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CLOSING THE GAP: EXPLORING MINORITY ACCESS TO CAPITAL AND CONTRACTING OPPORTUNITIES

ROUNDTABLE

BEFORE THE

COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP UNITED STATES SENATE

ONE HUNDRED TWELFTH CONGRESS

FIRST SESSION

MARCH 3, 2011

Printed for the Committee on Small Business and Entrepreneurship

Available via the World Wide Web: http://www.fdsys.gov

U.S. GOVERNMENT PRINTING OFFICE

87–579 PDF WASHINGTON : 2014

For sale by the Superintendent of Documents, U.S. Government Printing Office
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C O N T E N T S

Opening Statements

	Page
Landrieu, Hon. Mary L., Chair, and a U.S. Senator from Louisiana	1
Snowe, Hon. Olympia J., Ranking Member, and a U.S. Senator from Maine	4
Hagan, Hon. Kay, a U.S. Senator from North Carolina	18

Witness Testimony

Panel I

Johns, Marie, Deputy Administrator, U.S. Small Business Administration	6

Panel II

Fairlie, Robert W. Ph.D., Professor of Economics, University of California, Santa Cruz	21
Morial, Marc, President and Chief Executive Officer, National Urban League	32
Allen, Susan, President and Chief Executive Officer, U.S. Pan Asian American Chamber of Commerce	53
Mitchell, B. Doyle, Chairman, National Bankers Association	64
Montoya, Martha, Procurement Chair and Board Member, U.S. Hispanic Chamber of Commerce	68

Panel III

Gustafson, Peggy, Inspector General, U.S. Small Business Administration	82
Kutz, Greg, Managing Director of Forensic Audits and Special Investigations, U.S. Government Accounting Office	91

Alphabetical Listing and Appendix Material Submitted

Allen, Susan	
Testimony	53
Prepared statement	55
Summary of testimony	113
Fairlie, Robert W.	
Testimony	21
Prepared statement	24
Summary of testimony	111
Gustafson, Peggy	
Testimony	82
Prepared statement	85
Summary of testimony	115
Hagan, Hon. Kay	
Opening statement	18
Johns, Marie	
Testimony	6
Prepared statement	9
Summary of testimony	110
Kutz, Greg	
Testimony	91
Prepared statement	93
Summary of testimony	116
Landrieu, Hon. Mary L.	
Opening statement	1

Page

Mitchell, B. Doyle
Testimony 64
Biography 67
Montoya, Martha
Testimony 68
Prepared statement 70
Summary of testimony 114
Morial, Marc
Testimony 32
Prepared statement 34
Summary of testimony 112
Snowe, Hon. Olympia J.
Opening statement 4
U.S. Census Bureau
Report titled "Survey of Business Owners: Black-Owned Businesses: 2007" 117
Report titled "The Compelling Interest for Race—and Gender Conscious Federal Contracting Programs: An Update to the May 23, 1996 Review of Barriers for Minority and Women-Owned Businesses" 157

CLOSING THE GAP: EXPLORING MINORITY ACCESS TO CAPITAL AND CONTRACTING OPPORTUNITIES

THURSDAY, MARCH 3, 2011

UNITED STATES SENATE,
COMMITTEE ON SMALL BUSINESS
AND ENTREPRENEURSHIP,
Washington, DC.

The committee met, pursuant to notice, at 10:12 a.m., in Room 428–A, Russell Senate Office Building, Hon. Mary L. Landrieu (Chair of the Committee) presiding.

Present: Senators Landrieu, Hagan, and Snowe.

OPENING STATEMENT OF HON. MARY L. LANDRIEU, CHAIR, AND A U.S. SENATOR FROM LOUISIANA

Chair LANDRIEU. Good morning. Thank you all for joining us this morning for a meeting of the Small Business Committee about Closing the Gap: Exploring Minority Access to Capital and Contracting Opportunities, specifically focused on closing the wealth gap in America and what our committee and the Small Business Administration can contribute to that effort.

Since becoming Chair of this committee, I, along with other members, have made it a top priority to make sure the nation's small businesses, and that is 27 million small businesses, have access to capital and ready access to government contracting, particularly Federal Government contracting. I have asked my staff to update me regularly on the number of banks, particularly community banks, as you know, Ms. Johns, who are participating in the small business lending programs, and we have seen a significant increase of banks in America stepping up to be partners with the SBA trying to streamline those processes and get capital to Main Streets throughout our country.

In addition, this committee is on constant lookout for new and better ways to improve those programs to streamline them, eliminate regulation, and to try to open up capital markets and increase contracting opportunities for small business when those opportunities present themselves through Federal contracting. It is clear to me that small businesses need reliable and non-predatory financing opportunities in both the debt and equity market in order to start, to grow, and to succeed. They want to know that when the Federal Government does contract for goods and services and it is in the billions of dollars—and we are going to try to have that figure before the end of the meeting today—that small businesses can com-

pete on a level and fair playing field with large businesses that also compete for contracting.

As Chair, I will continue to focus on removing any arbitrary barriers that are identified as blocking this goal. In some cases, those barriers are not unlike the challenges all businesses face that are trying to work with the Federal Government—red tape, regulations, slow time frames. But in some cases, the obstacles that minority business owners face, whether it is African American or Hispanic or Asian or women, are quite unique. Since 2009, I have convened at least three meetings to address ways that this committee and the SBA through many of its programs can address and provide remedy to these issues.

The purpose of today's hearing is clear. We are here to discuss solutions, initiatives and solutions on how this committee, this Congress, and the SBA administration can close and eventually, if possible, try to erase the wealth gaps in this nation that were so clearly identified by Dr. Robert Fairlie, a professor of economics at the University of California at Santa Cruz, who is again with us today and will be testifying on our second panel.

I know, and I have known through many years of experience that the only way to close these disparities in wealth gaps in our nation is through a holistic approach, obviously, improved access to education, improved access to home ownership using traditional and safe models of lending and equity building. These issues, however, are not within the jurisdiction of this committee. But improving access to capital for small businesses, expanding opportunities for contracting with the Federal Government, expanding opportunities for export, the broadband initiative, part of that is under the jurisdiction of this committee, and we are going to remain focused on these areas and closing this gap.

Last year at a hearing on this subject, Dr. Fairlie, who will be testifying today again, testified that many factors are responsible for the disparity in business performance between minority and non-minority-owned businesses. Access to financial capital is one. He pointed out that one of the major roots of the problem is the extremely high level of wealth inequity, or I would say it as an extremely low wealth accumulation by African American families.

I was astonished to learn, and I have been in public office now for over 30 years, that the median wealth for African American families in America in the year 2000—and this was the Census, I think, of 2000, now we have some updated figures today—was only $5,000, compared to $87,000 for a majority of white families. And for Latino families, it was less than $8,000. These levels of wealth are one-eleventh to one-sixteenth the levels of wealth held by non-minorities.

I want to show this graph which is up here. I am sorry that all of you cannot see it. I do not know if there is anything the staff can do to hand this out, but for those of you that can see the video, it is really startling. The disparities in wealth are substantially larger than disparities of income, and I think that sometimes in America, we focus on closing the income gap. And you can see the income gap for non-minority families at $55,000. For African American families, it is $34,000. And for Latino families, it is $37,000. There is a gap. It is troubling. It has been improving, I think, sub-

stantially, but we are going to hear some testimony as to whether that is improving.

But when you look at the wealth gap, the net worth, the gap of net worth between white families in America at $87,000 and African American families at $5,400 and Hispanic families at $7,900, it is absolutely startling, jaw dropping, and if it does not make more than just this committee focus, I am not sure what data or testimony would.

And that is why we are here today, to talk about solutions to closing this gap. I have shared this with my family, who was in disbelief. I have shared it with people that do not believe it when I say it, and so we are going to have a second hearing today. And I have shared it in speeches all over this country. I have made it one of my priorities as Chair of this committee to do what I can, which is limited under the jurisdiction of this committee, but this committee is one of the standing committees of the Senate and we are going to take this issue on.

Despite the sobering impact of Dr. Fairlie's testimony, which we will hear on the second panel, there is some good news for minority business owners that we will hear today. The good news is the number of businesses in our minority communities continues to grow. According to the most recent data available from the SBA Office of Advocacy, minority-owned small businesses are among the fastest growing segment of the small business community. From 1997 until 2002, firms owned by African Americans grew almost by 45 percent, Hispanics by 31 percent, Asian Americans by 24 percent, and Hawaiian and Pacific Islanders by 49 percent.

Minority-Owned Business Enterprises accounted for more than 50 percent of the two million new businesses over the last ten years, far outstripping, I think, their make-up of the population. There are now more than four million minority-owned companies in the United States with annual sales totaling $700 billion. These businesses cross the entire industrial spectrum, from financial services and health care to construction and transportation.

So it is clear there is great potential here. It is clear that besides access to high levels of education for minority communities, and I should say quality education, it is besides just the opportunity for traditional wealth creation through home ownership, not what we have seen in the last few years, which has been actually moving in the wrong direction, but in the traditional sense of equity building. But having the ability to build a business, to build wealth, to transfer that wealth to future generations is absolutely essential to close this startling and shameful gap that we are experiencing right now in our country.

So that is what this hearing is about. There will be hearings over the next month or two in the areas of fraud, abuse, in all programs related to the SBA. That is not the subject of this hearing. This hearing is about positive solutions for closing this gap and for acknowledging that this gap actually exists.

So that is why the Secretary is here this morning, Marie Johns, to testify about, A, does the SBA recognize this gap? Do you consider it in your mission an opportunity to try to, or within some aspect of the mission of the SBA to see what you can do to close

this gap through the programs that the SBA basically runs and monitors and how we are addressing that.

So I am looking forward to this panel. We have a large second panel. And then the third panel, because of the minority's request, will focus on some additional issues.

I am joined by my Ranking Member, Senator Snowe, and then we will turn to our first panel for their testimony.

OPENING STATEMENT OF HON. OLYMPIA J. SNOWE, A U.S. SENATOR FROM MAINE

Senator SNOWE. Thank you, Chair Landrieu, for holding this hearing today to discuss the barriers that continue to exist for our nation's underserved small businesses. I also thank our distinguished panelists that include the SBA Deputy Administrator, Marie Johns, SBA Inspector General, Peggy Gustafson, Greg Kutz from the Government Accountability Office, and all of our other witnesses to appear in the second panel, who will offer invaluable insight into the various hurdles minority-owned small businesses encounter when trying to access capital to participate in the Federal marketplace.

Regrettably, January marks the 21st consecutive month that the unemployment rate has been at or above nine percent. Even more astounding, the Bureau of Labor Statistics reported in January unemployment of African Americans was 15.7 percent, and 11.9 percent among Hispanics.

According to the U.S. Department of Commerce, minority-owned firms generate $1 trillion in economic output to the U.S. economy and create 9.5 million jobs. Just imagine the strides we could achieve towards an economic recovery if the Federal Government could better harness minority-owned firms' job creation potential.

Ensuring that minority-owned businesses have fair access to Federal contracting opportunities is one way that our government can help foster minority entrepreneurial success. Last year, when it was brought to my attention that the HUBZone program would be given a super-preference for contracts above the other SBA contracting programs, I was very pleased to introduce legislation addressing this inequity by leveling the playing field so that contracts to service-disabled veterans, 8(a), HUBZone, and women-owned firms may be awarded with equal deference to each program. Particularly during these difficult economic times, it is imperative that small business contractors possess an equal opportunity to compete for Federal contracts, and so I am pleased that this parity legislation became law last fall.

Furthermore, when it comes to small business goaling requirements, I am pleased to also note that the Federal Government exceeded its five percent Small Disadvantaged Business contracting goal in fiscal year 2009, awarding 7.5 percent of total contracts to these firms. I strongly encourage the administration to continue to build on these successes. However, much more needs to be done.

For example, there remains a glaring problem facing minority-owned small businesses in accessing Federal contracts and that is the fraud that plagues the SBA's 8(a) Business Development Program. In March of 2010, the GAO issued a report detailing the extensive fraud within the 8(a) program. The report revealed that 14

ineligible firms received $325 million in sole source and set-aside contracts, even though these firms were not eligible for the 8(a) program. As we use this hearing to examine barriers facing the minority community, I look forward to hearing from the GAO and their recommendations, as well as the SBA, to remedy the illegitimate firms siphoning away contracts from the rightful businesses trying to compete within the 8(a) program.

As Ranking Member of this committee, I take very seriously our responsibility of vigorous oversight. That is why last December, Chair Landrieu and I sent a letter to the SBA highlighting the recent headlines and GAO reports of fraud and abuse that have plagued the agency's contracting programs. I want to echo again today, as we did in our letter, our first priority this Congress is ensuring that all of the SBA's contracting programs, because we know that fraud and abuse are not unique to the 8(a) program, are running efficiently, effectively, and free of exploitation.

Shifting to access to capital, in April of last year, this committee held a hearing on the obstacles and opportunities for minority small business owners in capital markets. At that hearing, the committee investigated Dr. Robert Fairlie's, who we are fortunate to have with us again today, report, Disparities in Capital Access Between Minority and Non-Minority-Owned Businesses. This report highlights a wide disparity in capital access between minority and non-minority firms.

For example, the study concludes that minority-owned firms are, one, less likely to receive loans than non-minority firms; two, receive lower loan amounts than non-minority firms; and three, are more likely to be denied loans; and four, pay higher interest rates on business loans. These conclusions are certainly alarming, and clearly, as I have said repeatedly to the SBA, more must be done to address these problems.

But I am pleased to say that, overall, the SBA has broken the mold in regard to minority lending. In fact, SBA-backed loans are about three times more likely than conventional loans to go to minority-owned firms, and micro loans have a particularly high success rate in fiscal year 2010. Forty-six percent of the SBA's micro loans, a five percent increase over the previous fiscal year, went to minorities.

I am pleased to also say that the increased micro loan limits and the heightened 7(a) and 504 loan limits, which I had initially called for in my legislation, the Next Step For Main Street Credit Availability Act, were recently enacted into law, and I thank the Chair for her role in helping to secure those changes. It is my hope that this initiative, combined with other measures that we will be able to provide, like the $24 million in the Recovery Act for micro loan intermediaries who were encouraged to carry over the funds into future fiscal years, will help provide even greater capital access to minorities.

I also expect the micro loan program to continue to be a powerful tool for minority entrepreneurs moving forward and hope that Deputy Administrator Johns can speak to this issue today.

Additionally, the SBA has initiated two new lending programs, the Small Loan Advantage and Community Advantage Programs, which have the potential to provide additional sources of capital to

underserved communities. So today's hearing does provide an opportunity for the Administration to explain to key stakeholders how these new lending programs will increase access to capital for minority entrepreneurs.

Again, thank you, Chair Landrieu, for your leadership in these critical issues and I am looking forward to working with you and to hearing from our witnesses.

Chair LANDRIEU. Thank you, Senator Snowe.

Let me go right into our introductions to Marie Johns, who is the Deputy Administrator for the SBA. Since being confirmed by the Senate, Ms. Johns has been focused on the management of the agency, the development of SBA policies. Recently, she has focused much of her efforts on the development and implementation of the policies enacted by the Small Business Jobs Act, which was signed into law, which this committee led, and we are very, very proud of that particular Act. Prior to becoming SBA Deputy Director, Ms. Johns served as President of Verizon Washington, where she was responsible for over 2,000 employees and 800,000 customers. We thank you, Ms. Johns, for being here today.

We are joined by Senator Hagan and we will go through a round of questioning after your presentation. Please begin. Thank you.

STATEMENT OF MARIE JOHNS, DEPUTY ADMINISTRATOR, U.S. SMALL BUSINESS ADMINISTRATION

Ms. JOHNS. Thank you, Chair Landrieu, Ranking Member Snowe, and Senator Hagan. Thank you for inviting me to testify today on these very important issues. It is an honor to be speaking before you this morning.

As an African American woman, as a former small business owner, and most importantly, as an American citizen, I greatly appreciate this committee's commitment to ensuring that minority-owned companies have the same opportunities as small businesses across our country.

Core to our mission at the Small Business Administration is expanding opportunities for companies in traditionally underserved areas, including those owned by minorities, women, veterans, people with disabilities, and people from rural areas. These businesses typically have a harder time accessing the tools they need to grow and create jobs in their communities.

The SBA is well poised to reach these businesses. For example, our lending programs support companies that struggle with access to conventional capital. One study by the Urban Institute, and this was referenced earlier, showed that women- and minority-owned small businesses are three to five times more likely to receive an SBA loan than a conventional loan. We are proud of the work that we have done supporting underserved communities, but always we know we can do more, and this is especially true since many of these communities have been disproportionately hard hit by the recession.

As a result of the tight credit market over the last two years, the overall share of SBA loans going to small businesses in underserved communities has decreased significantly. From fiscal year 2008 to fiscal year 2010, overall SBA 7(a) lending to small businesses in underserved communities dropped nearly five percent,

and that decline has been even greater in some communities. But that decline equates to a drop of $780 million in loans to businesses that need them most. This drop in lending has been a call to action for us at the SBA.

We found that the lower-dollar loans were significantly important to helping entrepreneurs in underserved communities start and grow their businesses. Often, a small business does not need a $1 million or a $5 million loan. Some do, but others need more in the range of $50,000 to buy new equipment or $100,000 to renovate a building. We have heard from our lending partners that the paperwork and the processing time involved with those loans frequently meant that they were not as cost effective to make a low-dollar loan through the SBA.

So to address this, we recently announced two new loan initiatives, part of our 7(a) program, Small Loan Advantage and Community Advantage, and those programs are designed to get lower-dollar loans into the hands of small business owners. These initiatives streamline the application process and cut down the paperwork while still offering our standard guarantee.

Small Loan Advantage is open to lenders in our Preferred Lending Program, and I am happy to report that the SBA began accepting applications for Small Loan Advantage loans on February 15, a full month ahead of schedule.

Meanwhile, Community Advantage opens our 7(a) lending program to, quote-unquote, "mission lenders," such as Certified Development Companies, Community Development Financial Institutions, or CDFIs, and SBA certified micro lenders. This is for the first time ever. We are very excited about bringing these non-bank lenders on as partners because of the proven track record they have in serving underserved communities, including providing effective technical assistance that many of those borrowers need.

The SBA has also begun accepting applications from mission lenders to become SBA lenders, and once approved, those lenders will immediately be able to offer Community Advantage Loans.

The SBA also works to help small businesses compete for and win government contracts, which are an important source of revenue in many instances. Our 8(a) Business Development Program has been critical to helping these small businesses win contracts, grow, and create jobs. To strengthen the 8(a) program even further, the SBA recently undertook the first regulatory review process in over a decade. The agency actually began the process back in 2007. Once we had a draft proposal for new regulations, SBA officials went on an extensive listening tour, where we gathered over 1,500 comments from around the country.

