least two program participants** would submit offers; and,
    - The contract could be awarded at a **fair market price**.
- **Contracting officers would be required to consider awarding contracts under the pilot program**, before awarding the contract under full and open competition, and could be required to report as to why contracts were or were not awarded under the restricted program.

Congressman Mike Rogers (R-Ala.) offered an amendment to Title VIII of H.R. 1540, the pending defense authorization bill, as reported, which would establish a similar program in the Defense Department, though there for contracts over $25 million.

Other pending legislation would also address small business size standards. *See* H.R. 585 (would amend the Small Business Act to provide for the establishment and approval of small business concern size standards by the Chief Counsel for Advocacy of the Small Business Administration).

IV. Key Issues to Address in Proposed Legislation

While the legislative proposals outlined above are relatively modest in scope, as noted they stem from a much broader question: how to address the special hurdles that medium-sized firms face in the procurement marketplace. The proposed legislation, and any broader remedial legislation, will have to address a number of questions, including but not limited to:

- Should a new preference category of "medium-sized" businesses be created, or should existing "small business" categories be expanded?
- Should acceptable size for these firms be a uniform standard -- say, 1500 or 2500 employees -- or should the size standards vary?
- Should affiliation rules apply, to disqualify firms that are affiliated with other firms and so form much larger joint enterprises?
- Should "size" protests be allowed, so that competitors and others may challenge firms that are apparently improperly benefiting?

- Will the "Rule of Two," which says that eligible procurements must be reserved for small business if it appears two or more small businesses will compete, apply?

- Should there be a limit on the number of contracts that can be awarded?

- Would benefiting firms have a priority in preference?

- Will these initiatives enhance competition? Create jobs?

The discussion below addresses these questions. As the discussion below reflects, because international trade obligations suggest that Congress should *not* create a new category for "medium-sized" businesses, but instead should expand the benefits available through existing small business categories and programs, many of the questions are resolved by resorting to the existing legal framework for small business preferences.

A. Because of International Trade Obligations, Legislation Should Expand the Definition of "Small" Business, or Encourage Mentor-Protégé Programs, Rather Than Creating New Category of "Medium-Sized" Enterprises

A threshold question is whether larger firms' access to procurement contracts -- the access of those firms that exceed the traditional size standards for "small businesses" -- should be resolved by expanding the definition of "small" businesses, or by creating a new category called "medium-sized" enterprise, as European governments have done. H.R. 1812 does not squarely present this issue -- the bill does not create a new "medium" category of firms, but instead creates a special pilot program for certain larger-than-small firms -- but this issue is likely to arise as policy discussions continue.

The answer to this question -- whether to treat the benefiting firms as relatively large "small" firms by expanding the size standards or as "medium-sized" firms -- may lie buried in a World Trade Organization (WTO) agreement, the plurilateral Government Procurement Agreement (GPA).[3]

The WTO members that join the GPA agree, with conditions, to open their procurement markets to vendors from other members of the GPA. Under the agreement, signatory nations agree (a) not to discriminate against other members' vendors, (b) to treat vendors from other member states as they would their own vendors, and (c) to follow certain procedural minima in conducting covered procurements. The United States is a member of the GPA, as are many of the United States' key trading partners, including the 27 member states of the European Union, Hong Kong/China, Iceland, Israel, Japan, Korea, Liechtenstein, Norway, Singapore, and Taiwan (Chinese Taipei). China is negotiating its accession to the GPA, and India is likely to follow behind China in joining the agreement. The GPA, which has been (in various forms) an important part of U.S. trade policy for many decades, is arguably the cornerstone to opening world procurement markets for U.S. exporters over the coming years. *See generally* Sue

[3] For background on the GPA, see the Office of the U.S. Trade Representative website, http://www.ustr.gov/trade-topics/government-procurement/wto-government-procurement-agreement.

