

Designing Small Business Programs that Work

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For decades, government organizations have used race- and gender-based measures to encourage the participation of person of color (POC)- and woman-owned businesses in the contracts and procurements they award. However, over the past few years, such programs have increasingly faced legal challenges and political scrutiny. For example, over the past year, the State of Texas removed race- and gender-based measures from its Historically Underutilized Business program, converting it exclusively to a race- and gender-neutral program.[1] Governor Henry McMaster of South Carolina signed an executive order banning state agencies' use of POC-owned business participation goals, and a bill in the South Carolina legislature aims to codify this ban in state law.[2, 3] Similarly, Tennessee and Arkansas have also banned the use of race- and gender-based measures in public contracting across the state.[4, 5] All these efforts are part of an ongoing national movement against diversity, equity, and inclusion initiatives in government contracting, including for federal agencies. Last year, the United States Department of Transportation issued an Interim Final Rule that removed the presumption that POC and women are *socially disadvantaged* as part of the Federal Disadvantaged Business Enterprise and Airport Concessions Disadvantaged Business Enterprise Programs.[6] As a result, businesses owned by POCs and women are no longer automatically considered socially disadvantaged as part of either program.

In light of this legal and political uncertainty, government organizations that remain committed to supporting disadvantaged businesses and to ensuring that their contracting reflects the diversity of the communities that they serve can do so by developing and implementing small business programs that are tailored to the characteristics and needs of the businesses in their marketplaces. A well-designed *small business program* is one of the most effective ways an agency can encourage competition for the contracts it awards and improve outcomes for small and disadvantaged businesses in its marketplace.



Small businesses make up the vast majority of businesses across the country and are key drivers of the American economy, accounting for the majority of new job creation each year.[7] However, because of financial barriers, labor constraints, susceptibility to marketplace fluctuations, and other barriers, small businesses are more likely than other businesses to fail.[8, 9, 10, 11, 12] They also face substantial barriers to conducting contract work for government organizations, including potential difficulties scaling their capacities to meet the demand of government work and to accessing insurance and bonding, which are often required to perform that work.[13]

Government organizations have long used various efforts to encourage small business growth and to better prepare them for conducting contracting work for them. Such efforts have been shown to be beneficial to the organizations themselves, to the small businesses they support, and to the marketplaces in which they operate. Organizations' investments in their local small business populations have resulted in increased competition for their work, higher-quality bids and proposals, cost savings, and greater innovation.[14] In addition, increasing small business participation in government contracting can increase the participation of businesses owned by POCs, women, veterans, and other historically disadvantaged groups in that work, because, compared to other businesses, an

even larger percentage of those businesses are small in size. For example, based on data from *disparity studies* BBC conducted between 2014 and 2023, we have found that more than 90 percent of POC-owned businesses available for government contracts across the country earn less than $5 million in annual revenue, and the overwhelming majority of those businesses earn less than $1 million.

Not all small business programs are designed with enough consideration to truly meet the needs of the businesses that they are intended to support. For example, consider how most programs define small businesses. Many programs rely on the United States Small Business Administration (SBA)'s revenue standards to identify small businesses.[15] But, based on its own revenue standards, the SBA estimates that small businesses generally account for 99.9 percent of all businesses in the United States, indicating that the SBA's definition of a small business might be too inclusive.[16] It is hard to imagine that a business program for which virtually all businesses are eligible can effectively provide meaningful support to those businesses that need it most.

An effective small business program should be based on good research that accounts for the locations, work types, capacities, sizes, and other characteristics of the small businesses in an organization's marketplace as well as the specific economic barriers they might face. For example, a government organization can use information about business size from an *availability study* or a disparity study to design a small business enterprise (SBE) certification program based on the sizes of the businesses actually operating in its marketplace, ensuring that the program aligns with the realities of the businesses interested in performing work on its contracts. The organization could take its certification program a step further by establishing multiple tiers of certification so that small businesses of different sizes have different SBE designations (for example, micro SBEs, medium SBEs, and large SBEs). Such a program would allow the organization to tailor its efforts to the sizes of each tier of SBEs rather than assuming that all small businesses, regardless of their sizes, require the same kinds of support. In addition, it would help the organization avoid contracting practices that force the smallest of small businesses to compete for the organization's work on unequal footing with much larger businesses.



Once an organization has developed an SBE certification framework, it can then use a variety of measures designed to increase small business participation in its contracting effectively and sustainably. Examples of such measures include offering support services programs, mentoring programs, financing assistance, and bonding assistance as well as using small business contract goals and small business set asides. All those measures can and should be tailored specifically to the needs and characteristics of the small businesses operating in the organization's marketplace. Two measures that have been shown to be particularly effective in encouraging small business participation in government contracting are the use of *small business set asides* and *small business contract goals*.



Small business set asides are where an organization reserves, or sets aside, certain prime contracts for exclusive bidding among SBEs to give those businesses an opportunity to participate in the organization's work as prime contractors and to compete for that work against other businesses that are similar in size to their own. Although most small businesses gain experience working for government organizations by performing work as subcontractors, set asides can provide them with opportunities to work with an organization directly, helping them develop closer relationships with government organizations, develop their technical and project management skills, and build their capacities to perform work on larger and larger contracts over time. When determining which projects to set aside for SBEs, organizations can rely on information about the types of work different tiers of SBEs perform, the sizes of contracts for which they can realistically compete, the locations within the marketplace where they can perform work, and on other factors, all of which is available from a well-conducted availability or disparity study. Using such information to select set-aside projects helps to ensure that the projects an organization selects align with the characteristics of the small businesses it aims to support and helps to ensure that the firm that ultimately performs the work can do so successfully.



An availability or disparity study can also help an organization develop and tailor the use of small business contract goals. Many small businesses are introduced to government contracting as subcontractors. Small business contract goals encourage prime contractors to subcontract portions of contracting work to small businesses, providing them with valuable opportunities to cultivate their growth. As part of a typical goals program, when awarding a contract, an organization sets a percentage goal for the participation of small businesses in the associated work. Bidders or proposers have to meet the goal by being small businesses themselves, by committing work to small business subcontractors, or

by submitting documentation demonstrating that they made *good faith efforts* to meet the goal through participation with small business subcontractors and explain why they were unable to do so. As with small business asides, organizations can use information from an availability or disparity study to select projects for which the use of small business goals are most appropriate, aligning the characteristics of those projects—for example, their sizes, work types, and locations—with the characteristics of the small businesses operating in the marketplace.

As government organizations consider whether to pivot away from the use of race- and gender-based measures as part of their contracting—and if so, to what extent—it is critical for them to consider alternative efforts to continue supporting disadvantaged businesses in their marketplaces. One of the most effective ways for an organization to do so is to develop a data-driven small business program that is tailored to the needs of the businesses operating its marketplace and that is designed to address the specific barriers that those businesses face. For decades, organizations have used information from BBC availability and disparity studies to develop programs for POC- and woman-owned businesses but also, increasingly, for small business programs. We are continuously exploring ideas for how organizations can use our research to reliably improve outcomes for small and disadvantaged businesses. Whether your organization is looking to strengthen its program, create a new program, or discuss new ideas, we welcome the opportunity to engage with you so we can work together to address the economic barriers so many businesses face in obtaining government work.

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