And after much hard work, the new 8(a) regulations were posted this month. These new rules cover a variety of areas in the program, from clarifications on determining economic disadvantage to tightening the requirements on joint venture contracts. Overall, our goal was to strengthen the program while eliminating opportunities for waste, fraud, and abuse, and ensuring, as was said earlier, that the program benefits flow to their intended recipients, and I believe these new regulations go a long way to achieving that goal.

The SBA also recently finalized and released the Women's Contracting Rule. The rule is a critical step toward giving women-

owned small businesses better opportunities to compete for Federal Government contracts.

Our steps to strengthen the 8(a) program and the structure behind the Women's Contracting Rule are also examples of the three-prong oversight strategy that we are implementing across all of our programs. That strategy focuses on, one, effective up-front certification. Two, ongoing surveillance and monitoring. And three, timely and robust enforcement. These steps are aimed directly at ensuring that only eligible small businesses benefit from our programs and that when we suspect that bad actors are present, we go after them appropriately and aggressively.

While I am proud of what the SBA has accomplished under the leadership of Administrator Mills, alongside this committee, I believe we must continue to be diligent in our work with underserved communities. We know that with the right tools in hand, entrepreneurs and small businesses in these communities can have significant impact in driving economic growth and creating jobs where they are needed most.

Thank you very much. I look forward to your questions.

[The prepared statement of Ms. Johns follows:]

U.S SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

TESTIMONY OF MARIE C. JOHNS
DEPUTY ADMINISTRATOR
US SMALL BUSINESS ADMINISTRATION
BEFORE THE SENATE SMALL BUSINESS COMMITTEE
CLOSING THE GAP: EXPLORING MINORITY ACCESS TO CONTRACTING OPPORTUNITIES
MARCH 3, 2011

Chairwoman Landrieu, Ranking Member Snowe, and Members of the Committee,

Thank you for inviting me to testify today. It is truly an honor to be speaking before you on this important issue. As an African-American woman, a former small business owner, and most importantly, an American citizen, I greatly appreciate this Committee's commitment to ensuring that minority-owned companies have the same opportunities as all small businesses across the country.

Core to our mission at the Small Business Administration (SBA) is expanding opportunities for companies in traditionally underserved communities, including those owned by minorities, women, veterans, people with disabilities, and people from rural areas. These businesses typically have a harder time accessing the tools they need to grow and create jobs in their communities.

The SBA is well poised to reach these businesses. For example, our lending programs support companies that struggle with access to conventional capital. One study by the Urban Institute showed that women- and minority-owned small businesses are three-to-five times more likely to receive SBA loans than conventional loans[1].

We are proud of the work we have done supporting underserved communities, but as always, we know we can do more. This is especially true since many of these communities have been hit disproportionately hard by the recession.

As a result of a tight credit market over the last two years, the *overall* share of SBA loans going to small business in underserved communities has decreased significantly. From Fiscal Year 2008 to FY10, overall SBA 7(a) lending to small businesses in underserved communities dropped nearly 5 percent—and that decline has been greater in some communities. This equates to a drop of $780 million in loans to the businesses that need them the most.

This drop in lending has been a call to action for all of us at the SBA.

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[1] *Competitive and Special Competitive Opportunity Gap Analysis of the 7(A) and 504 Programs*, Urban Institute, January, 2008. http://www.urban.org/UploadedPDF/411596_504_gap_analysis.pdf.

We found that lower dollar loans were significantly important to helping entrepreneurs in underserved communities start and grow their businesses. Often, a small business does not need a $1 million or $2 million loan. They need $50,000 to buy new equipment, or $100,000 to renovate their building. However, we have heard from our lending partners that the paperwork and processing time involved frequently means that it is not cost effective to make a low dollar SBA loan.

To address this, we recently announced two new loan initiatives, **Small Loan Advantage** and **Community Advantage**, which are designed to get lower dollar loans into the hands of small business owners.

These initiatives streamline the application process and cut down on the paperwork, while still offering our standard guarantee.

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Meanwhile, **Community Advantage opens our 7(a) lending program to "mission lenders,"** such as Certified Development Companies (CDCs), Community Development Financial Institutions (CDFIs), and SBA-certified microlenders. We are very excited about bringing these non-bank lenders on as partners because of the proven track record they have in underserved communities, including providing effective technical assistance that many borrowers may need.

The SBA has also begun accepting applications from mission lenders to become SBA lenders. Once approved, these lenders will immediately be able to offer Community Advantage loans.

The SBA also works to help small businesses compete for and win government contracts, which are an important source of revenue in many industries.

Our **8(a) business development program** has been critical in helping these small businesses win contracts, grow, and create jobs. To strengthen the 8(a) program even further, the SBA recently undertook the first regulatory review process in over a decade.

The agency actually began the process back in 2007. Once we had a draft proposal for new regulations, SBA officials went on an extensive listening tour where we gathered over 1500 comments. After much hard work, the new 8(a) regulations and guidelines were posted this month.

These new rules cover a variety of areas of the program, from clarifications on determining economic disadvantage, to tightening the requirements on Joint Ventures contracts. Overall, our goal was to strengthen the program, while eliminating opportunities for waste, fraud, and abuse, and ensuring that program benefits flow to their intended recipients. I believe that the new regulations go a long way toward achieving this goal.

The SBA also recently finalized and released the Women's Contracting Rule. The rule is a critical step toward giving women-owned small businesses better opportunities to compete for federal government contracts. Women business owners can now log on to our website to begin

the certification process. We expect everything to be up and running by the all-important 4th quarter of FY 2011, which is when the majority of federal agency purchasing takes place.

While, I am proud of what the SBA has accomplished under the leadership of Administrator Mills alongside this committee, I believe we must continue to be diligent in our work with underserved communities. We know that with the right tools in hand, entrepreneurs and small businesses in these communities can have a significant impact in driving economic growth and creating jobs where they are needed most.

Thank you.

Marie C. Johns

Marie Johns is Deputy Administrator of the US Small Business Administration, where she contributes to management of the agency and development of SBA policy. Johns was nominated by President Obama on December 17th, 2009 and confirmed by unanimous consent in the Senate on June 22nd, 2010.

Prior to becoming Deputy Administrator, Johns was the Managing Member of L&L Consulting, LLC, an organizational effectiveness and public policy consulting practice. Previously, she served as President of Verizon Washington, where she was responsible for nearly 2000 employees and more than 800,000 customers, including many small businesses. Johns worked to develop products and services to meet the needs of Verizon's small business customers, and worked closely with Verizon's vendors, suppliers, and subcontractors, some of whom were SBA borrowers. She retired from Verizon in 2004 after 21 years of service in the telecommunications industry.

Johns has a long record of business and civic leadership. She is the founder of the Washington DC Technology Council, former chair of Leadership Greater Washington, and a member of the board of the Girl Scouts USA. Johns served for 10 years as a trustee at Howard University, where she chaired the Academic Excellence Committee. Johns also served as the founding chair of the Howard University Middle School of Mathematics and Science. As chair of the DC Chamber of Commerce, as well as chair of its Small Business Committee, Johns helped small businesses get technical assistance and mentoring from larger area firms, and helped create a Visitors Center to encourage tourists to explore more of Washington's many vibrant neighborhoods and visit local small businesses.

While at Verizon Washington, Johns created the Students Educated for Economic Development Success program (SEEDS). SEEDS prepared over 200 high school dropouts for entry-level positions in the telecommunications industry, many of whom were hired by small local firms.

Johns earned her BS and MPA degrees from Indiana University's School of Public and Environmental Affairs, and was awarded an honorary doctorate of humane letters from Trinity University in Washington, D.C. She is the recipient of many awards in recognition of her business and civic leadership. Among her honors, Johns was recognized as a "Leader of the Years" by the Greater Washington Board of Trade, one the of "25 Most Influential Black Women in Business" by the Network Journal and one of the "100 Most Powerful Women" by Washingtonian Magazine. In 2004, Johns was inducted in the Greater Washington Business Hall of Fame.

Johns has been married for 39 years to Wendell Johns. They reside in Washington, DC, and have one son, Richard, an attorney in private practice in Washington, DC and Maryland. They are the proud grandparents of Richard Franklin II and Lauren Marie Johns.

Chair LANDRIEU. Thank you very much. I really appreciate particularly the comments about the Small Loan Advantage and the Community Advantage Programs.

One of the goals that I share with Senator Snowe is to really get our community banks in America partnered with the SBA in a much stronger partnership to make sure that the capital that is available and that the Federal Government is guaranteeing, particularly in our new lending program, actually hits the streets on Main Street. And making the SBA programs more user-friendly is something that the two of us and all of us, I think, hear a great deal about. So I appreciate those efforts and will look forward to monitoring the success of those programs.

Let me ask you, though, about loan size for African American businesses, minority businesses. The data that is coming in to us shows that from 2001 to 2006, the average loan size for African American business owners dropped from $181,000 to $84,000. That is a 53 percent drop in the size of loan. By contrast, the average loan to non-minorities dropped only 19 percent, to around $2,013. Is the SBA aware of this? What do you think is pushing that trend? Do you think it is something that should be cause for concern, and are you aware of those numbers?

Ms. JOHNS. Senator Landrieu, this recession has been very difficult on all businesses, but it has been incredibly hard on small businesses and particularly minority businesses, businesses operating in underserved communities. And we are very focused on that as an agency and that is exactly why we have developed a new initiative that is strictly focused on underserved communities.

The Advantage Loans that I described earlier are a key part of that underserved strategy because access to capital is absolutely critical. But as you know, the SBA takes a very holistic approach to how we serve small business growth and development. Capital is a critical part of that approach, but we also focus on government contracting as well as our counseling programs. And taken together, that is the best recipe for ensuring that small businesses have the support that they need to grow and create jobs.

We also are in the process of establishing a council on underserved communities, an advisory council. I am delighted to share with you that we are honored that Catherine L. Hughes, a founder of Radio One and TV One and a true leader in media industry, and as an African American woman quite a ceiling-breaker, is chairing the council. Ms. Hughes also was an SBA borrower early in her business formation. So she knows our programs. She knows our agency. And we are going to have under her leadership 20 of the most—the best minds that we can find around this country to help us focus on these kinds of statistics and to give us the advice that we need to determine, where do we need to replicate programs that are working well and where do we need to focus on addressing the gaps.

You talked earlier very eloquently about the effects of the recession and the effects of—for example, housing values that have dropped. Using equity in a home has been, forever has been a primary source of capital for small business owners to use in order to capitalize their business. So when we have seen the drop in hous-

ing values, that has had an impact on businesses' ability to get loans and to grow their businesses.

But we are confident that with the Advantage Loans as well as the improved counseling, the more robust counseling that we are going to be able to provide out in the field, because of—and thank you for your support on the Small Business Jobs Act—$50 million was appropriated for our Small Business Development Centers so that we can have more robust facility—counseling capacity available for small businesses around the country. We touch over a million entrepreneurs a year and we are hoping to grow that number because of the additional capacity that was available through the Small Business Jobs Act. So that is an example of some of the things that we are doing to address the issue that you raise.

Chair LANDRIEU. Well, I know this committee is going to stay very focused as we address the challenge of budgets and closing the deficit gap to recognize that this particular agency has a very special and important mission. If this recovery is going to be evenly felt across the country, it is going to take a well-resourced and well-structured and well-managed SBA, working with partners in the private sector and State governments, to make sure that these programs are reaching to areas that are obviously, by the data that has been presented to this committee, sometimes left out and underserved. And so I think we have to be very careful, I would caution my colleagues, about cutting back on these areas when we are really trying to turn the corner.

Let me turn it over now to Senator Snowe and then to Senator Hagan, and then we will go maybe through a second round of questioning, as well.

Senator SNOWE. Thank you, Chair Landrieu.

Ms. Johns, I want to get to the issues that I raised earlier in my testimony regarding the GAO report to get a better understanding of exactly how the SBA is responding to that report, because in the final analysis, given the fact that we are grappling with enormous deficits and trying to ensure that we maximize the efficiency and effectiveness of all of our programs and obviously root out any fraud and corruption, the fact is that there were 14 ineligible firms that were determined by the GAO to be fraudulent and designated as 8(a) contractors ineligible for the contracting program.

As I understand it, between 2009 to today, the SBA Office of Inspector General has referred 26 contractors for suspension or debarment, meaning permanent removal from Federal procurement. From those 26 referred, the SBA has suspended a grand total of three contractors. What happened to the other 23 contractors that were referred by the Inspector General's Office?

Ms. JOHNS. Let me begin, Ranking Member Snowe, by talking about our approach to fraud, waste, and abuse. First of all, there is zero tolerance for fraud, waste, and abuse. I spoke in my opening statement about our process for how we address fraud, waste, and abuse through effective certification on the front end, effective monitoring and surveillance during a business's time with us in a particular program, and then timely and robust enforcement. If there is a bad actor, that is how we address that company.

Any business that comes to our attention as a potential case for fraud, we investigate every single one, and there are three basic

paths that one of those complaints can take. There is a criminal path, which involves the Department of Justice and the Inspector General. There is the civil penalty path, which again involves the DOJ and the IG. And then there is the administrative path, where the agency has the most latitude to act. We are in regular touch with our IG's office about matters of this type and we are—as I said, we take any case of potential fraud very seriously.

You mentioned some numbers. What I would like to share with you, under our suspension and debarment process, in the last two fiscal years—now, this covers our lending as well as our procurement programs—we have had seven suspensions, 54 proposed debarments, and 44 actual debarments under the administrative track. I would be happy to provide additional——

Senator SNOWE. Well, can I get to these specifically——

Ms. JOHNS. Mm-hmm.

Senator SNOWE. And to this program and what the GAO cited?

Ms. JOHNS. Well, the GAO——

Senator SNOWE. On the 14 ineligible——

Ms. JOHNS. On the 14——

Senator SNOWE. Yes, and then——

Ms. JOHNS. Every one of the 14 firms that were cited by the GAO had been investigated and——

Senator SNOWE. So what is the disposition, then?

Ms. JOHNS. There were a variety of dispositions. First of all, of the 14 that the GAO cited, by the time we received the report, I believe about six or seven of those companies were no longer in the program for a variety of reasons. Of the remaining eight, others were removed from the program or left the program voluntarily. There were a variety of dispositions, and again, I can provide that detail for you.

Senator SNOWE. Well, I think the committee needs to have a response from the SBA on these issues. I mean, it is this program and every other program. We need exact responses on these questions so that we have a full appreciation and understanding. We have an obligation here in the oversight capacity of this committee, but in every committee on every program, frankly. I mean, that is where we stand today and always with respect to how taxpayers' dollars are being used. So I think we need to have an accounting for each and every one of those.

Ms. JOHNS. We will be happy to provide that.

Senator SNOWE. Okay. And so on the 26 contractors that were recommended, was that part of that 14? Only three contractors were suspended out of the 26 that were referred to the SBA.

Ms. JOHNS. I have to say, I am not familiar with the data that you are quoting from, but I will be happy to—if we can get that information in writing, we will be happy to provide a detailed answer.

Senator SNOWE. Well, who is responsible in the SBA for addressing these issues? Who is singularly responsible? What level of priority is this accorded within the SBA?

Ms. JOHNS. Responsibility for——

Senator SNOWE. For addressing these issues. Correct.

Ms. JOHNS. Well, Administrator Mills and myself are ultimately responsible. But the responsibility is not singularly focused. It is a

responsibility across the agency, and that gets to a new process that we put in place, the Suspension and Debarment Task Force, which is chaired by our General Counsel. That task force is looking at how we can ensure that, across the agency, employees are trained, better trained, to identify instances of possible fraud at every possible point throughout the process, either the certification process, time in the program, et cetera. And so we are—that task force is doing its work and we intend to have an even stronger view—process, rather, on fraud, waste, and abuse later this spring.

But what I assure you again, Ranking Member Snowe, is that every instance of fraud that comes to our attention is fully investigated and we are working in concert with the Inspector General, and the process that I described earlier as far as certification, monitoring, and enforcement, is modeled directly after the recommendations that were in the GAO report.

Senator SNOWE. Okay. Then I would like to see the final results of all that.

Ms. JOHNS. Sure.

Senator SNOWE. I think the committee deserves a response to the report, to the specific disposition of each and every firm or individual that was cited in the GAO report or any individual or firm that has been reported to SBA. I think at the end of the day, we have to go after those people, even if they have been removed from the program or left in the program, whatever they did, we have to go after them with a vengeance, as well. If you inappropriately use Federal dollars or access Federal programs illegally, then we obviously have to make sure that we take appropriate action.

Ms. JOHNS. And we are as serious about that as——

Senator SNOWE. We cannot relent on that.

Ms. JOHNS. Absolutely. We are relentless, as well, because we know that the integrity of the program is to make sure that they are available for those business owners for whom they are intended, rest on the fact that we run good programs and that we ferret out fraud, waste, and abuse at every turn.

And so I also want to thank the committee for the support of the Small Business Jobs Act because you gave us another very important tool in that regard. The presumption of loss provision in the Small Business Jobs Act says that even if a company has provided a service to the government and has misrepresented itself, that we can, once that is determined, we can go back and collect treble damages from that company. That is a new tool that our agency did not have before and that is available now to us through the Small Business Jobs Act.

Senator SNOWE. I would just mention that those 26 that I cited were in the IG's testimony. So that was from their report specifically. Thank you.

Chair LANDRIEU. I thank Senator Snowe. And as I have shared with her and with the staff, we are going to have a—we feel so strongly about the issue of waste, fraud, and abuse throughout the entire agency, obviously not just with the minority and African American programs but with the entire agency, particularly the IG's scathing report relative to HUBZones, we are going to have a very specific hearing on fraud, waste, and abuse, particularly with

the HUBZone program and with other programs in the SBA. But the subject of this hearing is about closing the wealth gap.

Senator Hagan.

Senator SNOWE. Madam Chair, can I just raise an issue in that regard?

Chair LANDRIEU. Yes.

Senator SNOWE. I think that any time we have the opportunity to have witnesses in front of the committee from the agencies that are responsible for these programs and these issues should be raised. I am not suggesting that it is just unique to these programs. I would ask these questions of any program. And so we are starting today. You happen to be the witness. We happen to have the Inspector General's report. We want a response to those issues and I think we deserve, but more importantly, not just us, but the taxpayers. So that is the issue. I would hope we would do this with every program. If it warrants it, then we should be raising those questions.

Chair LANDRIEU. We will have ample opportunity to do that.

Senator Hagan.

OPENING STATEMENT OF HON. KAY HAGAN, A U.S. SENATOR FROM NORTH CAROLINA

Senator HAGAN. Thank you, Chairman Landrieu, and it is an honor to be here and thank you for convening this important hearing. I do think there is obviously a disparity, and through the SBA and through the lending practices, we certainly do need to step up and see what we can do to proactively help change that.