Arrowsmith & Robert Anderson, *The WTO Regime on Government Procurement* (2011); Christopher R. Yukins & Steven L. Schooner, *Incrementalism: Eroding the Impediments to a Global Public Procurement Market*, 38 Geo. J. Int'l L. 529 (2007), *available at* http://ssrn.com/abstract=1002446.

Each nation that joins the GPA reserves certain elements of procurement from the agreement's free trade obligations. The United States, when it joined the GPA, made a number of reservations, including one vitally important to our discussion today: the United States reserved its right to give a preference to U.S. small businesses, even if that means discriminating against foreign vendors seeking to sell to federal agencies. The reservation, which is set forth in the United States' General Notes to the GPA, states (in relevant part) that **"this Agreement will not apply to set asides on behalf of small and minority businesses."** Other GPA member nations have not made similar reservations to protect their small businesses.

The United States thus has *not* reserved a right to discriminate against foreign vendors from GPA nations with regard to *medium*-sized businesses. A new, unreserved U.S. preference for procurement from medium-sized businesses also could undermine the United States' negotiating position with China and other developing nations, which are seeking broader protections for their own emerging industries before they agree to join the GPA. Moreover, were the United States to create a preference for medium-sized businesses, that preference could trigger a challenge by the European Union, or other GPA members, under the WTO disputes process. Finally, a new preference for medium-sized enterprises could prompt the European Union to demand that its member nations, too, be allowed to extend preferences to small and medium-sized enterprises (SMEs).

The European Union has long criticized the United States' procurement preferences for small businesses, arguing that the preferences in effect wall off European vendors from a major portion of the U.S. federal procurement market. In a 2009 report, for example, European policymakers wrote:

> The active promotion of small businesses is a common concern for the EU and the US. The EU is, however, concerned that the US "set-aside" measures and their exemption from the GPA favour US industry and have exclusionary effects to the detriment of foreign competitors.

European Union, *Market Access Database* (updated Mar. 1, 2009), http://madb.europa.eu/madb_barriers/barriers_details.htm?barrier_id=960300&version=5.

The European comments both reflected concern that small business preferences are excluding foreign vendors *and* hinted at where the European Union may go: the European Union may demand that it, too, be allowed to erect preferences to protect *European* SMEs from U.S. and other foreign exporters. *See* Max V. Kidalov, *Small Business Contracting in the United States and Europe: A Comparative Assessment*, 40 Pub. Cont. L.J. 443 (2011). European preferences "walling off" the market currently occupied by small- and medium-sized enterprises in European procurement could have a substantial impact on U.S. exporters, because a very large

share of that market -- an estimated 42% of all European prime contracting in 2005, for example -- goes to SMEs. *Id.* at 447 & n.12.[4] While the European Union has stopped short of creating SME procurement preferences to date (the European "Small Business Act"[5] issued last year instead sought merely to *facilitate* SMEs' participation in public procurement markets), a sweeping new U.S. preference for "medium-sized" enterprises could trigger a broader European political reaction.

Creating a new protected category of "medium-sized" enterprises may, therefore, raise serious issues under existing trade obligations. One way to avoid these issues would be to avoid creating a new category, and instead to work within the existing framework of small business preferences, perhaps as expanded by the pilot program contemplated by H.R. 1812.

B. One Option: Revising Size Standards

One policy option would be to revise the size standards for small businesses, to expand those standards to sweep up larger firms. *See* 13 C.F.R. § 121 (SBA size standards); FAR Part 19, 48 C.F.R. Part 19 (size standards in Federal Acquisition Regulation). This approach, which many advocates for medium-sized enterprises have urged, would not run afoul of the United States' trade obligations because the key trade agreement, the GPA, does not define "small business." While the European Union has generally lower guidelines for defining small business,[6] those guidelines are not binding on the European member states, and there is no binding international definition for "small business." The United States could, therefore, expand its definitions of protected "small" businesses, to sweep in larger firms.