And obviously, it is all about jobs. We need to see what we can do at the Federal level to make a better business climate so that private industries can grow and hire more people.

But I also know that creating that better business climate is central to our economic recovery. I have been holding hearings around the State in North Carolina, and I do hear all the time that small businesses are having trouble accessing capital. And that is why I was very pleased with the bill that we passed, the Small Business Jobs bill with the Small Business Lending Fund. I think it is one of the most important pieces of that legislation was the Small Business Lending Fund, and by providing resources to community banks and independent banks, that Small Business Lending Fund is certainly encouraging those banks to increase their lending to small businesses throughout the country and in North Carolina. And I think it is important because it is targeted to the community lenders that serve businesses that otherwise struggle to secure financing.

And encouraging entrepreneurship, I believe, is critically important to the sustained economic development and self-sufficiency in our underserved communities. While the SBA currently administers a number of well-meaning programs designed to make it easier for entrepreneurs in these communities to start a business and ultimately to grow that business, we have obviously got to be sure that those programs are working effectively, and to do so, the SBA programs must effectively encourage lenders to make those small-dollar loans that are needed most in our underserved communities.

But we have also got to ensure that Federal contracting preferences designed to assist disadvantaged businesses are not subject to fraud and abuse, and I think this hearing is a good opportunity to learn more about the state of these programs.

I just want to compliment the Deputy Secretary, Ms. Johns. I have read your bio and we are mighty fortunate to have you come in to the public service work and I appreciate your efforts and your leadership.

In your comments, you mentioned the Small Loan and Community Advantage Programs, which are intended to make it easier for the SBA lenders to make these smaller loans, in particular, to the underserved small business owners. The SBA Small Business Investment Company Program is designed to leverage private venture capital funds to encourage equity investments, which we know we need in these qualifying small businesses.

Can you explain to me how the proposed would work in practice, having to do with—in President Obama's 2012 budget, he proposes to leverage the SBIC program to support $200 million annually over the next five years in so-called impact investments that are targeted to economically and socially disadvantaged businesses. Can you explain how they would actually work and how it is intended to help minority- and women-owned small businesses expand more rapidly?

Ms. JOHNS. Yes, Senator. Thank you for the question. We are in the process of developing the contours of that program. What I view as my key role at this stage in the process is to build awareness, because we want to make sure that we have a pool of firms, money managers and investment firms, that reflect our country, that reflect our business sector. And so I am taking a lot of my time to talk to individuals at every opportunity to say we have created this impact fund and now we want to make sure that you are aware of this resource and that you stay connected to the SBA so that we can hopefully get you involved with this opportunity.

Businesses are—the minority business community as well as the small business community is not monolithic, and at the agency, we have got to make sure that we have capital programs, capital resources available for businesses wherever they are. Another advantage for your support of the Small Business Jobs Act was the ceiling for our 7(a) program was raised to $5 million and there are firms, if they are manufacturing companies, for example, or franchisers, they need those higher-dollar loans. But as I have spoken about earlier, we have a large segment of our business community that needs the smaller dollar loans. Then there are businesses that are looking for an equity infusion and that is where the Impact Fund comes in.

I would be happy to come back and talk to the committee at a later date when we have more of the structure of the Impact Fund in place, but in the meantime, I am talking everywhere I go about the Impact Fund to encourage a very diverse set of interests in the fund so that we can, at the end of the day, have a strong and a diverse portfolio of managers who are ready and capable of serving businesses in underserved communities and across the board.

Senator HAGAN. Well, in many instances, those smaller loans are the hardest ones for small business owners to actually have access

to, and so I do think it is important that you continue focusing in that area——

Ms. JOHNS. Yes, Senator——

Senator HAGAN [continuing]. Which is what this is.

Ms. JOHNS. Yes. And if I may, Senator, I mentioned in my opening statement that we are a month ahead of schedule in getting the Small Loan Advantage Program up and running, and in fact, just yesterday, I learned of one of the first Small Loan Advantage loans was taken on by, as it turns out, an African American pharmacist in rural Georgia who took out an $80,000-plus Small Loan Advantage loan in order to expand her—it is a working capital loan in order to expand her footprint of pharmacies in rural Georgia. So I was very excited to get that news because that is exactly the kind of thing that we were hoping to see with the Small Loan Advantage and we just look forward to that continuing.

Senator HAGAN. Thank you.

Chair LANDRIEU. Thank you.

We really appreciate your testimony this morning. We are going to move to the second panel. Any additional questions can be submitted to Ms. Johns.

And I just want to submit for the record, following Senator Snowe's comments about the highlights of the GAO study on the substantial abuses in the HUBZone program, and this is going to be the subject of our hearing the week of April 14, just to give everyone notice. We are going to have a two- or three-hour hearing on streamlining fraud and abuse in the SBA. Of course, those questions are always relevant in any meeting that we have, but this Chair feels very strongly about some of those same issues and we will be going into some detail about the fictitious firms that filed addresses for HUBZones using The Alamo in Texas, a public storage facility in Florida, and a city hall in Texas as their principal office locations that should have easily been identified as fraud when they applied and self-certification.

Thank you, Ms. Johns.

The second panel, if you all would come forward and I will introduce you as you are seated.

To keep us moving, Dr. Robert Fairlie will be testifying first. He is a Professor of Economics at the University of California. He has done extensive research on entrepreneurship, technology, inequality, labor economics, and education. He testified before the committee last year and we are looking forward to having him testify this morning.

Our second witness is Marc Morial, former Mayor of New Orleans and outstanding leader for the city, region, and nation. He is an entrepreneur, lawyer, professor, President of the U.S. Conference of Mayors, and is currently serving as CEO of the National Urban League. We welcome Mayor Morial to be with us today. He is leading a national effort in this regard and we are very pleased to hear his strategies this morning.

Our next witness is Susan Allen. Ms. Allen founded U.S. Pan Asian American Chamber of Commerce. She became the National President and CEO in 2001 after a 17-year career in law. President Bush appointed her to the Council of Administrative Conference of the United States. She is a recipient of numerous awards and we

are looking forward to her testimony, particularly in regards to the Asian American community.

Doyle Mitchell is our next witness. Doyle is President and CEO of Industrial Bank, headquartered here in D.C. He also serves as Chairman of the National Bankers Association, which was founded in 1927 as the trade association for the 103 minority- and women-owned banks in America. We look forward to his testimony this morning.

And Martha Montoya is the owner and partner of three companies, Los Kitos and several others, including a newspaper. She serves as Procurement Chair and Board member of the Hispanic Chamber. We are looking forward to hearing her testimony, as well.

But why do we not start with Dr. Fairlie to sort of lay the data out, and then we will be hearing comments from men and women who work in this area to close this gap every day and to hear from them the kind of strategies that may be working, the things that they see that are not working, or any ideas that they would have to share with the committee about how we can continue to expand opportunities in the development of minority-owned businesses in our country to help close this wealth gap that is quite startling.

Dr. Fairlie.

STATEMENT OF ROBERT W. FAIRLIE, PH.D., PROFESSOR OF ECONOMICS, UNIVERSITY OF CALIFORNIA, SANTA CRUZ

Mr. FAIRLIE. Thank you, Chair Landrieu, Ranking Member Snowe, and members of the committee.

Chair LANDRIEU. Could you pull the microphone a little bit closer to you, please, and when all of you speak—yes, and pull the seat in. Thank you.

Mr. FAIRLIE. Thank you, Chair Landrieu, Ranking Member Snowe, and Senator Hagan. It is an honor to testify in front of you on the important topic of wealth and equality and access to capital for minority businesses.

I am a Professor of Economics at the University of California at Santa Cruz and have studied small business and entrepreneurship issues for almost 20 years. I am here to talk briefly about the findings from my research on the topic.

The great recession ended in December 2009, more than a year ago, but the national unemployment rate remains above nine percent. Fourteen million people are still looking for jobs and a record number have been jobless for more than a year. Although many people have turned to self-employment in the face of limited employment opportunities, it is not an easy time to start businesses.

Small businesses are continuing to be hit hard by the sluggish economy. The rate of businesses filing for bankruptcies in the United States is more than twice as high as it was in mid-2007. Contributing to the high rate of business closings are the lingering tight credit conditions faced by small businesses. Housing prices have also not rebounded from the beginning of the recession, which is important because home equity is often used to finance business starts.

Minority-owned businesses are being hit especially hard in the current economy. Research that I and others have conducted indi-

cates that minority businesses face significant barriers to entry, growth, and survival, even in more favorable economic conditions. Minority firms are more vulnerable because they are generally smaller and have fewer resources to draw on in difficult economic times. The average minority-owned business has revenues of $178,000 per year, which is less than 40 percent of the non-minority level. Minority-owned firms also hire fewer employees and have lower profit levels.

One of the most important factors responsible for these disparities in business performance is access to financial capital. A large body of research shows that limited access to financial capital hinders the formation and growth of minority businesses. Minority-owned businesses have substantially lower levels of financial capital invested in their businesses.

The first figure I wanted to show is estimates from the Federal Reserve, the latest estimates available showing the amount of equity and loan investments in minority firms. And what you see is startling low levels of investments, on average. What we find is that minority firms have about $3,400 of equity investments in their firms, on average, and $46,500 of loan amounts. The levels for non-minorities are more than twice that level, okay. What I also found doing research on this is these disparities do not go away when I control for owner and firm characteristics, and others and I have also found this in other data sources.

One of the major causes of this lack of access to capital is the shockingly high level of wealth inequality found in the United States. The disparity in wealth between minorities and non-minorities is an order of magnitude larger than income inequality. So estimates of median net worth are displayed in the next figure. What we find here is the latest data available are from 2004 from the Census Bureau, and what we find is that African American families have $8,700 in median wealth. Latino families have $13,400 in medial wealth. White levels are over $100,000 higher and they are nine to 13 times higher than these levels.

These low levels of wealth are a problem. They translate into fewer start-ups and undercapitalized businesses because an entrepreneur's wealth is often used to finance a business. Entrepreneurs are also frequently required by investors to invest their own money in the business as an incentive.

Contributing to the patterns in wealth inequality are low rates of minority home ownership and lower levels of home equity. The next figure shows the latest data available for 2010 on home ownership rates. What I found is that less than half of minority families have a home, or own a home, whereas three-quarters of non-minority families own a home. So there are major differences in home ownership.

But some new data that I wanted to present shows banking rates from a new study by the FDIC and the Census Bureau, and what it shows is a striking number of minority families do not have a banking account, either through a savings or checking account. More than 20 percent of Latino and 20 percent of African American families do not have a bank account, whereas the level for whites is around three percent. The same data from the FDIC and Census

Bureau show that minorities are more likely to use higher-cost financing services, such as payday loans.

Further limiting the ability of minority entrepreneurs to obtain financial capital is lending discrimination, which I show in the next figure. What I find here is that minority firms are more likely to experience loan denials, pay higher interest rates, and are less likely to apply for loans because of a fear of rejection in those loans. The minority levels of applying for loans and getting loan acceptances are more than twice as high, and minority firms that do get loans pay one-and-a-half percentage point higher interest rates on those loans.

The minority-owned businesses make enormous contributions to the U.S. economy. Businesses owned by minorities produce more than $1 trillion in total sales, they employ six million workers, and have an annual payroll of $168 billion. They also create another six million jobs for themselves as the owners of those businesses.

In closing, although minority-owned firms contribute greatly to the economy, there remains a lot of untapped potential among these firms. As I have discussed minority entrepreneurs face substantial barriers to obtaining financial capital. These barriers include low levels of wealth, low rates of home ownership, low rates of banking, and lending discrimination. Restricting minority businesses in their growth ultimately limits total U.S. productivity, job creation, and innovation, which are all essential for getting our economy back on track.

Thank you for the opportunity to present the findings from my research. I look forward to hearing your comments.

[The prepared statement of Mr. Fairlie follows:]

Closing the Gap: Exploring Minority Access to Capital and Contracting Opportunities

U.S. Senate Committee on Small Business & Entrepreneurship

March 3, 2011

Testimony by:

Robert W. Fairlie
Professor of Economics
University of California, Santa Cruz

Thank you, Chair Landrieu, Ranking member Snowe, and members of the Committee. It is an honor to testify before you on the important topic of wealth inequality and access to capital for minority businesses. I am a Professor of Economics at the University of California, Santa Cruz and have studied small businesses and entrepreneurs for almost 20 years. I have been asked to briefly discuss the findings from my research on the topic.[1]

The Lingering Effects of the Great Recession

The Great Recession ended in December 2009 – more than a year ago. But, the national unemployment rate remains above 9 percent. Fourteen million people are still looking for jobs and a record number have been jobless for more than a year. Although many people have turned to self-employment in face of limited employment opportunities, it is not an easy time to start a business.

Small businesses are continuing to be hit hard by the sluggish economy. The rate of businesses filing for bankruptcies in the United States is more than twice as high as it was in mid 2007. Contributing to the high rate of business closings are the lingering tight credit conditions for small businesses resulting from the financial crisis. Housing prices have also not rebounded from the beginning of the recession which is important because home equity is often used to finance business starts.

Minority-owned businesses are being hit especially hard in the current economy. Research that I and others have conducted indicates that minority businesses face significant barriers to entry, growth and survival even in more favorable economic conditions. Minority firms are more vulnerable because they are generally smaller and have fewer resources to draw on in difficult economic times. The average minority-owned business has revenues of $178,000 per year, which is less than 40 percent of the level for non-minority businesses. Minority owned firms also hire fewer employees and have lower profit levels.

Access to Capital among Minority-Owned Businesses

One of the most important factors responsible for these disparities in business performance is access to financial capital. A large body of research shows that limited access to capital hinders the formation and growth of minority-owned businesses.

Minority-owned businesses have substantially lower levels of financial capital invested in their businesses. Figure 1 displays estimates from Federal Reserve data indicating that minority firms have much lower levels of equity investments and loan amounts than non-minority firms.

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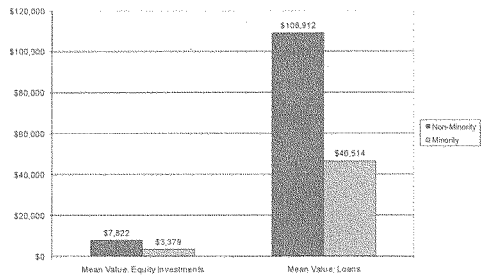
[1] For more information see Robert Fairlie and Alicia Robb, *Race and Entrepreneurial Success: Black-, Asian-, and White-Owned Businesses in the United States* Cambridge: MIT Press (2008). Robert Fairlie and Alicia Robb, *Disparities in Capital Access between Minority and Non-Minority-Owned Businesses: The Troubling Reality of Capital Limitations Faced by MBEs.*, U.S. Department of Commerce, Minority Business Development Agency, January 2010.

Figure 1: Average Equity Investments and Loan Sizes
Federal Reserve, Survey of Small Business Finances, 2003

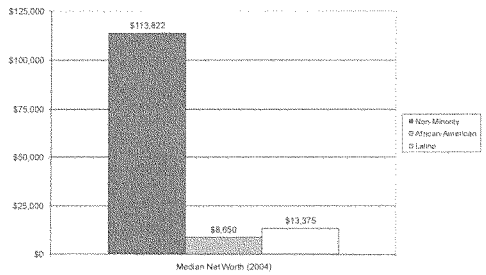


Minority-owned businesses have an average of $3,400 of equity investments and $46,500 in loans. Non-minority owned businesses have values of equity investments and loans that are more than twice as large. These disparities do not disappear even after controlling for owner and firm characteristics, and have been found in several other data sources.

Wealth Inequality

One of the major causes of the lack of access to capital is the shockingly high level of wealth inequality found in the United States. The disparity in wealth between minorities and non-minorities is an order of magnitude larger than the disparity in income, for example. Estimates of median net worth from the Census Bureau are displayed in Figure 2.

Figure 2: Median Household Wealth (Net Worth)
U.S. Census Bureau



Half of all African-American families have less than $8,700 in total wealth, and half of all Latino families have less than $13,400. These levels of wealth are one-ninth to one-thirteenth the levels of wealth held by non-minorities ($113,800).

These low levels of wealth among minorities translate into fewer startups and undercapitalized businesses because an entrepreneur's wealth is often invested directly in the business or used as collateral to obtain business loans. Entrepreneurs are also

frequently required by investors to invest their own money in the business as an incentive.

Contributing to the patterns in wealth inequality are low rates of minority home ownership and lower levels of home equity. Estimates of home ownership from the Census Bureau are displayed in Figure 3. Less than half of African-American and Latino families own their own homes compared with roughly three-quarters of non-minority families.

Figure 3: Home Ownership and Unbanked Rate
U.S. Census Bureau, Bureau of Labor Statisics and FDIC

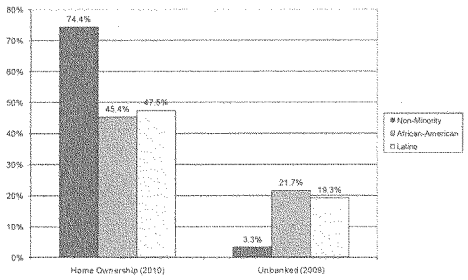


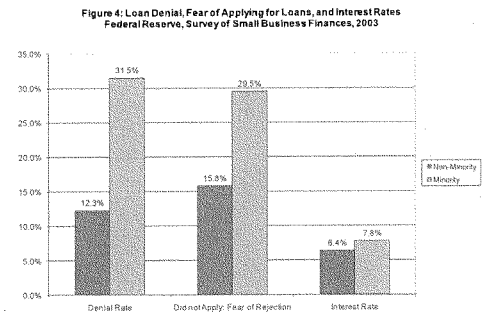
Figure 3 also displays recent estimates from a joint study by the Census Bureau, BLS and FDIC on unbanked rates. As both a symptom and cause of wealth inequality many minority families do not have a savings or checking account. More than 20 percent of African-American families and just under 20 percent of Latino families do not have a bank account. The same data indicate that minorities are more likely to use higher-cost financial services such as payday loans.

Lending Discrimination

Further limiting the ability of minority entrepreneurs to obtain financial capital is racial discrimination in lending practices. Several studies have examined whether minority firms face discrimination in obtaining business loans.[2] The main finding from this

[2] David G. Blanchflower, P. Levine, and D. Zimmerman, "Discrimination in the Small Business Credit Market," *Review of Economics and Statistics* 85, no. 4 (2003): 930-943. Ken Cavalluzzo, Linda Cavalluzzo, and John Wolken. "Competition, Small Business Financing, and Discrimination: Evidence from a New Survey," *Journal of Business* 75, no. 4 (2002): 641-679. Ken Cavalluzzo and John Wolken, "Small Business Loan Turndowns, Personal Wealth and Discrimination," *Journal of Business* 78, no. 6 (2005): 2153-2177. Lloyd Blanchard, John Yinger and Bo Zhao, "Do Credit Market Barriers Exist for Minority and Women Entrepreneurs?" Syracuse University Working Paper (2004). Susan Coleman, "The Borrowing Experience of Black and Hispanic-Owned Small Firms: Evidence from the 1998 Survey of Small Business Finances," *The Academy of Entrepreneurship Journal* 8, no. 1 (2002): 1-20. Susan Coleman, "Borrowing Patterns for Small Firms: A Comparison by Race and Ethnicity." *The Journal of Entrepreneurial Finance & Business Ventures* 7, no. 3 (2003): 87-108. K. Mitchell and D.K.

literature is that minority-owned businesses are more likely to experience loan denials, pay higher interest rates, and are less likely to apply for loans because of a fear of rejection. Figure 4 reports estimates from an analysis that I conducted with Federal Reserve data.