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[4] Citing European Commission, *European Code of Best Practices Facilitating Access of SMEs to Public Procurement Contracts*, at 4, SEC (2008) working doc. (June 25, 2008), *available at* http://ec.europa.eu/internal_market/publicprocurement/docs/sme_code_of_best_practices_en.pdf.

[5] *Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions - "Think Small First" - A "Small Business Act" for Europe*, SEC(2008) 2101, *available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0394:FIN:EN:HTML*

[6] The European Union has published the following guidelines for defining SMEs:

Enterprise category	Headcount	Turnover	or	Balance sheet total
medium-sized	< 250	≤ € 50 million		≤ € 43 million
small	< 50	≤ € 10 million		≤ € 10 million
micro	< 10	≤ € 2 million		≤ € 2 million

Available at: http://ec.europa.eu/enterprise/policies/sme/facts-figures-analysis/sme-definition/index_en.htm. These are generally much lower that U.S. standards. A "small" business under U.S. federal standards, for example, typically may have as many as 500 - 1000 employees, rather than the 50 employees contemplated by the European standards, above. *Cf.* U.S. Small Business Administration, *Table of Size Standards*, *available at* http://www.sbaonline.sba.gov/idc/groups/public/documents/sba_homepage/serv_sstd_tablepdf.pdf.

Although adjusting the size standards to sweep up "medium-size" firms would not necessarily trigger a trade dispute, the issue could be highly contentious because of the collateral impact on firms that do, or do not, qualify under current or prospective size standards. *See, e.g.,* Press Release: *Grassroots Movement Blasts SBA's Proposed New Size Standards: Proposed Size Standards Are No Help to Small Businesses in Key Sectors* (Mar. 12, 2011), *available at* http://www.prweb.com/releases/2011/03/prweb5176354.htm. Because the size standards ultimately rest largely on factual, not legal, questions of industry size and composition, this analysis will not address potential revised standards in detail.

C. Second Option: Proposed Pilot Program to Create Preference for Mentor-Protégé Participants

This brings us, then, to the option before the Committee today: H.R. 1812, the proposed legislation to create a procurement preference for vendors in the GSA mentor-protégé program. Because foreign firms could, in principle, participate as mentors in the GSA program,[7] this option raises far fewer concerns regarding possible trade frictions. This approach does, however, raise other practical concerns, which were alluded to above.

1. Should Affiliation Rules Apply?

The first question we will address is whether to disqualify mentor-protégé arrangements that involve affiliations to form much larger joint enterprises -- whether through joint ventures or other forms of common control -- that would normally be disqualified as "small" businesses under the SBA affiliation rules regarding business size.

As currently drafted, H.R. 1812 does not necessarily trigger concerns under the affiliation rules. Under the current bill, a business that did not qualify as "small" could still take the benefit of the preference, so long as that business had fewer than 1500 employees and was a participant in the GSA mentor-protégé program.

Affiliation concerns could, however, be triggered in two different ways. First, a participating firm could affiliate itself with a third party, in order (for example) to gain access to that third party's capital resources. The proposed legislation should clarify whether a potential

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[7] The GSA acquisition regulation, GSAM 519.7006, Mentor Firms, sets the following minimum criteria for mentors, none of which *explicitly* discriminates against foreign prime contractors:

> (a) Mentors must be:
> (1) A large business prime contractor that is currently performing under an approved subcontracting plan as required by FAR 19.7 - Small business mentors are exempted; or
> (2) A small business prime contractor that can provide developmental assistance to enhance the capabilities of protégés to perform as contractors, subcontractors, and suppliers;
> (b) Must be eligible (not listed in the "Excluded Parties List System") for U.S. Government contracts and not excluded from the Mentor-Protégé Program under section 519.7014(b);
> (c) Must be able to provide developmental assistance that will enhance the ability of protégés to perform as contractors and subcontractors; and
> (d) Must provide semi-annual reports detailing the assistance provided and the cost incurred in supporting protégés.

"affiliation" of this kind could disqualify a mentor firm, if the affiliated entities, combined, had more than 1500 employees (the proposed cap under H.R. 1812). If the goal of the legislation is to foster previously "small" firms that have grown out of the small business preference programs, and to encourage broader competition by mid-market companies in federal procurements, then applying "affiliation" rules to the mentor firm would seem to make sense, to ensure that the program did not create a masked preference for much larger firms. Before this question is concluded, however, policymakers should assess the costs -- including the costs of more complicated governance -- if the affiliation rules are applied to participating firms in this way.

A second possible line of affiliation would be between a mentor firm and the protégé firm. This line of affiliation would be less prone to abuse, and, by pulling the protégé firms into the procurements in which the mentor had a special advantage, would in fact help the small firms targeted for assistance by the mentor-protégé program.

The question for Congress, therefore, would be whether to extend current regulatory exemptions for affiliates to mentor-protégé ventures. As GAO's recent report to Congress on mentor-protégé programs noted, the SBA's mentor-protégé program permits a waiver of the affiliation rule between mentors and protégés that are small disadvantaged businesses participating in SBA's "Section 8(a)" program. Report GAO-11-548R, at 5. This means, in practice, that these mentor-protégé ventures may bid jointly on 8(a) contracts set aside for small businesses without the two firms being considered "affiliated." *See* 13 C.F.R. § 121.103. In addition, the report noted, the Small Business Jobs Act of 2010 granted SBA authority to establish new mentor-protégé programs for small businesses run by service-disabled veterans and women, and for HUBZone small businesses, modeled on SBA's current program for 8(a) participants. *See* Small Business Jobs Act of 1010, § 1347, *to be codified at* 15 U.S.C. § 637 note.

By their terms, the SBA size standards are used to determine "whether a business entity is small and, thus, eligible for Government programs and preferences reserved for 'small business' concerns." 13 C.F.R. § 121.101. At present those standards do not, therefore, normally apply to larger mentor firms. If the proposed legislation *did* impose a cap of 1500 employees on mentor firms in the pilot programs, then the size standards could be amended so that the SBA size rules (regarding, for example, affiliation to third parties) could be applied to mentor firms. This would, however, make the mentor firms subject to the complex and intrusive SBA rules on size, including the rules regarding affiliation, which in effect constrain firms' decisions regarding governance, staffing, revenue streams, and capital structures. Before taking this step -- before imposing these constraints on mid-size mentor firms -- policymakers should assess the potential costs and impacts of these new constraints.

2. Should Size Protests Be Allowed?

The next question is whether traditional "size" protests be allowed, so that competitors and others could challenge mid-size firms that apparently exceeded the cap -- 1500 employees, under the current bill -- for participation.

The SBA size protest system has proven an effective means of regulating the highly complex SBA size standards. While the protests can be expensive and disruptive, as with bid protests in general, they provide a means of third-party monitoring that balances the government's compliance needs with broader demands for efficient procurement.

Subjecting mentor firms to size protests would, however, trigger the systemic concerns outlined above, regarding the size standards in general. By subjecting the mentor firms to the SBA size standards, and then exposing them to size protests, the initiative would open the mid-size firms to scrutiny regarding affiliations and staffing, among other management decisions. This might create substantial costs, and discourage mid-sized firms from joining the GSA mentor-protégé program.

3. Should the "Rule of Two" Apply?

Under current law, procurements above the simplified acquisition threshold (generally $150,000) must be reserved for small business, subject to certain conditions, if the contracting officer reasonably concludes that two or more small businesses will compete for the work. *See* FAR 19.502-2.[8] The question is whether the same rule should apply under the proposed bill, which would otherwise apparently require GSA contracting officers to consider *all* full-and-open procurements, presumptively, for the pilot program. *See* H.R. 1812, sec. 2(d).

The current version of H.R. 1812 would apply a version of the "Rule of Two." Similarly, the amendment proposed by Congressman Rogers to H.R. 1540, discussed above, would apply the "Rule of Two" to a parallel initiative in Defense Department procurement. *See id.* sec. 845 (b)(1)(C) (contracting officer must consider whether "there is a reasonable expectation that at least 2 such program participants will submit offers with respect to the contract").