These data show that minority firms are twice as likely to be denied a loan application and are twice as likely to not apply for a loan because of a fear of rejection. Minority firms that do obtain loans pay one and a half percentage points higher interest rates on those loans than non-minority firms. These disparities do not disappear even after controlling for the age, experience and education of the owner, and the creditworthiness, size, industry, age and location of the firm, which is consistent with the existence of lending discrimination.

The Potential of Minority-Owned Businesses

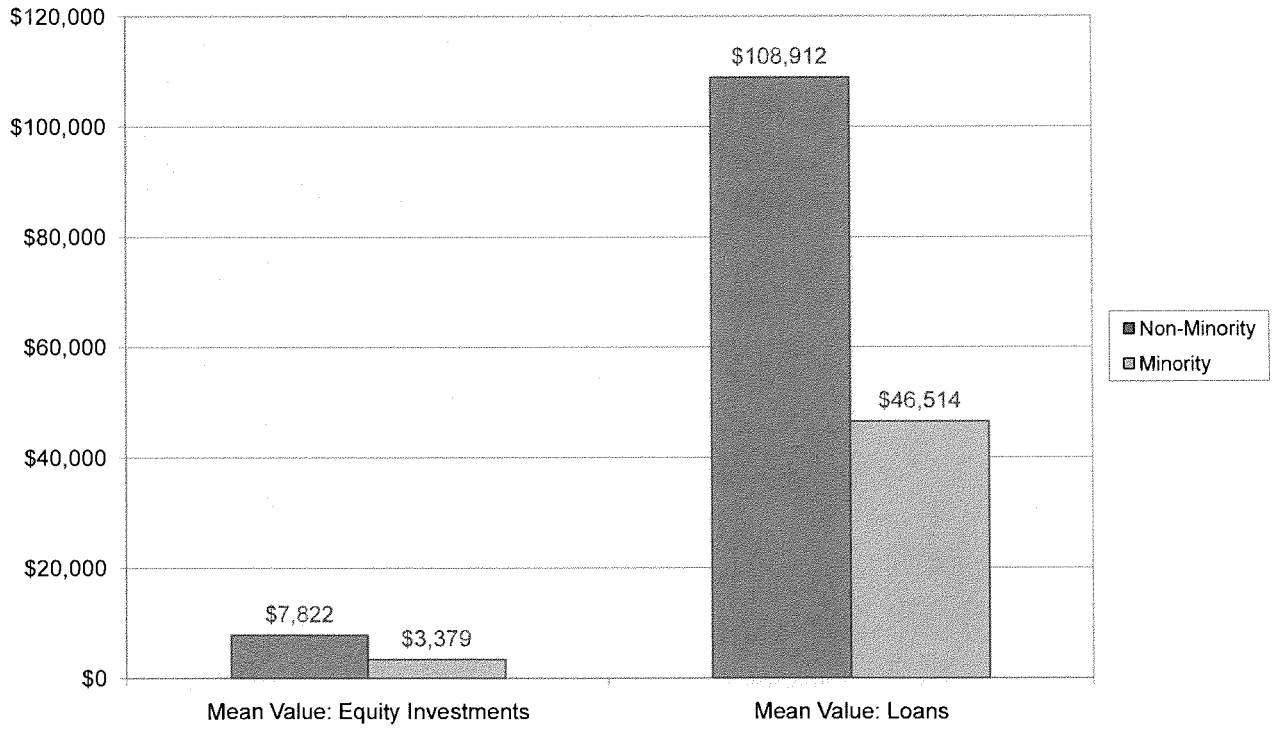
Minority-owned businesses make enormous contributions to the U.S. economy. Businesses owned by minorities produce more than $1 trillion in total sales. They employ 6 million workers and have an annual payroll of $168 billion. They also create another 6 million jobs for themselves as owners.

In closing, although minority-owned businesses contribute greatly to the economy, there remains a lot of untapped potential among this group of firms. As I have discussed, minority entrepreneurs face substantial barriers to obtaining financial capital. These barriers include low levels of wealth, home ownership and banking, and lending discrimination. Restricting minority business growth ultimately limits total U.S. productivity, job creation and innovation, which are essential for getting our economy back on track.

Pearce, *Availability of Financing to Small Firms using the Survey of Small Business Finances*, U.S. Small Business Administration, Office of Advocacy (2005). R. Bostic and K.P. Lampani, "Racial Differences in Patterns of Small Business Finance: The Importance of Local Geography," Working Paper (1999).

Thank you for the opportunity to present the findings from my research on this topic. I look forward to hearing your comments and questions.

Figure 1: Average Equity Investments and Loan Sizes
Federal Reserve, Survey of Small Business Finances, 2003



Robert W. Fairlie
Background and Experience

Dr. Fairlie is Professor of Economics at the University of California, Santa Cruz, Director of the UCSC Masters Program in Applied Economics and Finance, and adjunct researcher at RAND. He was a Visiting Fellow at Yale University, Australian National University, and the Institute for the Study of Labor (IZA), Germany. His research interests include entrepreneurship, technology, inequality, labor economics, education, and immigration. He recently published "Race and Entrepreneurial Success: Black-, Asian-, and White-Owned Businesses in the United States" with MIT Press. He is also author of the Kauffman Index of Entrepreneurial Activity. His research has been published in leading economics, public policy, management and demography journals. He has testified to the U.S. Congress, U.S. Department of Treasury, and the California State Assembly regarding the findings from his research. Dr. Fairlie holds a Ph.D. and M.A. in Economics from Northwestern University and a B.A. with honors from Stanford University.

Chair LANDRIEU. Thank you, Dr. Fairlie.

Before we move to Mayor Morial, could you present to this committee the Asian American population, because it is helpful to have African American, Hispanic, and Asian, and if you can do it today, that is great, and if not, if you would just submit it, that would be helpful.

Mayor Morial.

STATEMENT OF MARC MORIAL, PRESIDENT AND CHIEF EXECUTIVE OFFICER, NATIONAL URBAN LEAGUE

Mr. MORIAL. Thank you very much, Senator Landrieu. Let me, first of all, thank you for calling this hearing and also Ranking——

Chair LANDRIEU. Can you speak a little bit closer into the microphone? I am sorry.

Mr. MORIAL. Thank you. Is that better?

Chair LANDRIEU. It is better.

Mr. MORIAL. Let me thank you for calling this hearing and for inviting me here today. Also, to Ranking Member Snowe, let me thank you also for being here today, and both of you for your leadership.

I want to cover a few areas, and on behalf of the National Urban League, we are absolutely committed to the growth and the strength of small businesses with a particular focus on the nation's businesses owned by people of color.

One, I want to outline four key challenges that confront minority-owned businesses in the United States. One is the need for effective communication of programs that are intended to benefit and assist Minority Business Enterprises.

Two, and Dr. Fairlie has talked about this, access to reasonably-priced capital through private sector commercial sources.

Number three, access to Federal, State, and local contracting opportunities, either prime or subcontracting opportunities.

And number four, lack of adequately designed measures of assistance, whether they are poorly designed lending initiatives or inadequate forms of technical assistance.

Let me say this, because this point should not be lost. There is tremendous job creating potential in the nation's black-owned small businesses and other MBEs. Why? If one in three of this nation's micro enterprises—just one in three—those are those with fewer than five employees—were to add one additional employee, we would be at full employment. If one of three of the nation's micro enterprises added one employee, we would be at full employment.

Number two, self-employed business owners earn more on average than wage and salary workers. And there is evidence that disadvantaged workers have more upward income mobility and faster earnings growth than disadvantaged wage and salary workers.

Number three, black-owned firms outpaced the growth of non-minority firms based on the Census report that just came out, which studied the period from 2002 to 2007. These are interesting numbers. The gross receipts of African American firms increased by 55 percent. Their employment increased by 22 percent. And the number of firms increased by 61 percent. And while most of the firms in the black community are very small, African American firms with receipts of $1 million or more generate a large percentage of

all the revenues generated by all African American businesses. The fact of the matter is that black-owned businesses in this country remain very small.

Now, if black-owned small businesses reach representative parity, that is, 13 percent of the U.S. adult population, meaning if black-owned small businesses were proportionate in size, there would have been 3.3 million firms generating $1.4 trillion in gross receipts and creating seven million jobs instead of less than a million jobs.

My point is very simple. Investing in the nation's minority-owned small businesses is a way to create jobs for all. It is a way to build the economy of the United States. If minority-owned businesses, particularly African American-owned businesses, could grow that fast—notwithstanding all of the barriers that have been documented and that will be documented on this panel—it goes without saying that if these barriers were lessened, if some of these restrictions were loosened, then these businesses would grow at an even more rapid pace, which would be good not only for the African American community and the minority business community, but good for the nation at large.

A couple of recommendations that we make as the National Urban League to promote the growth of MBEs. One, raising the cap for set-aside small business contracts from $100,000 to $500,000.

Unbundling contracts, that would be helpful in assisting small and minority-owned businesses to have the opportunity to bid on Federal contracts.

Number three, increasing Federal procurement goals and the development of subcontracting plans as well as a more effective way to monitor, create transparency, and push the agencies in the Federal Government towards greater performance in meeting the goals that are already on the books.

And number four, a technical assistance fund, perhaps run through the MBDA, that could assist minority and other women-owned businesses.

And finally, the elimination of SBA guarantee fees, and we suggest the elimination of the guarantee fee on the SBA's new Advantage Loan initiative. This fee can run from two to 3.8 percent of a loan amount, which adds to the cost of borrowing and makes it expensive. We applaud the efforts to create new loan products, but we urge diligence and vigilance on the cost of these products so that on one hand we are not taking a powerful step forward and then taking two steps back by simply making capital so expensive and so burdensome that it affects growth.

My final point is to share with you the successes we have had at the National Urban League. We operate today nine Entrepreneurship Centers. These are small business assistance centers funded with private dollars. We serve approximately 6,000 businesses a year. We have learned through that experience sometimes that partnership efforts between the government and the private sector can yield more benefits.

So let me thank you for your time. Thank you for giving me this time, and I will be happy to answer any questions.

[The prepared statement of Mr. Morial follows:]

National
Urban League

Empowering Communities.
Changing Lives.

TESTIMONY OF
MARC H. MORIAL
PRESIDENT AND CEO
NATIONAL URBAN LEAGUE
BEFORE FOR THE
US SENATE COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP
THURSDAY, MARCH 3, 2011
"CLOSING THE GAP: EXPLORING MINORITY ACCESS TO CAPITAL AND CONTRACTING OPPORTUNITES"

Madame Chair, Ranking Member Snowe, members of the Committee, thank you for the opportunity to testify today on the challenges facing minority-owned small business in America. I am Marc Morial, President and CEO of the National Urban League. Established in 1910, the National Urban League is the nation's oldest and largest civil rights and direct services organization serving 2.1 million people each year in over 100 urban communities.

The guiding mission of the National Urban League throughout its one hundred year history has been the economic empowerment of our nation's economically disadvantaged. Every day our affiliate CEOs and their staff members assist our constituents in the pursuit of economic self-sufficiency. One of the most fundamental elements of any such economic self-sufficiency is the role of the entrepreneur. It is increasingly the case in modern America that the person most-likely to sign your paycheck is the person living at the end of your street, in line next to you at the grocery, or in the pew next to you at your house of worship. Nowhere is this more-true than in the black community.

Small businesses have always played a critical role in the economic well-being of communities of color. The Great Recession of recent years has made this fact of life an even greater reality. Recent statistics published by the US Census Bureau show that the black-owned business grew by 60% in the 5-year period between 2002 and 2007[1]. While these

[1] *"US Census Bureau Survey of Business Owners: Black Owned Business"* Census Bureau Economic Data Released February 8, 2011.

numbers might seem on their face as evidence of widening economic prosperity, they in are actuality, evidence of a new class of entrepreneurs of circumstance, borne of the increasingly dismal job market confronting African American and Hispanic workers alike. Within these numbers lie evidence of the role entrepreneurship plays in communities where big-business hiring has slowed to a trickle, or even frozen to a complete halt. Of the 1.9 million American small businesses identified by the US Census Bureau as being African-American owned, over 1.8 billion are sole proprietorships – that is to say, single worker enterprises where the owner is usually the only employee of the company. Yet, in the larger economic picture, black-owned business is one of the greatest untapped resources in America's economic arsenal. African-American owned firms have proven to be an engine of job creation, with paid employment growing by 22% from 2002 through 2007, compared to less than 1% such growth for non-minority owned firms.[2] Nowhere else is the commonly-acknowledged phenomena of the small business sector as a staging ground for economic recovery more factual than in communities of color.

Consequently, were African-American owned small businesses to reach representative parity with the African-American portion of the adult US population in 2007, there would have been 3.3 million firms (instead of 1.9 million) generating $1.4 trillion in gross receipts (instead of $138 billion), and creating 7.1 million jobs (instead of 921,000).

So what's holding us back? Unfortunately Madame Chair, as I'm sure you might have guessed, there is much more to the story. Minority Business Enterprises (MBEs) face major systemic challenges that make their success an uphill battle against the odds from the moment of their inception, and at every step of the way to success. We see these challenges as falling into four primary categories:

1. Clear communication of programs that are intended to assist MBEs. Many MBEs are either unaware of programs geared toward MBE development or the information is not clearly communicated which leads to missed opportunities and frustration on the part of the business owner.

2. Access to reasonable priced capital through private-sector commercial sources. Most MBEs have to settle for either high priced alternative capital sources or the use of personal resources such as

[2] "*African-American-Owned Firms Outpace Growth of Non-Minority-Owned Firms,*" by Ivonne Cunnaro, Chief Knowledge Management Officer, US Department of Commerce Minority Business Development Agency, February 8, 2011.

their own credit cards to have the capital necessary to start or grow their business concerns

3. Access to federal contracts, either prime or subcontract opportunities. Many MBEs do not where contract opportunities are posted or how to access the federal on-line system. Also given that many prime contractors need MBE participation, MBEs need to know how to access and identify these opportunities.

4. Technical assistance that is provided for the many different levels of MBEs. Currently many technical assistance programs are not well publicized, and very often are not suitably geared toward the target market of MBEs that are at different levels in their business development

1) The Problem of Communication:

While the Small Business Administration (SBA) and the Minority Business Development Agency (MBDA) have done a remarkable job advocating for, and introducing new programs intended to help MBEs gain increased levels of access to government-sponsored capital, many such programs go undersubscribed due to a lack of awareness among the target audience. While the SBA often touts the number of Business Development Centers it sponsors throughout the country, those MBE owners who routinely enter our NUL Entrepreneurship Centers for management training and technical assistance have no idea of our SBA-sponsored counterpart's existence, or what avenues to capital these SBA centers might offer. MBEs are largely unaware of the currently outdated modes of SBA outreach, including traditional press releases, or jargon-heavy government announcements buried in the bowels of a cumbersome, non-user friendly website. While NUL certainly does not have the outreach budget of the SBA, or the Department of Commerce, our Entrepreneurship Centers are in the community, and our target service audience knows exactly where we are. The same must be made true of SBA and MDBA.

2) The Problem of Access to Reasonably-Priced Capital:

Given the hearty brand of survivalist entrepreneurship within the mindset of many MBE owners, their next course of action is typically that of self reliance. MBEs without access to traditional sources of private sector

capital are often forced to 'go-it-alone' delving in to already limited means of personal capital, or even financing their enterprises by way of personally-secured high-interest rate debt – the only form readily available to the MBE – with disastrous results.

It's a commonly-accepted fact that firms with higher levels of start-up capital are less likely to close, more likely to have higher profits and revenues, and much more likely to hire employees than those without. The median level of wealth for African-Americans is $6,166, compared with $67,000 for whites. As a result, African American-owned small businesses often start with substantially lower levels of financial capital than white owned firms, making the presence of reasonably priced capital extraordinarily crucial to success of MBEs during their early incubation.[3]

3) The Problem of Access to Federal Contracting Opportunities:

Perhaps one of the most ineffective means of opportunity made available to MBEs is that of the competitive federal contract. Much to their credit, the federal government, and in particular the Senate Small Business and Entrepreneurship Committee and the Obama Administration, understand the vital role federal contracting opportunities can play in the success of any small business. Last year alone, the federal government purchased over a half trillion dollars in goods by way of contracts with private vendors. Now, undoubtedly, this entire amount was not contracted to small businesses, but a significant portion of the whole is contracted to small enterprises each year. Why then is it so difficult for MBEs to procure a larger share of such contracts? There is quite literally a host of systemic reasons.

- Cumbersome and desperately complicated means of gaining announcement information and applying for contracts (i.e., Fedbizopps.gov, the government's primary website for public access to contract information.)
- Ineffective and poorly enforced policies designed to heighten access for MBEs.
- Skeleton staffing in the area of federal procurement that breeds shortcuts and awards to the 'known quantity', or the same fortunate few MBEs that have won awards in the past

[3] *"Race and Entrepreneurial Success: Black, Asian, and White-Owned Businesses in the United States"*, by Robert W. Fairlie and Alicia M. Robb, September, 2008.

- A lack of outreach and technical assistance. Literally scores of qualified potential MBE contractor application are disqualified outright given minor procedural flaws.

4) The Problem of Appropriately Designed Remedies:

The term minority-owned small business is by no means a 'one-size-fits-all' proposition. A recent US Census Bureau survey of black-owned business in 2007 highlights the sheer numerical differences between the top and the bottom of the black-owned small business spectrum. Of the 1.9 black-owned small businesses recorded in 2007, only 14,000 had revenues over $1 million, while 87% of the 1.9 million had revenues below $50,000 annually. While the capital access and technical assistance needs of these two separate classes within MBEs are obviously different, it should be acknowledged and understood that a small business lending initiative targeted for those enterprises with $1 - $4 million in annual revenues[4], such as the Startup America initiative recently announced by the White House, misses at least 87% of black-owned small business, and could potentially serve only 14,000 out of 1.9 million – or less than 0.1% at best. Whether capital access or technical assistance, when it comes to MBEs, all too often the proposed cure is not properly prescribed in a dosage suited to help the patient.