Should Congress decide to retain the "Rule of Two" constraints under H.R. 1812 and H.R. 1540, Congress may decide to reference the regulatory and caselaw authority that now surrounds the rule. The "Rule of Two" has been very controversial in application, and the lessons learned in applying that rule would, logically, help to ease administration of the proposed preference under the GSA mentor-protégé program.

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[8] The Federal Acquisition Regulation provides, in relevant part:

> FAR 19.502-2 Total small business set-asides.
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> * * *
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> (b) Before setting aside an acquisition under this paragraph, refer to 19.203(c). The contracting officer shall set aside any acquisition over $150,000 for small business participation when there is a reasonable expectation that:
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> (1) Offers will be obtained from at least two responsible small business concerns offering the products of different small business concerns (see paragraph (c) of this section); and
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> (2) Award will be made at fair market prices. Total small business set-asides shall not be made unless such a reasonable expectation exists (see 19.502-3 as to partial set-asides). Although past acquisition history of an item or similar items is always important, it is not the only factor to be considered in determining whether a reasonable expectation exists. In making R&D small business set-asides, there must also be a reasonable expectation of obtaining from small businesses the best scientific and technological sources

4. Should There Be a Limit on Awards?

Because of the potential power of this preference -- it could, in principle, apply presumptively to all full-and-open procurements run by GSA -- some firms could, at least in theory, amass substantial contract awards under the program. Because of the relatively high cap on employees -- 1500 -- there is no guarantee that accumulated awards would "bump" a mid-size company from the program. This is, therefore, a question that should be looked at seriously.

An anomaly in the GSA mentor-protégé program may make it easier to set guidelines in this area. As it discussed below, the mentor firms in the GSA mentor-protégé program appear to be clustered exclusively in the professional services, janitorial, and construction services industries. Because there is a relatively high degree of concentration in services, it may be possible to set overarching limits on awards, without being unduly disruptive.

5. Would Benefiting Firms Have a Priority in Preference?

The issue of priorities in preferences has also been highly controversial. In addressing this issue, policymakers may want to look to the hierarchy of preferences established under existing programs, and set forth in FAR 19.203(c).[9]

6. Will This Initiative Enhance Competition? Create Jobs?

In assessing the proposed legislation, it is important to assess the broader potential economic impacts of the legislation. *See, e.g.,* Albert Sanchez Graells, *Public Procurement and EU Competition Rules* (2011) (arguing that, in assessing proposed procurement legal rules, we should assess not only the microeconomic impact on specific competitions, but more broadly the rules' impact on competition across a market). Under current conditions, the most important economic goal is jobs creation. The proposed legislation is not, however, necessarily well-suited to ensure rapid jobs growth. A simple example will illustrate why.

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[9] The regulation reads as follows:

> 19.203 Relationship among small business programs.
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> (a) There is no order of precedence among the 8(a) Program (subpart 19.8), HUBZone Program (subpart 19.13), Service-Disabled Veteran-Owned Small Business (SDVOSB) Procurement Program (subpart 19.14), or the Women-Owned Small Business (WOSB) Program (subpart 19.15).
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> (b) *At or below the simplified acquisition threshold*. The requirement to exclusively reserve acquisitions for small business concerns at 19.502-2(a) does not preclude the contracting officer from awarding a contract to a small business under the 8(a) Program, HUBZone Program, SDVOSB Program, or WOSB Program. If the contracting officer does not proceed with a small business set-aside and purchases on an unrestricted basis, the contracting officer shall include in the contract file the reason for this unrestricted purchase.
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> (c) *Above the simplified acquisition threshold*. The contracting officer shall first consider an acquisition for the 8(a), HUBZone, SDVOSB, or WOSB programs before using a small business set-aside (see 19.502-2(b)). However, if a requirement has been accepted by the SBA under the 8(a) Program, it must remain in the 8(a) Program unless SBA agrees to its release in accordance with 13 CFR 124, 125 and 126.
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> (d) Small business set-asides have priority over acquisitions using full and open competition. See requirements for establishing a small business set-aside at subpart 19.5.