The National Urban League has a long-established record of successfully serving MBEs at all levels through our network of Entrepreneurship Development Centers and other community affiliates

The National Urban League's Entrepreneurship Center Program (ECP) enables minority entrepreneurs to take advantage of new business opportunities and qualify for financing that will lead to high-level business growth through the provision of proper management skills. Entrepreneurs who qualify for the program receive individualized management assistance and group training services designed to increase their business acumen and ability to operate their businesses on a profitable basis, increase their market share and offer living wage employment opportunities to residents in their market area.

The Entrepreneurship Center program is in its 6th year of operation. Currently there are nine centers, which operate in Atlanta, GA, Chicago,

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[4] *"Obama Administration Commitments: Expanding Access to Capital for Entrepreneurs"* Startup America online fact sheet, http://www.whitehouse.gov/startup-america-fact-sheet#administration.

IL, Cincinnati, OH, Cleveland, OH, Jacksonville, FL, Kansas City, MO, Los Angeles, CA, New Orleans, LA and Philadelphia, PA.

In 2010, the centers provided 10,911 hours of counseling and 11,242 hours of training services to 5,938 entrepreneurs. These services assisted entrepreneurs in receiving $20.19 million in new bonding, new contracts and financing during the year.

National Urban League Recommendations for Promoting the Growth of MBEs

Madame Chair, the numbers show that the development of the economic power within MBEs and their respective communities is not a black problem, or an issue relegated to any one class or grouping of individuals – it is a distinctly American problem, or perhaps stated more accurately, a matter of American potential. Our country cannot reasonably hope to outpace the growing economic and productive momentum of our international competitors with such a large swath of our productive capability willfully left to idle. MBEs have already demonstrated their propensity for survival and growth by expanding in the face of economic headwinds that have stalled the progress of even the most resilient sectors of our economy. It is time that our country set about a course of dramatic and sustained steps in support of black-owned, as well as all other minority and women owned small business enterprises.

- **Raising the Cap for Set-Aside Small Business Contracts** – We suggest that the cap for set-aside small business contracts be increased from $100,000 to $500,000. This will allow the increasing number of small- and minority-owned businesses to participate in set-aside contract opportunities, thus providing more growth opportunities for businesses that have the capacity to perform on contracts up to $500,000.

- **"Bundled Contracts"** – We suggest that "unbundling contracts" will be helpful in allowing more small- and minority-owned businesses to have the opportunity to bid on federal contracts. This should define the contract amounts at which unbundling will take place, and define what a small business concern is to clarify size standards. To this end we would recommend language stating that, the small

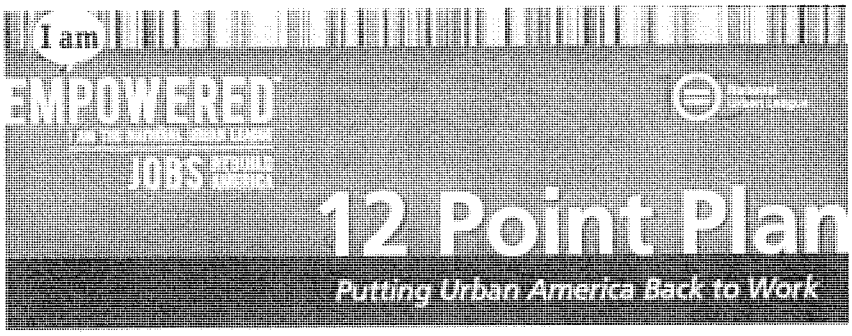
business size standards shall be those that have been set by the US Small Business Administration and should be published on their web site for public viewing.

- **Increasing Federal Procurement Goals and Subcontracting Plan** – We suggest increasing the federal procurement goals for small- and minority-owned businesses and the requirement of a subcontracting plan would need to include a non-federal monitoring system which ensures that each agency is working toward these goals. We recommend that monitoring should be performed by *an independent* non- profit or for- profit firm that has experience in the oversight of public procurement programs for small and minority business owners. This will provide an impartial overview of the program activities and can provide recommendations on how to make the program more effective if necessary. A good example of an independent monitor would be the Greater Baltimore Urban League which has been successful in monitoring and increasing small and minority business participation in public procurement in Baltimore over the past few years.

- **Technical Assistance Fund** – We suggest the creation of a fund for technical and contracting assistance through the Minority Business Development Agency (MBDA). We recommend that this should be open to service providers in and outside the MBDA network as more minority business owners can be identified and participate in the program.

- **Elimination of SBA Guarantee Fees-** We suggest the elimination of the guarantee fee on the SBA's new Advantage loan initiatives as a way to stimulate loan activity for small and minority businesses. The guarantee fee which can run from 2- 3.8% of the loan amount make the cost of borrowing expensive for small and minority business owners. The elimination of these fees would borrowing more affordable and was successful as part of the stimulus efforts last year.

Thank you for the opportunity to testify and I will be pleased to answer any questions.



National Urban League Proposes A Dozen Dynamic Ideas for Urban America

As a historic civil rights organization devoted to the economic empowerment of underserved communities, the National Urban League has witnessed debilitating impact of the nation's current employment crisis firsthand. Our 98 local affiliates, which serve 300 communities, are economic first-responders in the ongoing effort to help ease the burden of those most profoundly affected by this recession, serving some 2.1 million citizens in 2010 alone.

Record numbers of Americans were forced into foreclosure in 2010, and many urban families in communities already long beset by economic stagnation are enduring unemployment rates as high as 20%.

Even though we rigorously applaud a growing economy, and the substantial new jobs created in 2010, the economic recovery is hollow and incomplete if it does not include jobs for all Americans, especially those who have borne the brunt of the Great Recession.

Without a national effort to invest in economic opportunity for all, any statistical return to prosperity will continue to fall far short of real 'recovery' for millions of Americans – and with truly disastrous consequences.

With this fact in mind, the National Urban League's Jobs Rebuild America Plan offers a dozen dynamic and imaginative measures to both rescue those most profoundly affected by the ongoing economic emergency, while also remedying many of the underlying causes behind the recession's inordinate and seemingly-amplified impact on the communities we serve:

1. **Restore the Summer Youth Jobs Program as a Stand-Alone Program Employing 5 million Teens in Summer 2011** through a new investment of $5-7 billion. Under the Workforce Investment Act (WIA), the summer jobs program lost its status as a stand-alone program with its own dedicated funding and instead became one of ten programs that states could elect to fund using the WIA funds designated for youth services. In addition, WIA required year-round participation in order for disadvantaged youth to be eligible to participate during the summer. This requirement increased the cost considerably and severely limited the number of participants. Since the changes adopted in WIA became effective in 2000, there has been a dramatic decline in the share of teenagers who are employed over the summer months. According to research by the National Urban League Policy Institute, between 2000 and 2009, the share of teenagers who were employed was down 40 percent for blacks and down 35 percent for whites. Teenage summer labor force participation has also declined dramatically and progressively since 2000 – from 52 percent in the summer of 2000 to 38 percent in the summer of 2009. Even before the curtailing of the dedicated summer jobs funding in 2000, the portion of black teenagers employed during the summer was consistently about 20 percentage points lower than their white counterparts. This is critical to the future of the American workforce because lack of early labor market experience has significant effects on future earnings and productivity.

2. **Create 100 Urban Jobs Academies to Implement an Expansion of the Urban Youth Empowerment Program (UYEP)** to employ and train the critically unemployed. UYEP, a four-year demonstration project created in partnership with the Department of Labor in 2004, is a youth career preparation initiative designed for at-risk, out-of-school, and adjudicated youth and young adults between the ages of 18 and 24. With 27 National Urban League affiliate sites and a total of $29.3 million, the program served 3,900 youth, 65% of whom either had job placements (paying an average wage of $9.32/hour) or completed their high school diploma or GED. 200 participants were placed in postsecondary schools or college upon completion of their secondary education. Scaling this program up to 100 sites would increase the program cost to $108.5 million

3. **Develop a Dynamic National Public Private Jobs Initiative to Create Jobs and Train Urban Residents and Stimulate Economic Growth** in the following areas:
    a. Technology and Broadband Jobs - Use unobligated Recovery Act funding to support competitive grants fueling the private creation of Urban Business Incubators, Technology Campuses from dormant industrial sites, and other measures intended to foster targeted and localized small business growth.

    b. Health Care Jobs - Use unobligated Healthcare IT funds and realized Medicare savings resulting from the Obama Healthcare Plan to expand efforts to recruit, train, and hire Urban Residents as nurses, physician assistants, etc. Develop a program not unlike the Civilian Conservation Corps aimed at retraining qualified workers while addressing a critical national need in the shortage of trained medical personnel.

    c. Manufacturing Jobs- Develop and enforce a "Buy American" Initiative promoting the purchase of American manufactured goods by federal agencies, semi-public transportation authorities, local and state governments. Incentives could include favorable government subsidized financing terms for the purchase of domestically manufactured equipment and vehicles with continued terms of renewal.

    d. Urban Transportation/Water, and Community Facilities Infrastructure Jobs - Expand public initiatives in rail projects, urban water systems maintenance and expansion, parks, public buildings, and school buildings in distressed urban communities through shared financing obligations such as the highly popular, recently expired Build America Bond program.

    e. Clean Energy Jobs – Encourage investment in clean energy businesses, particularly those that promote alternative energy and energy conservation. Targeted tax inducements for clean energy investment in urban areas, programs encouraging urban building retrofits for improved energy efficiency, measures ensuring the manufacture of clean energy infrastructure in the U.S. and multi-

government initiatives to increase the efficiency of regulatory approvals might all prove effective ideas in this area. Ineffective approaches to these issues have proven major impediments to the growth of a vibrant, sustainable clean energy manufacturing and service industry in the U.S. All inducements and reforms must be tightly targeted to benefit urban, underserved communities and be designed with a long-term focus in order to have a material impact on relevant business models.

4. **Boost Minority Participation in Information and Communication Technology (ICT) Industries.** ICT industries provide one of the most extensive job and entrepreneurship opportunities for black and urban communities. In 2002 only 42,000 minority owned businesses were in the information sector -- one of the lowest levels of minority participation. Triggering minority participation in ICT industries is critical for a robust, long-term recovery. ICT industries can greatly contribute to achieving the U.S. Department of Commerce's 2010 estimate of extra 16.1 million jobs and $2.5 trillion in gross revenues from minority owned businesses. This requires creative and efficient solutions focused on both the skills needed to get ICT industry jobs and facilitating minority entrepreneurship -- lift skills in science, technology, engineering and math, expand low-income programs of the universal service fund to broadband, reform the universal service fund to better target urban areas, adopt national policies on contracting diversity similar to those of state utilities commissions and ensure that minority intermediaries are active participants in the decision making process.

5. **Reform, Revise, and Reauthorize Workforce Investment Act** to focus on preparing and retraining workers for 21st century jobs by targeting young adults with less than college, as well as high school dropouts and older workers whose jobs were eliminated by the recession.

6. **Create Green Empowerment Zones** in areas where at least 50% of the population has an unemployment rate that is higher than the state average. Manufacturers of solar panels and wind turbines that open plants in high unemployment areas will, for a period of three years, be eligible for a zero federal income tax rate and a zero capital gains tax rate under the condition that they hire at least half of their workforce from the local high

unemployment area, and retain those workers for a minimum of three years.

7. **Expand Small Business Lending** through a series of steps:
    a. Reduce SBA Community Express loan interest rate to 1% targeted for business located in areas where local unemployment exceeds the state average

    b. Establish an additional New Markets Tax Credits Program, targeted to loan products for small businesses who wish to borrow less than $250,000 for start-up and expansion

    c. Establish a new mechanism to enforce MBE/WBE goals on federally funded projects

8. **Initiate Tax Reform** which reduces across the board rates while substantially eliminating all tax loopholes, deductions and credits. Any remaining deductions and credits must be simplified to make them better targeted and more effective at promoting important social and economic goals, particularly for low-income taxpayers and families with children (See: Bipartisan Policy Center Debt Reduction Task Force report which outlines one possible approach).

9. **Establish and Promote Multilateral International Trade Policies** that will expand the market for American goods and services to growing and emerging economies around the world; thereby generating increased demand for American exports and creating an environment for increased domestic hiring and economic growth. Trade agreements with foreign countries should be fair and balanced, creating the same opportunities for the entry of American products into overseas markets as afforded to our international competitors. Greater emphasis should also be placed on the elimination of fiscal policies used by foreign governments to artificially drive down the prices of imported goods and services through the intentional undervaluation of their respective currencies. As American households continue to deleverage and increase their savings in response to the consequences of the financial crisis, maximizing our relationships with foreign countries and servicing rapidly emerging markets are critical to stimulating robust economic growth and job creation.

10. **Enact the Urban Jobs Act (H.R. 5708)** amending the Workforce Investment Act to address the problem of unemployed youth between the ages of 18 to 24 living in urban areas and not enrolled in secondary or post-secondary school. The bill authorizes the Secretary of Labor to make grants to the National Urban League for the purpose of operating an Urban Jobs Program, based on its highly successful Urban Youth Empowerment Program (UYEP). Funds authorized will allow the National Urban League, as an intermediary to its local affiliates, to continue innovative approaches to improving the employment and educational prospects for high school drop-outs, adjudicated youth and youth at risk for gang involvement through a comprehensive set of job training, remedial education services, and mentoring.

11. **Create an Urban Homesteading Program** as a comprehensive, coordinated approach to create new homeowners by redirecting foreclosed bank owned properties into the hands of middle-class and working class families at low purchase prices and low interest rates. Support the approach with the expansion of Housing Counselors Nationwide through the investment of $500 million in housing counseling agencies that help delinquent borrowers work with loan servicers to secure more affordable mortgages. A recent report by the Urban Institute states that borrowers facing foreclosure are 60% more likely to hold onto their homes if they receive counseling and loan modifications with average monthly payments a mere $454 lower than those who did not see counselors.

12. **Fund Direct Job Creation** by offering financial support to cities, counties, states, universities, community colleges, and non-profit community based organizations to hire the personnel necessary to provide critical services in communities throughout the nation. Eligibility for support will be based on unemployment rates with a particular focus on the long-term unemployed. At least twice in American history, the government has responded to high rates of unemployment with investment in direct job creation – the 1935 Works Progress Administration, when nearly one-quarter of the labor force was without work, and the Emergency Jobs and Unemployment Assistance Act of 1974, establishing Title IV of CETA as a temporary countercyclical employment program when unemployment was rapidly approaching the

9% level. We are renewing our call for an investment of $150 billion to create 3 million jobs, a number that represents only half of the current unemployed. New investment should feature not only traditional means of direct government funding, but also newer creative measuring design to promote and spur non-profit, university, and community college hiring initiatives, alleviating the strain on federal and local budgets, while stimulating the economy, bolstering local budget revenues and adding to the public good.

Acknowledgements: Special thanks to our Chairman, John Hofmeister, as well as Chanelle Hardy, Valerie Rawlston Wilson, Madura Wijewardena, Garrick Davis, Cy Richardson, Donald Bowen, James Reed, Terrence Clark, Bernard Anderson, William M. Rogers, Lucy Rubens Urban League Affiliate leaders across the country for their input, research, advice and intellectual contributions toward the preparation of the plan.

National Urban League
Entrepreneurship Center Program

Introduction

Founded in 1910, the National Urban League (NUL) is the nation's oldest and largest community-based movement devoted to empowering African Americans to enter the economic and social mainstream. The Urban League is a nonprofit, nonpartisan community—based movement headquartered in New York City that reaches more than 60 million people nationwide through direct services, programs, advocacy and research with the services of professionally staffed affiliates in 35 states.

The mission of the National Urban League is to enable African American to secure economic self—reliance, parity and power and civil rights. Utilizing policies and tailored services like the Entrepreneurship Center Program, we carry out our mission by closing the equality gaps in education, the economy, health and quality of life, civic engagement, and civil rights.

The goal of the Entrepreneurship Center Program is to enable minority entrepreneurs to take advantage of new business opportunities and qualify for financing that will lead to high-level business growth through the provision of proper management skills. Entrepreneurs who qualify for the program receive individualized management assistance and group training services designed to increase their business acumen and ability to operate their businesses on a profitable basis, increase their market share and otter living wage employment opportunities to residents in their market area. The Entrepreneurship Center program is in its 6th year of operation. Currently there are nine centers, which operate in Atlanta, GA, Chicago, IL, Cincinnati, OH, Cleveland, OH, Jacksonville, FL, Kansas City, MO, Los Angeles, CA, New Orleans, LA and Philadelphia, PA.

The program has showed steady growth since 2006. In 2006, the centers provided 1,272 hours of management counseling and 1,777 hours of business skills training to 1,164 clients. In 2007, the centers provided 4,102 hours of management counseling and 4,272 hours of business skills training to 2,182 clients. In 2008, the centers provided 9,670 hours of management counseling and 9,424 hours of business skills training to 3,913 clients. In 2009, the centers have provided 8,010.77 hours of management counseling and 7,113.50 hours of business skills training to 4,930 clients. Given the current state of the US economy, more people are looking at entrepreneurship as a way to provide self employment opportunities and be able to grow their businesses to a scale which would allow them to employ people in their community. In 2010, the centers provided 10,911 hours of counseling and 11,242 hours of training services to 5,938 entrepreneurs. These services assisted entrepreneurs in receiving $20.19 million in new bonding, new contracts and financing during the year.

The Entrepreneurship Center Program combines direct entrepreneurial skills development assistance from business mentors with targeted referrals to insure that assistance received by entrepreneurs is specific to their skill level and needs Components of the program are:

Management Skill Evaluation Each program participant is evaluated to determine the type of assistance necessary and the source of that assistance.

Relationship Building Each center develops relationships with outside resources that provide management and technical assistance in the areas such as idea development, operations management, business plan development, marketing, procurement and financing.

Strategic Group Deployment- The grouping of outside resource providers by skill level of clients to ensure that the client is receiving the necessary assistance from the proper resource.

Business Management Training- Clients receive group training sessions on business management topics that can advance their entrepreneurial skill level along with information on new business opportunities and financing options that can be accessed. Training sessions are held monthly through direct sponsorship or co sponsorships with outside resource providers.

Marc H. Morial

Entrepreneur. Lawyer. Professor. Legislator. Mayor. President, U.S. Conference of Mayors. CEO of the National Urban League, the nation's largest civil rights organization.

In a distinguished professional career that has spanned 25 years, Marc Morial has performed all of these roles with excellence, and is one of the most accomplished servant-leaders in the nation.

As an Entrepreneur, Morial started several successful small businesses -- an apparel wholesale company, a special events company, and a janitorial company, his first venture at age 15 with two childhood friends.

As a Lawyer, Morial won the Louisiana State Bar Association's Pro Bono Publico Award for his legal service to the poor and disadvantaged. He was also one of the youngest lawyers, at age 26, to argue and win a major case before the Louisiana Supreme Court.

As a Professor, Morial served on the adjunct faculty of Xavier University in Louisiana, where he taught Constitutional Law, and Business Law.

As a Louisiana State Senator, Morial was named Legislative Rookie of the Year, Education Senator of the Year, and Environmental Senator of the Year, while authoring laws on a wide range of important subjects.

As Mayor of New Orleans, Morial was a popular chief executive with a broad multi-racial coalition who led New Orleans' 1990's renaissance, and left office with a 70% approval rating.

With vigor and creativity he passionately attacked his city's vast urban problems. Violent crimes and murders dropped by 60%, the unemployment rate was cut in half, and New Orleans' poverty rate fell according to the 2000 Census.

The city's economy experienced its most dramatic growth in over 20 years as the Convention Center was expanded, thousands of new hotel rooms were built, the Downtown Casino and Sports Arena opened and New Orleans hosted Super Bowls and Music Festivals, as well as International and Hemispheric Summits. The NBA also returned to New Orleans as he led the effort to relocate the Hornets from Charlotte.

During his tenure, New Orleans won the All-American City Award in 1996 for the first time in 50 years, as well as the prestigious City Livability Award, and finished first in the National Night Out Against Crime Competition on two occasions.

He produced eight balanced budgets, and led the passage of a new City Charter which authorized the creation of a City Revenue Estimating Conference, an Ethics Board and Inspector General.

Elected by his peers as President of the bi-partisan U.S. Conference of Mayors (USCM), he served during the 9/11 Crisis and championed the creation of the Department of Homeland Security, and the Federalization of airport security screeners.

The USCM achieved unparalleled visibility and prominence under his leadership.

As President of the National Urban League since 2003 he has been the primary catalyst for an era of change -- a transformation for the 100 year old civil rights organization. His energetic and skilled leadership has expanded the League's work around an Empowerment agenda, which is redefining civil rights in the 21st century with a renewed emphasis on closing the economic gaps between Whites and Blacks as well as rich and poor Americans.

Under his stewardship the League has had record fundraising success towards a 250MM, five year fundraising goal and he has secured the BBB nonprofit certification, which has established the NUL as a leading national nonprofit.

His creativity has led to initiatives such as the Urban Youth Empowerment Program to assist young adults in securing sustainable jobs, and Entrepreneurship Centers in 5 cities to help the growth of small businesses. Also, Morial created the National Urban League Empowerment Fund, which has pumped almost $200 million into urban impact businesses including minority business through both debt and equity investments.

A graduate of the prestigious University of Pennsylvania with a degree in Economics and African American Studies, he also holds a law degree from the Georgetown University Law Center in Washington, D.C., as well as honorary degrees from Xavier University, Wilberforce University, and the University of South Carolina Upstate.

He serves as an Executive Committee member of the Leadership Conference on Civil Rights, the Black Leadership Forum, and Leadership 18, and is a Board Member of the Muhammad Ali Center, and the New Jersey Performing Arts Center.

He has been recognized as one of the 100 most influential Black Americans by Ebony Magazine, as well as one of the Top 50 Nonprofit Executives by the Nonprofit Times.

Morial, a history, arts, music and sports enthusiast, has an adult daughter, and is married to broadcast journalist Michelle Miller. Together they have two young children.

Source URL: http://www.nul.org/who-we-are/executive-leadership/executive-staff/mark-morial

Chair LANDRIEU. Thank you so much for that excellent testimony.

Ms. Allen.

STATEMENT OF SUSAN ALLEN, PRESIDENT AND CHIEF EXECUTIVE OFFICER, U.S. PAN ASIAN AMERICAN CHAMBER OF COMMERCE

Ms. ALLEN. Thank you, Madam Chair Landrieu, Ranking Member Snowe, for the opportunity to testify before you today.

Chair LANDRIEU. Turn the microphone on.

Ms. ALLEN. Thank you, Marc. I need a man in my life.

[Laughter.]

Thank you, Chair Landrieu and Ranking Member Snowe, for inviting me here to speak to you today. I would like to answer your first question to Dr. Fairlie. For the Asian American part, we are about 15.1 million of the population and Asian American-owned businesses, according to the last Census figure, that was in 2007, was 1.3 million around the country.

I am Susan Au Allen, National President and CEO of the U.S. Pan Asian American Chamber of Commerce Foundation. Formed in 1984, we are the only national organization that represents all Asian Americans in various industries, very broad industries. We open doors to business opportunities for small and medium-sized enterprises, working with the government and corporations.

For the last 25 years, we have established a very strong record of helping our constituents to plan, develop, promote the businesses, and business owners, Federal and State agencies, corporations, the media, academic and research institutions come to us for our ability to bring people together from across the country, across ethnic lines, and because of the quality of our business development programs. We work in key market areas across the country and reach over 15,000 SMEs, small and medium enterprises, through our six regional chapters.

I speak today to the salient points that our 8(a) members experience, and all of my comments are based upon all the things they have been telling me throughout the years and especially the last two days.

First, access to capital. The financial crisis has led to the inability and unwillingness of many financial institutions to extend credit. This is a catch-22 situation. To grow a business, you need money—capital to expand, to hire staff, or pay for marketing, R&D, and to pay your staff and keep the good ones around, especially, and your wage. While some companies find small business loans attractive, many banks will not lend because of perceived risks. Unlike manufacturing companies that have collateral for a loan, small companies in the service area do not, so securing a loan is a very difficult proposition for them.

Although the SBA guarantees 90 percent of the loan, a large portion of it must be guaranteed through collateral. The current trend is that banks want to avoid exposure. When a business defaults, the government may take that bank out of the preferred lenders list. They do not want that. They also look at business performance through a much stricter asset-liability model, that is, high profit, high assets versus liability, net worth versus debt.

Controlling contract bundling. The Small Business Jobs Act contains language from S. 2989, called the Small Business Contract Revitalization Act of 2010, introduced by Senator Landrieu, you, and Senator Snowe, that addressed the contract bundling issue. However—however—we need strong oversight to ensure accountability and give teeth to this regulation so your intention will be truly carried out, Senator.

In addition, the mindset of some of the Federal key contract evaluators is an issue. In their mind, they think, if I select a prominent company, like IBM, I cannot be blamed if the project fails. But if I pick some unknown company and the project fails, I could lose my job. These evaluators will select prominent or what we call dominant companies over successful mid-sized companies. That is a very harsh reality that our members face.

Business development—the SBA now has 8,000 8(a) firms in its portfolio and they provide good basic business services to the start-ups. However, we need to provide a higher level of service that links mid-size companies to potential opportunities and help to transition soon-to-graduate 8(a) firms into the open market where they could not benefit from the set-aside programs.

To give effective business development assistance, SBA's Business Development Specialists should have a manageable number of companies to help them individually over the nine-year life of the 8(a) status. In the Washington, D.C. office, there are supposedly 1,800 8(a) firms assigned to eight or nine specialists. They also have to monitor compliance by the 8(a) firms. They multi-task. And today, in these days, compliance is priority at the expense of business services. So, therefore, special business services fall short.

If the SBA focuses on compliance, which is required, which we ask for, and leverage community resources, they could work with organizations like us, the U.S. Pan Asian American Chamber of Commerce, on business development. We provide business development services to the Asian American and other small business community nationwide. We are on the ground every day——

Chair LANDRIEU. Thirty seconds more.

Ms. ALLEN [continuing]. Every day, reaching out to small businesses. We have built a platform conducive to teaming between small and mid-sized companies.

Finally, past performance is a difficult task for those who have never gone into Federal contracting but have equally valid commercial experiences. This is another roadblock for small businesses who would otherwise be performing very well and create jobs and benefit the community.

Finally, Senator, we know that small businesses also have our own role to play. Many got into the 8(a) program and wrongly think that they are automatically entitled to a contract. That is wrong. We have been talking to our members and other members in the small business community that they need to do their own due diligence, they need to do their homework, they need to provide good services. They cannot cross the law. Then they will succeed.

Thank you for the opportunity to testify before you. I have submitted a detailed statement. I hope that it will be included in the record.

[The prepared statement of Ms. Allen follows:]

TESTIMONY

Hearing entitled: *Closing the Gap: Exploring Minority Access to Capital and Contracting Opportunities*

SUSAN AU ALLEN

National President & CEO
US Pan Asian American Chamber of Commerce
Education Foundation (USPAACC)

Testimony presented before the
U.S. Senate Committee
on Small Business and Entrepreneurship

March 3, 2011

Thank you Madame Chair Landrieu, Ranking Member Snowe, and the Committee members for the opportunity to testify today.

I am Susan Au Allen, National President & CEO of the US Pan Asian American Chamber of Commerce Education Foundation (USPAACC). Founded as a 501 (c) (3) nonprofit organization in 1984 in the nation's capital, we have been serving and will continue to serve as the gateway to large corporate and government contracts, top-caliber Asian American and small/minority suppliers, key information about Asian American and small/minority businesses, and contract opportunities in the dynamic Asia-Pacific market.

As the only national, nonprofit, non-partisan organization representing all Asian American and Asian American-related groups in a wide array of disciplines, USPAACC promotes and propels economic growth by opening doors to business and professional opportunities for small and medium enterprises (SMEs), Asian American-owned businesses and their partners in government at the federal, state, and local levels, corporate America, and the small and minority communities.

Our main goal is to work with each of our constituents to achieve successful contracting relationships and business growth in the mainstream marketplace. We also leverage the combined economic strength of Asian Americans and their partners to propel growth.

In 25 years, USPAACC has established a strong and proven record of helping our constituents plan, research, develop, implement, and promote their businesses. A broad spectrum of people — from business owners to federal and state agencies, corporations, the media, academic and research institutions — call upon us because of our nationwide outreach ability and expertise in bringing people together, and the quality and substance of our business development programs.

We work in key markets across the country, reaching over 15,000 Asian American-owned and other SMEs through our Regional Chapters in the West Coast, Southeast, Southwest, Midwest, Northeast, and Washington, DC-Maryland-Virginia in the National Capital Area.

My testimony today is based upon my knowledge on the salient issues that our 8(a) business members face today:

1) *Access to Capital*

While we see signs of an economic rebound, small business owners have yet to see recovery, especially one that translates into actual sales.

The turmoil created by the recent financial crisis in the credit market has led to the inability or unwillingness of many financial institutions to extend credit. Those who bear the brunt of this debacle are the small businesses who could not move forward with opportunities that could generate jobs that would also grow the economy.

This has become a "Catch-22." To grow a business, you need money – capital to expand, to take it to the next level, to hire staff, or invest in marketing and R&D. In some cases, higher sales can cost more cash and so more cash is needed to run the business. For others, when sales slow dramatically because of the recession, they need cash to make up the shortfall, maintain payroll and wait.

While some 8(a) companies may find small business loans attractive, many banks continue to be reluctant to lend because there is still a lot of risk. Unlike the companies in the manufacturing sector that have collaterals for a loan, small businesses in the service sector do not. So securing a loan is a difficult proposition.

Even though the U.S. Small Business Administrarion (SBA) guarantees 90% of the loan, a major portion of it must be guaranteed through collateral. There appears to be a trend – banks want to avoid potential exposure when a business would default, then the government may take the bank out of the preferred lenders list. In addition, they now look at business performance through a more stringent financial model of ratios and quotas (e.g., profit, assets versus liabilities, net worth versus debt, etc.) because they view small businesses as "risks."

2) *Contract Bundling*

We are pleased that the Small Business Jobs Act, which contains language from S.2989 (The Small Business Contracting Revitalization Act of 2010), a bill introduced by Senator Landrieu and Senator Snowe, has addressed the issue of contract bundling. However, there must be strong Congressional oversight to ensure accountability and give teeth to this regulation in order to carry out the intent of the law.

Corollary to contract bundling is the mindset of some Federal key contract evaluators, "If I select a prominent company like IBM, I can't be blamed if the project fails; but if I pick some unknown company and the project fails, I could lose my job."

So these Federal contract evaluators will select the large and recognizable companies with a well-known reputation over mid-sized businesses. This mentality is so prevalent that even if the procuring entity knows that the large company they intend to select is failing in certain areas within their organization, they would still select them over the unknown companies. This is the very harsh reality that mid-sized federal contractors have to contend with.

This mindset stops federal contractors who have grown from small to mid-sized companies, can and are ready to compete with large businesses, if given the chance. However, they are not allowed to enter the ring.

The remedy is to give incentives to the agencies, their contracting team, or to the Primes for giving opportunities to new businesses. This will also reduce or avoid complacency because of doing business with the same entities without having to meet new challengers.

Moreover, changing this way of doing business with their suppliers will mean more scrutiny and accountability, and transparency on all levels throughout the contracting process. It also means re-training staff. This way, some of the hurdles small and medium-sized companies are going through may be removed and replaced with more access and opportunities.

3) ***Business Development***

The fact that the SBA has increased the 8(a) roster from 3,000 to 8,000 in the last 10 to 15 years is commendable. While the SBA has been providing basic services to start-ups, we believe there should be a program to provide the next-level of training that actually links mid-tier companies to potential opportunities, and helps to transition soon-to-graduate 8(a) companies into the open marketplace when they are no longer eligible for set-asides.

To provide good and effective business development assistance, an SBA business development specialist should have a reasonable number of companies to help and pay individual attention to the company over the 9-year life of its 8(a) status. In one SBA office in the West Coast, a specialist manages about 100 companies. However, here in the East Coast, at the Washington, DC district office, there are reportedly 1,800 8(a) firms assigned to 8 to 9 specialists. And all these specialists perform business development and compliance duties. Oftentimes, compliance has become a priority at the expense of helping small companies grow and succeed, the mission for which the 8(a) program was created.

Because the funding issue will not go away, we strongly recommend that the SBA focuses on compliance and leverage community resources and work with organizations like us — USPAACC — on business development.

For over 25 years, USPAACC has been providing business development services to the Asian American and other small businesses nationwide. We have built an effective platform conducive to teaming arrangements between small and mid-tier companies. We are on the ground everyday reaching out to small businesses, making new connections, educating a wider public on available business opportunities.

4) ***Standardized RFP***

The quality of the Request for Proposals should be addressed. Oftentimes, they are not clear, contain inconsistencies, had to be pulled back and reissued. When this happens, it wastes time and resources — the RFP-issuing agency, the business preparing the bid, and organizations associated with this process. Much more care should be given to the preparation of an RFP with clearer, concise, and standard language.

5) ***Past Performance***

The past performance is crucial to a small business in the bidding process. However, more often than not, a smaller firm is less likely to have previously worked on a project which is virtually identical to the types of services being sought in the RFP, and to have also done it for the federal government. If experience on the commercial or privare side were to be equally valued and taken into consideration, then it would help level the playing field for small businesses to enter the federal marketplace.

6) ***Insourcing***

Insourcing has become more pervasive in recent years and is likely to continue. Is this the quick-fix answer to cost control? Depending on the industry, and except for legal services and scientists, the preponderance of evidence says no.

Meanwhile, insourcing limits new opporrunities for small businesses and takes existing contracts away from them. There is also a lack of transparency in the government's decision process for deciding which jobs will be insourced. Moreover, many small federal contractors find that their employees are hired away by government agencies when they move jobs in-house. This is a lose-lose situation for small businesses.

7) ***Mentor-Protégé***

There is one SBA program that we feel, when expanded, can help both small and mid-sized companies. The 8(a) Mentor-Protégé Program (MPP) allows 8(a) Protégé companies to form Joint Ventures with their Mentors. It enables the JV to bid for contracts as an 8(a) small business, with the qualifications and the past performance of both the Mentor and the Protégé companies.

It gives the mentor company a chance to be a small business, to teach the other small company how to create a great proposal to win jobs, grow and to become a fully independent company.

The issue now is that this MPP is limited to small businesses in the 8(a) program and the Mentors are the large, well-known companies who continue to benefit from this program, i.e., to be a small business. We suggest the immediate implementation of the parity language on the Jobs Bill (S. 1489) that Senator Snowe introduced. It provides for an MPP for every small business designation (i.e., have one for SDVOSB, 8(m), HubZone, SDB, etc.) and will create more winning partnerships. To enlarge the pool of Mentors, we could have a program that puts mid-sized companies and small companies together to foster successful teaming relationship. It will stimulate the right kinds of competition among like-sized companies.

Graduated 8(a) firms would be a good source of Mentors. This would allow the new 8(a) company to learn from the experiences of the former certified company.

In closing, the responsibility of resolving these issues also lies on the small business community to do its part. Many small businesses assume that by having 8(a) designation, they are immediately entitled to business opportunities. This expectation is incorrect. Small businesses must realize that being an 8(a) company only gets them a ticket through the door into the room where they can compete with their peers. It is important for small businesses to be proactive, do their homework, pursue due diligence, deliver good products or services, and after-sales service. Then, they could thrive and compete effectively in the marketplace.

Thank you for the opportunity to appear before the Committee. I would be happy to answer your questions.

Susan Au Allen, Esq.
National President & CEO
US Pan Asian American Chamber of Commerce Education Foundation
National Headquarters - Washington, DC 20036

SUSAN AU ALLEN founded the US Pan Asian American Chamber of Commerce Education Foundation (USPAACC) with a group of civic and business leaders in Washington, DC in 1984 to bring the Pan Asian American business and professional people together as one unified voice in business, commerce and trade.

She became its National President and CEO in 2001, after a 17-year career in law. A long time and effective advocate for Asian American issues on Capitol Hill, in the White House, and the media, Susan achieved a new level of influence when President George H.W. Bush appointed her to the Council of the Administrative Conference of the United States from 1991 to 1996. She is the recipient of numerous awards and distinctions for her efforts on issues such as ethnic and minority inclusion, supplier diversity, international trade, and business growth of Asian Americans in the mainstream.

Susan came to the United States from Hong Kong on an invitation from the White House in recognition of her work on behalf of people with disabilities. She earned a Juris Doctor from the Antioch School of Law and an LL.M. in International Law from Georgetown University. During her 17 years with Paul Shearman Allen & Associates of Washington, DC and Hong Kong, she became nationally recognized for her work on immigration, international trade and investment.

Susan is a frequent guest at White House and Congressional events that are focused on America's small, minority and women business communities. Through her participation in these forums, she plays an important role in shaping the national agenda on the economy.

Susan draws an analogy between USPAACC and the acorn that has grown into an Oak tree since its founding 25 years ago. USPAACC's strong roots and wide branches now extend to thousands of Asian American entrepreneurs and professionals across the country. She is most proud of their ability to open doors to contract, educational and professional opportunities for Asian Americans.