A 2008 study published by the Small Business Administration, *High-Impact Firms: Gazelles Revisited,*[10] pointed out that firms the study called "*high-impact firms*" -- firms whose sales had doubled over a four-year period, and which had an employment growth quantifier (= firm's absolute change x percentage change in employment)[1] of two or more over the period -- *accounted for "almost all employment and revenue growth in the economy."* Conversely, with regard to firms with *lower* performance, the authors found that *nearly all the "job losses in the economy over [the periods] studied are attributable to low-impact firms with more than 500 employees.*" The "high-impact" firms are not, the authors found, necessarily new and emerging companies. "The average age of a high-impact firm is around 25 years old," the report concluded. "These firms exist for a long time before they make a significant impact on the economy." *Id.* at 1-2.

This study affords one rough measure, then, of the proposed pilot program's potential success in generating jobs. If the program is likely to foster "high-impact" firms, per the SBA's sponsored study, the program is much more likely to generate jobs in the near term. Conversely, if the program will -- or *could* -- be used to foster large, "low-impact" firms, the program might even *worsen* job loss, if contracts were diverted from truly "high-impact" firms that simply did not qualify for the program.

The criteria for inclusion in the proposed program are spelled out above. To join the pilot program contemplated by H.R. 1812, a firm must: (1) be enrolled as a mentor or participating in the GSA's Mentor-Protege program; (2) if a mentor, have at least one protégé that is a small business; (3) have fewer than 1,500 employees; and (4) not be a small business. *None* of these criteria, of course, assures that only "high-impact" firms will participate; in fact, a large *low-impact* firm, which was shedding jobs, could also qualify. The criteria for program admission are not, therefore, highly aligned to assure that the proposed pilot program will generate substantial jobs in the coming years.

Nor is it clear that those firms that fit within the proposed program's eligibility are the ones most likely to warrant support, *i.e.*, firms which have matured out of the small business programs, or which will lend robust competition to the federal procurement market. The firms listed as participants in the GSA mentor-protégé program[11] are clustered in the professional services, janitorial, and construction services industries. There is nothing in the criteria for admission to the program to suggest -- or, more concretely, to confirm -- that firms in the program are struggling because they were previously protected by small business preferences, or that they are firms essential to maintain competition in their respective markets.

V. Conclusion

There is an abiding concern that mid-sized firms are disadvantaged in the federal marketplace, because of structural forces within that market and because the mid-sized firms may have grown up under the protection of small business preferences. There is also a

[10] Available at http://archive.sba.gov/advo/research/rs328tot.pdf.

[11] http://www.gsa.gov/portal/content/105301.

consensus that mid-sized firms typically provide healthy competition in the federal marketplace. Addressing these concerns by creating a special preference category for “medium-sized” firms could, however, trigger serious trade frictions, and could undermine ongoing efforts to open global procurement markets.

Another path, therefore, would be to establish a pilot program, as contemplated by H.R. 1812, to create a procurement preference for mentors in the GSA mentor-protégé program, so long as those firms remained under a certain size limit. Doing so, however, may mean in practice that these mid-sized firms are subject to intensely complex size and affiliation standards, which could have a real impact, in turn, on the those firms’ business decisions, including decisions regarding revenue strategies, capital structure, business development, staffing levels, and governance. At the same time, given the criteria for admission to the program, there is no guarantee that the proposed pilot program will generate jobs rapidly (an economic imperative at this point), or that it will nurture recently graduated “small” businesses, or even that the pilot program will ensure robust competition in the federal market. These concerns suggest, therefore, that the program should be more aggressively focused, so that the public policy goals that undergird the legislation can be better met.

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