Susan is a member of Pfizer's Small Business Advisory Council; Diversity Council of the American Hotel & Lodging Association, International Franchise Association and American Red Cross; National Association of Women Business Owners National Advisory Council; and the Kennedy Center Community Board, among others. She also has served on the Small Business Advisory Committee of the U.S. Department of Energy and U .S. General Services Administration; U.S. Small Business Administration National Women's Business Council; Diversity Council of TimeWarner, Wyndham International, and Commissioner of the Minority Business Opportunity Commission of the District of Columbia, among others.

Among Susan's awards are the Urban Wheels Lifetime Achievement Award (2010) ,
Diversity Business.com's Top Diversity Advocates (2007), Minority Business Hall of Fame (2005), Nation al Association of Minority Automobile Dealers' Diversity Advocacy Award (2006), NASA Special Recognition Award for Extraordinary Efforts in Promoting Small Business Programs Nationally and Internationally (200 2), Business Person of the Year Award from the League of Korean Americans-USA (2002), AT&T Spectrum Award for Advocacy for Minority Business Opportunity (2001)a,nd Skirt in Power Award from the District of Columbia Chamber of Commerce (1992), among others.

Susan speaks and writes Chinese fluently. Married with two sons, she lives in McLean, Virginia.

Susan Au Allen, Esq.

National President & CEO
USPAACC National Headquarters - Washington, DC

SUSAN AU ALLEN founded the US Pan Asian American Chamber of Commerce Education Foundation (USPAACC) with a group of civic and business leaders in Washington, DC in 1984. She became its National President and CEO in 2001, after a 17-year career in law. A longtime and effective advocate for Asian American issues on Capitol Hill, in the White House, and the media, Susan achieved a new level of influence when President George H.W. Bush appointed her to the Council of the Administrative Conference of the United States from 1991 to 1996. She is the recipient of numerous awards and distinctions for her efforts on issues such as ethnic and minority inclusion, supplier diversity, international trade, and business growth of Asian Americans in the mainstream.

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In 1984, Mrs. Allen founded the US Pan Asian American Chamber of Education Foundation (USPAACC) with a group of civic and business leaders in Washington, DC and California to bring the Pan Asian American business and professional people together as one unified voice in business, commerce and trade. In 2001, while taking a leave of absence from her law practice, after winning two cases for her clients, she volunteered as its National President & CEO. She never returned to law and has been serving as its full time National President & CEO ever since.

Long an effective advocate for Asian American business and professional issues on Capitol Hill and in the White House, Mrs. Allen achieved a new level of influence when President George H.W. Bush appointed her to the Council of the Administrative Conference of the United States. She served in this capacity from 1991 to 1996.

In January 2010, Mrs. Allen received the *Urban Wheels Lifetime Achievement Award* in Detroit. In 2007, DiversityBusiness.com named her to its roster of *Top Diversity Advocates*, along with former President Bill Clinton, former President Jimmy Carter and media mogul Oprah Winfrey.

In 2005, in ceremonies at the Harvard Club in New York, Mrs. Allen was installed into the *Minority Business Hall of Fame by Minority Business News USA*.

In 1999, A-Magazine named her one of *25 Most Influential Asians in America*.

Mrs. Allen is a frequent guest at White House and Congressional events that are focused on America's small, minority and women business communities. Through her participation in these forums, she plays an important role in shaping the national agenda on the economy.

Mrs. Allen draws an analogy between USPAACC Education Foundation and the acorn that has grown into an Oak tree since its founding 25 years ago. USPAACC Education Foundation's strong roots and wide branches now extend to thousands of Asian American entrepreneurs and professionals across the country. She is most proud of their ability to open doors to contract, educational and professional opportunities for Asian Americans, the fastest-growing group with the highest business growth in the United States. Once an immigrant herself, she knows the obstacles that must be overcome to achieve the American Dream and she has dedicated her life to help others in pursuit of their Dream - develop, grow and build a successful business.

Mrs. Allen is a member of Pfizer's Small Business Advisory Council; Diversity Council of the American Hotel & Lodging Association, International Franchise Association and American Red Cross; National Association of Women Business Owners National Advisory Council; and the Kennedy Center Community Board.

She also has served on the Small Business Advisory Committee of the U.S. Department of Energy and U.S. General Services Administration; U.S. Small Business Administration National Women's Business Council; NASA's Minority Business Resource Advisory Committee; Women's Small Business Summits National Adisory Board; Washington Board of Trade's Board of Trustees for The Washington Initiative; Diversity Council of TimeWarner, Wyndham International, Premier Automotive Group (Aston Martin, Jaguar, Volvo and Landrover); U.S. Marine Transportation System National Advisory Council; Board of Directors of the Virginia Small Business Finance Authority; Diversity Boards of AMTRAK and the U.S. Marine Corps; and Commissioner of the Minority Business Opportunity Commission of the District of Columbia.

She was a member of the President's Council on the 21st Century Workforce Committee on the Future of the Workplace, and the Board of Trustees of Excelsior College in New York.

As national president and one of the founders of this 25-year old pan Asian American business organization, Mrs. Allen is frequently approached by the media to comment on Asian American businesses, US-Asia business, commerce and trade, and Asian American woman executives, entrepreneurs, and professionals.

She has contributed op-ed articles to *USA Today*, *The Washington Times*, *The Baltimore Sun*, *Asian Week*, and *Asian Fortune*. She has also appeared as a commentator on C-Span, CNN, CNBC, ABC, Fox News, *The News Hour*, *To the Contrary*, *This is America*, and *The Editor*.

Among Mrs. Allen's awards are the *Urban Wheels Lifetime Achievement Award* (2010), *DiversityBusiness.com's Top Diversity Advocates* (2007), *Minority Business Hall of Fame* (2005), National Association of Minority Automobile Dealers' Diversity *Advocacy Award* (2006), NASA *Special Recognition Award for Extraordinary Efforts in Promoting Small Business Programs Nationally and Internationally* (2002), *Business Person of the Year Award* from the League of Korean Americans-USA (2002), AT&T *Spectrum Award for Advocacy for Minority Business Opportunity* (2001), and*Skirt in Power Award* from the District of Columbia Chamber of Commerce (1992).

Mrs. Allen speaks and writes Chinese fluently. Married with two sons, she lives in McLean, Virginia.

Chair LANDRIEU. Thank you very much, Ms. Allen, for that very powerful testimony, and this committee looks forward to working with you more closely in the future. We thank you so much.

Ms. ALLEN. I do, too.

Chair LANDRIEU. Mr. Mitchell.

STATEMENT OF B. DOYLE MITCHELL, CHAIRMAN, NATIONAL BANKERS ASSOCIATION

Mr. MITCHELL. Good morning, Madam Chair and members of the committee. I am honored to testify before you this morning on closing the gap on minority access to capital. I am B. Doyle Mitchell. I am President and CEO of Industrial Bank, a minority-owned commercial community bank operating in the nation's capital and in Prince George's County, Maryland. The issues that I mention today are vital to each of the States of the members of this committee, that they represent, and they are vital to the nation as a whole. Without decisive action and cohesive leadership from this committee, the Senate, House, administration focusing in a cost effective manner in the right place, the economy will continue to stagnate.

Industrial Bank was formed in 1934 by my grandfather to fill the gap in lending, which at the time was primarily to African Americans. I am third generation, and we have been successful in achieving our part of bridging that gap, evident by the assets of over $380 million, a loan portfolio of $210 million to faith-based organizations, home mortgages, small real estate investors, and small businesses. The bank is well capitalized and we have been profitable throughout the recession in 2008, 2009, 2010—not by much, though.

Ladies and gentlemen, I also represent another very important organization. In January, I assumed the Chairmanship of the National Bankers Association, or the other NBA, as we call it. This entity, as you heard, is over 80 years old and consists of nearly 50 minority-owned, managed, or focused insured financial institutions from all over the country, places like Washington, D.C., Maryland, Pennsylvania, North and South Carolina, Illinois, Louisiana, and the list goes on.

Our association represents African American banks, Asian banks, Hispanic banks, Native American banks, and one American Indian bank, and at one point there was even a woman-owned financial institution that was part of our membership until they were acquired by another institution.

Our members and all minority banks focus their lending efforts in mostly minority communities where evidence of joblessness is way more pronounced than in other communities, even in good times. So just imagine what they are going through now. The unemployment rate in many of these communities is at least twice the national average. That is everybody's problem. The effect of unemployment in these neighborhoods impacts us all via crime, health care concerns, and benefit programs that provide the necessary safety net for millions of Americans. People would actually rather work than draw on government-provided programs.

State and local governments are paying dearly and will continue to pay if the economy stalls. In Prince George's County, the fore-

closure rate has hit African American families disproportionately to other ethnic groups.

We know that 80 percent of all jobs in this country are created by small businesses and the only pathway back to an economy that allows private industry to work is to employ them from small businesses.

As the testimony of Ms. Johns reflects, the SBA provides a very important vehicle for small businesses through the banking system. Their programs can and have filled the gap that exists in funding small businesses. Many of these companies have already tapped the equity in their homes, their credit cards, and their savings to pursue their dream of entrepreneurship. The SBA, through its programs, leverages the funding tenfold. The returns to the economy are tremendous. They should be fully funded. The 90 percent guarantee program should be extended or even reinstituted, if necessary, for another two years, if not made permanent. Also, the elimination of the fees or at least the reduction of the fees from the traditionally high levels should be instituted.

Last year, the Industrial Bank provided an SBA loan to an entrepreneur that opened an International House of Pancakes, IHOP store. That store created 120 full-time jobs. It is running around the clock, 24 hours a day. They even deliver nearby. And many of these jobs were young people looking for employment, but many were also individuals that had been laid off and been looking for a job for a long time. Some had significantly higher-paying jobs, but accepted employment there just to make it through these tough times, and the store is doing very, very well.

More money, not less, should be invested in the SBA and its loan programs. It is a good government solution that provides returns to the economy and taxpayers.

The Department of Transportation has a short-term lending program, basically for a line of credit, for companies, DBEs, that have Department of Transportation contracts. This program should be applauded, as well, and financially supported. The committee should consider encouraging other agencies that do not have such a lending program——

Chair LANDRIEU. Thirty seconds, please.

Mr. MITCHELL [continuing]. To develop similar types of programs.

Finally, the Small Business Lending Fund that is currently being administered by the Treasury Department is an excellent example of how government can incent community banks to lend more by providing them short-term capital. If I had one suggestion on this program, it would be this. The rate resets to nine percent in four-and-a-half years, which is a very high rate and due in a very short period of time. I understand the reason for resetting to the higher rate to encourage quick repayment to the Treasury. Most small businesses have loan repayment terms of five to ten years, the average being about seven. The Small Business Lending Fund would be more effective and attractive if the interest rate reset period to nine percent were amended to seven percent, and we just ask that the committee consider making that minor adjustment in such an important program.

Thank you.

[The biography of Mr. Mitchell follows:]

B. Doyle Mitchell, Jr., President and CEO

B. Doyle Mitchell, Jr. is President and CEO of Industrial Bank, the largest minority-owned commercial bank in the Washington Metropolitan area, and the ninth largest African-American owned financial institution in the country (Black Enterprise Magazine, June 2010). A native Washingtonian, Mr. Mitchell was born and raised in the Washington banking community that his grandfather, the Bank's founder, and father helped to create. After receiving his Bachelors degree in Economics from Rutgers University in 1984, he began a full-time career with Industrial Bank. He was elected to the Board of Directors in 1990, and succeeded his father as President in 1993. Under his leadership, the Bank formed the IBW Financial Corporation (Holding Company) in 1994 to facilitate expansion into Prince George's County, Maryland. As one of the first banks to utilize the new interstate banking laws, he was recognized by the Secretary of Treasury, Lloyd Bentsen, as a pioneer in the banking industry at the signing of the Interstate Banking Bill enacted in September 1994.

Mr. Mitchell serves on the Board of Directors of the Federal City Council, Greater Prince George's Business Roundtable, Archbishop Carroll High School, the National Coalition of Minority Businesses, Sewell Music Conservatory, the Council for Court Excellence, the Minbanc Foundation and he is Chair of the D.C. Chamber of Commerce Foundation. Mr. Mitchell was also the Chairman of the D.C. Chamber of Commerce in 2001. He is currently the Chair of the National Bankers Association.

Mr. Mitchell is a former Board member of the Greater Washington Board of Trade, the Washington Performing Arts Society, Leadership Greater Washington, and the U Street Theater Foundation (Lincoln Theater). In the past he has also served on the Board of the American Institute of Banking, the Luke C. Moore Aeademy, the MAAT Center for Human Development, the D.C. Water and Sewer Authority, the Maryland Economic Development Assistance Authority, and the Bowie State Board of Visitors.

The three generations of Mitchell bankers have all had vision for their community even when the rules of the road were different. B. Doyle Mitchell Jr., and Industrial Bank are dedicated to servicing the Greater Washington area. Industrial Bank provides a full range of quality banking, real estate, and financial services, including internet banking and surcharge free access to over 25,000 ATM's worldwide.

Chair LANDRIEU. Thank you, Mr. Mitchell, and we appreciate that and that is very timely as we try to implement the concepts of that program. Some adjustments may need to be made.

Ms. Montoya.

STATEMENT OF MARTHA MONTOYA, PROCUREMENT CHAIR AND BOARD MEMBER, U.S. HISPANIC CHAMBER OF COMMERCE

Ms. MONTOYA. Madam Chair, it is an honor to testify before the Senate Committee on Small Business and Entrepreneurship. My name is Martha Montoya. I am the President of several enterprises, Los Kitos Produce, in the business of growing and getting fruit from the field to the supermarkets and restaurants and commissaries. In fact, we have farms in North Carolina, converting them from tobacco to strawberry growers.

Currently, 95 percent of our Hispanic businesses do not fit the lending profile of banks. We are too small for private equity funds, receive minimal attention from venture capital firms, yet we are the fastest-growing segment of the entire country. Even the landscape and alarming lack of capital available for Hispanics and entrepreneurs, we are coming up with capital solutions for you on behalf of the United States Hispanic Chamber of Commerce.

With regards to the public sector, the biggest solution we see is the CRA, the Community Reinvestment Act, funding into our communities. Let me give you an example. Under the CRA program, Rabobank retained us to bring financial management training to Hispanic and minority growers at the local level throughout California. They needed this training because they grow things well, but they are not good in financial management and do not manage their banking relationships well. This is a key reason why they are unable to get banking financing.

I have very capable growers who are struggling to even get the crops into the ground without adequate financing. In fact, I have one grower for Washington State present today. I have seen good growers unable to get their products to markets because they could not afford to pay the packing house fees as a result of their not being able to get a line of credit from the bank.

This story of lack of access of capital is repeated everywhere across the U.S. for Hispanic growers. It is a crying shame, because there are over 80,000 Hispanic growers in the United States and they are doubling per year. With proper access to capital and bank financing, Hispanic growers can make a significant contribution to the food supply of the country. Needless to say, farmers were the original entrepreneurs of this country.

It is clear that CRA funding could serve as a vehicle for the following reasons and actions. One, equity funds for local banks, investment funds, and others with more flexibility to deploy funds and with a higher level of patience for returns.

Second, large-scale banks to deploy the CRA funding themselves and work the ground while training the next generation of minority bankers.

Third, request a minimum of 25 percent of CRA funding to go to rural areas. Why? It will motivate and unlock the creativity in our rural areas and growth.

Fourth, match CRA funding with local financial tools from SBA and others. That way, the burden of infrastructure capital will create sustainable jobs for the next two to five years.

In terms of private sector, we need more companies to demonstrate the leadership that we see from Goldman Sachs in the creation of Goldman Sachs 10,000 Businesses Program. Visionary corporate leaders like Lloyd Blankfein and Warren Buffett understand that America's small businesses are the backbone.

I would say, also, the third is the access to contracts and access to capital are a symbiotic relationship. You need both simultaneously in order to give and survive business. However, they seldom arrive at the same time, and because of this, only companies that become completely creative can adapt to the environment. A business is required to demonstrate financial stability and growth in order to become a supplier, yet the bank will not talk to you unless you already have a significant track record.

We need more training through the small business or the financial. I, for example, received through Walmart Corporation a Dartmouth Tuck University program called Building a High-Performance Minority Growth in all the financial tools to grow the business.

I think that more important is the fact after 25 years traveling around the world and seeing how many of our programs go to those countries and are so flexible for the business, yet in this environment, the minorities is less flexible.

I thank you so very much for your time. I trust and hope that my personal community and business experience allow you to glimpse of what I see the terms and solutions that are just at our hand.

[The prepared statement of Ms. Montoya follows:]

Testimony

Small Business Participation in the Federal Procurement Marketplace

Senate Committee on Small Business and Entrepreneurship

Chair Mary L. Landrieu

March 5th, 2011

10:00 a.m.

Russell Senate Office Building

Room 428A

Washington DC

Martha Montoya
Pres/CEO – Los Kitos Produce/El Mundo Communications
Board Member – Chair Procurement and Access to Business Capital - USHCC

Testifying on Behalf of
United States Hispanic Chamber of Commerce

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[Type text]

Madam Chair:

It is an honor to testify before the House Senate Committee on Small Business and Entrepreneurship today on the issues of "Closing the Gap: Exploring Minority Access to Capital and Contracting Opportunities".

My name is Martha Montoya. I'm the President of several enterprises including, A) Los Kitos Produce, in the business of getting fruit from the farm to the store shelf, B) Los Kitos Entertainment a syndicated cartoon strip and content provider, and C) El Mundo Newspaper, the largest and oldest Hispanic newspaper in Washington State. Throughout the years, I have served on the Board of several local, state and national organizations in the capacity of Procurement Chair, Access to Capital Chair, and Regional Chair, while also being active in other posts including the State of California Governor's Conference on Small Business and Entrepreneurship Steering Committee, the Executive Committee of the United States Hispanic Chambers of Commerce and most proudly I am a product of our Hispanic Chambers of commerce.

Currently 95% of Hispanic businesses do not fit the lending profile of banks. We are too small for private equity funds, receive minimal attention from venture capital firms, yet we are the fastest growing segment of the entire country.

The current situation reminds me of the statement made by Charles Darwin, "It is not the strongest of the species that survives, nor the most intelligent that survives, it is the one that is the most adaptable to change."

I am here to give a solution without burdening you all with new requests or more work, but hopefully to shed some light on how I believe we can unlock capital for growing businesses.

Given the landscape and alarming lack of capital available for Hispanic entrepreneurs, I strongly encourage you to ask economic policy agencies and regulators such as the Federal Reserve and the Treasurer to focus their effort on supporting minority small business entrepreneurs through their Community Reinvestment Act obligations so they in turn will request the banks to deploy those funds into the communities, and particularly into rural areas.

Access to contracts and access to capital have a symbiotic relationship. You need both simultaneously in order to survive and grow a business. However they seldom arrive at the same time, and because of this only those companies that become completely creative and adapt in this business environment will make it.

[Type text]

Here is why:

1) A business is required to demonstrate financial stability and growth in order to become a supplier, yet a bank will not talk with you unless you already have a significant track record. This leaves most small businesses in an unfavorable position. To make things worse, minority business owners, in particular Hispanics whom I represent, lack elements needed to stop this "ping-pong" syndrome as I call it. Those elements include Financial higher education across the industries. Please note I did not say Financial literacy which reduces the conversation to simple financial transactions, but a more rigorous understanding of Balance sheets, income statements, and grounded financial projections. In my own case I have been fortunate to be a recipient of a scholarship to Dartmouth's Tuck School of Business program entitled "Building a High-Performing Minority Business" along with 35 otherr small businesses owners. This program had a positive impact on all of us because of its emphasis on financial tools and understanding.

2) Banking and personal relationships are crucial for the growth of a business, yet without the tools for the banker to deploy he/she is obsolete in the communities they serve. As a business owner I was a recipient of funding through a State of California bank guarantee program with a local bank some 12 years ago. Though it was a small credit line of $50,000.- , it was the spark that jumpstarted my company. It was done on the basis of flexibility and taking a calculated risk that allowed the banker to begin establishing the business relationship with our company which has lasted over a decade. By the way, that line of credit built my confidence, boosted my team's energy and made it possible for me to be here today.

3) There is a need for other tools such as funding the funders that provide liquidity to small businesses and do understand us. Contracting is a "scalable" business game and the only tools available are outside of the banking industry such as factoring and a few equity funds. Having funds headed by people of our own communities is crucial as they understand the nuances of the business environment we work within. Hispanics manage less than 0.2% of this funding though we represent the fastest growing segment of the population. Research by Altura Capital, which is a manager of emerging money managers, has shown that the performance of smaller funds is superior than larger peers due to flexibility and commitment to high growth markets.

4) Bankers from our communities need to be deployed yet be encouraged and nurtured to educate themselves on financial and business elements. It was definitely clear during this last period of financial difficulties that we had very limited personnel on the ground to assist our Hispanic business owners. Very few banks have addressed this lack of

[Type text]

qualified personnel to help our businesses and to bring them new clients. For one of my companies, while seeing how capital was closing on Hispanic farm growers here among mainstream banks, we approached a European owned bank with a highly educated Hispanic team that understands the financial tools, (CRA), the business model (Agriculture), and was able to turn fast and deploy funding for not only our growers but many others by plaeing effective programs and mechanisms directly in the community.

So here we go back to my Darwin statement, evolution, evolution and evolution, and also Dr. Einstein's transformation of Energy without burdening the system.

The Biggest solution should be CRA funding into our communities.

a) Community Reinvestment Bank funding could serve as a vehicle for the following reasons and actions:

- Equity funds for local banks, investment funds and others with more flexibility to deploy funds and with a higher level of patience for their returns.
- Large scale banks to deploy the CRA funding themselves and work the ground while training the next generation of bankers.
- Request minimum 25% of the CRA funding to go to rural areas. It will motivate and unlock creativity in our rural areas and growth.
- Match CRA funding with local financial tools from SBA and others to take away the burden of infrastructure capital yet create sustainable jobs for the next 2-5 years.
- Inform, inform and inform through our publications and media outlets. Bill HR2727 known as the "Financial Transparency Restoration Act". Requiring banks and financial institutions to publish a statement of financial condition at the end of each fiscal quarter in a newspaper of general paid circulation published in a city or county within each market area in which the financial institution is located.

b) Training – smaller banks and financial institutions need to implement Workforce training to better serve our communities. However if the proposed H.R. I passes, for the Fiscal Year 2011 Continuing Resolution (CR), it will eliminate all funding, over $3.6 billion, for the Workforce Investment Act (WIA) in Program Year 2011 and a $175 million rescission of Prior Year funds. Beginning in July I of this year, these cuts would zero out all new funding for state and local programs under WIA – programs that have made a substantial positive impact to employers, job seekers, their families and my community. The CR being proposed by House will cut off a valuable lifeline that is providing critical workforce training programs and business support.

[Type text]

To conclude I have traveled the world on my international agricultural role over the past 20 years and I am still puzzled to see more funding and opportunities provided by our government in other countries and their businesses than for our own Hispanic/minority businesses here in the USA. Clearly we are in a country that is far more stable financially and politically, and therefore I believe those funds would be better used here at home.

Thank you very much for your time and I trust and hope that my personal community and business experience will allow you a glimpse of what I see in terms of actions that need to be taken to foster growth in our small businesses.

MARTHA MONTOYA

Martha Montoya is a businesswoman whose imagination, creative talent, and drive keep her moving to the forefront of the dialogue regarding diversity contracting with corporate America. She is leading several initiatives on a national level to advance the position of Minority owned businesses. Martha has forged relationships with corporate America, State and Federal leaders to understand and bring to the table candid conversations to find solutions for the business position of Minority owned businesses.

As the Procurement Chair and board member for the advising United States Hispanic Chamber of Commerce, she is able to continue to develop such relationships at the national level, while also being active in other national, state, city and local organizations, including the State of California Governor's Conference on Small Business and Entrepreneurship Steering Committee.

Advocating on behalf of those businesses and leading dialogues are the areas in which Martha has chosen to direct her efforts as the United States adjusts to new demographics in all aspects of society: Political, Media, Home/Families and Business.

International Background
Upon immigrating to the United States, Martha developed a business career in International Trade in areas such as telecommunications, agriculture and many more. Traveling throughout 18 countries in business taught Martha cultural sensitivity, business practices and negotiating skills while delivering projects beneficial for the supplier and customer on 4 continents.

Hispanic Marketplace
Throughout her career in the United States she has developed a keen sense of the market. Her experience selling products and services to the Hispanic market over 15 years both at the corporate and retail level makes her an authority on the marketplace. She worked with many industries in various campaigns that were directed to employees, manufacturers, suppliers, retail consumers and business community. An example of her work in campaigns include working with canned pineapples from Thailand to the Hispanic market in United States tailoring flavor, size, packaging and delivery made of this program a success for the Mexican corporation.

Leadership
Martha has played a central role in the development of the U.S. Hispanic market. Among the many honors she has received include the Latin Business Association Latina Entrepreneur of the Year, Hispanic Businesswoman of the Year for 2002 by California Hispanic Chamber of Commerce among other distinctions she received from *Hispanic Magazine 2003 honoring her as one of the 100 most influential people in the U.S. market to National Latina Business Woman of the year in 2007 among many more.*

Grassroots, private sector and government
Currently, Martha is spearheading the Access to Business Capital (ABC) Program for Venture Capital. Recognizing that access to capital is the No. 1 issue for business owners, she took the steps to establish this program in 2004 and recruited the support of Venture Capitalists, corporations and governmental legislators to become the only program in United States addressing this issue at the grassroots level. Research and education are key components of the program

Affiliations
Procurement Chair and board member for the advising United States Hispanic Chamber of Commerce, advisory board Working Families for Wal-Mart, Past Chair Access to Business Capital for the California Hispanic Chambers of Commerce, Procurement pathway for the National Association of Hispanic Publications, being part of the team retooling the National Latina Business Women Association and formerly, Latin Business Association, leading convention Expo's in Los Angeles for several years.

The Business
Los Kitos Produce, LLC
LKP is a California Limited Liability Company with offices in several parts of the country, headquartered in Santa Ana, California. The majority owner and managing member is Martha Montoya. LKP's goal is to become a leader in **sustainability** with a commitment to excellent product quality and attention to the environment throughout the delivery process. LKP is diligently working on materials to further educate the various levels of the supply chain and in particular growers.

Dealing with humble growers and sophisticated buyers in Europe and the United States, Martha has learned to adapt and be patient while delivering results. Whether it was setting up a production line for lettuce for the Netherlands from Mexico via USA, a peach crop from South Africa into England or a new crop of Asparagus in Ica or Mangos in Paita, Peru for the U.S. marketplace, Martha understood the appreciation of different cultures and social issues that would mark her life to be able to deal with her career of today.

Based on her ample experience with different levels of growers and buyers, as well as the needs of today's "Green" agendas, our growers' sustainable practices include water efficiency in Panama for pineapples; use of biodegradable products for apples in Wenatchee, WA; waste reduction for strawberries in Salinas, CA; renewable energy sources in Valencia Spain for clementine oranges; minimization of carbon footprint transporting tree fruits across the country and use and protection of natural resources for melons in the Central Valley, CA.

Additionally, LKP is working with local growers and organizations to create opportunities for the region, not only for the economic well being of the region, but also making it a "Green" community. This includes, but is not limited to creating awareness for better practices in agriculture, healthy living for the local growers and their families as well as the consumers that buy our product.

Los Kitos Entertainment, LLC

Currently, Martha owns and directs a unique media enterprise, Los Kitos Entertainment LLC, which has three main divisions. The core business is the syndication, of the inspirational Los Kitos bilingual cartoon strip to over 300 Spanish language newspapers in the United States. The first newspaper that published Los Kitos is the Los Angeles based La Opinion, where the relationship is now evolving into the internet platform. A second division is the licensing of the characters to several licensees ranging from Good Humor Ice Cream, State Farm Insurance, and to assist those companies to expand their presence in the Hispanic market. The third division of LKELLC is utilizing the characters to bring edu-entertainment to the U.S. Hispanic community through lifting edu-entertaining comic books for organizations such as: NASA, Bank of America, Kraft, Wal-mart, Sodexho, SHPE (Society of Hispanic Professional Engineers) Johnson & Johnson, IBM, to name a few.

Countless hours of radio, TV, print and personal appearances in schools, parent's organizations and community events on diverse issues such as Science, Math, Health, Finance and mainly access to higher education have made Los Kitos and Martha Montoya a leader on Hispanic kids, their parents and their environment. Her immigration to the United Status and the lessons learned of tolerance, patience, respect, laughter, joy, are at the very core of the message in the Los Kitos cartoon strips.

El Mundo Newspaper

The paper was first founded in 1988 and throughout our twenty years of publishing in the Washington market has focused on quality, commitment to community and unmatched service to our advertisers.

As of October 2008, El Mundo was acquired by new management including Gustavo Montoya, President, and Martha Montoya, Publisher. Bringing an emphasis on customer service and new technology, the Montoyas are maintaining and building upon the award winning editorial content.

Academic

As a child born to educators, in Bogotá, Colombia, Martha began her professional career as a teacher of Chemistry, Biology and English in her native country. Upon arriving to the United States, Martha integrated herself into the educational system, having taught in both the public and private school systems in California.

Besides Martha's formal education in Colombia she has earned a certificate from the University of Chicago and has pursued post graduate business courses at the Tuck School of Business at Dartmouth.

Chair LANDRIEU. Thank you, Ms. Montoya. The Hispanic community is very fortunate to have you as a leader, and all of our country is. We really appreciate the passion.

And I am so excited about this testimony and the many specific recommendations that we have heard about ways that we can reduce the barriers that I outlined just a few of them, and you all have really built upon that and I really appreciate it.

I wanted to ask, starting with you, Ms. Montoya——

Ms. MONTOYA. Yes, ma'am?

Chair LANDRIEU. I, too, am familiar with this Goldman Sachs initiative and am very impressed with it. One of the reasons I happen to be familiar is because one of the cities that they happened to choose is New Orleans, so much to my joy and happiness, they have established this initiative in New Orleans and I think in 20 or 30 other communities around the country.

Could you describe just briefly, and we are going to do this for another five or ten minutes and then go to our third panel, but could you describe briefly why you are impressed with the program, the components of it? And I think, Marc, you are familiar with it, too, and I would like to ask—you are on the Advisory Board. I would like to ask you to comment about it, as well.

Ms. MONTOYA. Being on the ground, I will talk from the ground, bottom up. They have been working with the local community leaders, meaning that they really, instead of using bankers of their own, they come to the local community leaders and then they use organizations that have been on the ground longer with a little bit of track history, understanding that there is some flexibility that you need, that sometimes your score is not that great, that sometimes your interest in the employees, the way you report employees, are not that great, different angles that you normally, you need to buffer in order to be able to present to a bank. So it has allowed the organizations to have that patience to clean them up in order to bring them into the banking system. So that is number one.

And number two, because they are definitely being patient with the program, because it is a different type of program than the regular banking program, and that gives them a little bit of flexibility for reporting to the institutions here and their regulators.

Chair LANDRIEU. Okay.

Mr. Morial.

Mr. MORIAL. Let me—should raise the profile of the Goldman Sachs 10,000 Small Business Program, and I would say its promise and its success is based on, number one, it is a partnership between Goldman Sachs, people at universities like Wharton, and community-based organizations, of which the National Urban League, the U.S. Hispanic Chamber, and other organizations are part of it.

Secondly, its focus is, in effect, an entrepreneurs' boot camp where businesses are selected to participate in what is probably about a four- to six-month highly intensive technical assistance, hands-on training regimen, the result of which is to develop for each business that participates in the program a growth plan, if you will.

A couple of observations. One, the investment in a very specific curriculum designed primarily by Wharton, which is designed for the hands-on entrepreneur, it is not overly academic nor too pedestrian. It was designed to fit the entrepreneur who wants to grow their business.

Number two, it is not a program for the start-up. It is a program for the person who has made a commitment to entrepreneurship and has, in effect, fallen down, gotten up, has, in effect, some sweat in the game already.

And then I think, number three, with the endorsement of Goldman and people like Warren Buffett and an advisory board and partnerships, the hope is that they are going to be able to connect those businesses with capital opportunities. One focus area that I know this committee is familiar with is the CDFI community, the Community Development Financial Institutions, of which there are many. The National Urban League is just in the process of creating one. So they try to connect these businesses at the conclusion of the program, at the successful completion of the program, with CDFIs.

I would also point out that we at the National Urban League, in fact, hired a firm that graduated from the program to provide security at one of our special events. And so this is a great program and I would emphasize that it is the kind of thing that demonstrates what the private sector can do in a very real way, and there is no government money but there is significant government endorsement and support towards this program.

Chair LANDRIEU. Well, I appreciate that.

My last question, and then I will turn it over to Senator Snowe, is for Dr. Fairlie. This Goldman program, I think, can serve as a model of the kind of partnership that I am hoping the SBA and our community banks and other potential partners can develop. We will be interested to see how it pans out, because at the end of the program, I think, you actually get $25,000 or $35,000 or some significant amount of money to invest in your business.

But, Dr. Fairlie, anything you want to add? You submitted some wonderful testimony, but is there anything that you think the panel did not touch on that you would like to add, and then I am going to turn it over to Senator Snowe.

Mr. FAIRLIE. Well, I guess one of the things that, you know, in your kind of opening remarks that I think was really interesting is this issue about how people are very surprised by the wealth inequality. One of the things that I found in preparing for this testimony is that it has actually gone up, right. The difference before was $80,000, roughly, between non-minorities and African Americans and Latinos, and now that wealth disparity has increased to $100,000, at least the latest data that are available from the Census Bureau.

And home ownership, I looked at those trends and they really have not changed, either. We really do not see this kind of improving trend. And I think that, as you mentioned before, that we want to kind of encourage responsible home ownership, I think that is actually really important as kind of a long-term strategy here.

And the new numbers that I found from the FDIC on banking rates were shocking in the sense that 20 percent of industry families do not have a bank account. I mean, that just seems kind of

like a basic part of our attachment to being able to build wealth, to being able to kind of participate in kind of financial services.

And I also mentioned about the payday loans. A lot of minority firms also use credit cards to finance their businesses. These are higher-cost financial services, and there are a lot of alternatives out there and it seems like that maybe financial literacy or some kind of programs that could help that would really be useful.

Chair LANDRIEU. Thank you so much.

Senator Snowe.

Senator SNOWE. Thank you.

I will continue with you, Dr. Fairlie. In your research as well as in your testimony, you indicated that minority-owned firms are more likely not to apply for conventional loans from conventional lenders due to rejection fears, and you said among firms with gross receipts under $500,000, 33 percent of minority firms did not apply for loans because of fear of rejections, compared to 17 percent of non-minority firms.

What would you say with respect to the SBA's track record, which I think is reasonably good when you look at specifically, as I mentioned in my testimony, regarding the micro loans, 46 percent of SBA micro loans went to minorities. There were 21 percent 504 loans, 22 percent of the SBA's 7(a) loans. What would you think about the average minority entrepreneur—and I would ask others, as well—on behalf of your constituencies, about how they view the SBA's lending track record and do they apply, or do they view these loans as obtainable, or do they fear rejection from the SBA, as well?

Mr. FAIRLIE. You know, that is a good point. The data do not have that kind of information in them, unfortunately, so it is not clear of this 33 percent of minority firms that are not applying for a bank loan because of fear of rejection, if that is directly for an SBA-backed loan or if it is kind of a more sort of traditional loan from a bank account. That would actually be very useful information to know. I have not really heard any kind of anecdotal evidence on that, either, unfortunately.

Mr. MITCHELL. The fact of the matter is, you have to go through a bank to get to the SBA, so——

Senator SNOWE. That may be the starting point.

Mr. MITCHELL [continuing]. It is not as if they would go around the bank.

Senator SNOWE. Okay. So that may be—the point of entry still——

Mr. MITCHELL. Absolutely.

Ms. MONTOYA. Still the bank.

Senator SNOWE. Yes, Ms. Montoya.

Ms. MONTOYA. And I think the important point for us in the Hispanic community, the bankers are not culturally sensitive or language adaptable, and so in our case, going, it is a waste of time and it is like talking two different languages and two different cultures. So that, I think, is the biggest thing. That is why I insisted on the training through the CRA programs for the banks, because we need the banks to train more people on the ground.

Senator SNOWE. I see.

Ms. Allen.

Ms. ALLEN. Yes. This is anecdotal. Two points. Some of our members who have expressed to us that getting a loan through the SBA just costs too much money than getting the private market.

Second, there are some banks who are very aggressive, like Wells Fargo Bank is, I think, is the number one lender of SBA loans. I do not know what they did, but they have been very successful. Maybe there are some best practices there that we could——

Senator SNOWE. Who was that?

Ms. ALLEN. The Wells Fargo Bank.

Senator SNOWE. Oh, Wells Fargo. Okay.

Ms. ALLEN. They might have some best practices that we can learn from. However, overall, other folks that I have talked to in the Asian American business community is, if I cannot get it from the regular bank, I ain't going to the SBA because it costs me a few more points.

Senator SNOWE. That is interesting. Well, it is clearly something—Mr. Morial?

Mr. MORIAL. I would just affirm everything that has been said, but also to highlight the need for greater visibility for the SBA programs.

Senator SNOWE. Yes.

Mr. MORIAL. Mr. Mitchell made a very important point. You go to the bank. So in the mind of the business, unless you go to the bank, you are not even going to be aware of, perhaps, the availability of loans through the SBA. So there is a greater need for visibility about all of the programs that exist and that are available.

Senator SNOWE. Well, that is an interesting point. We have that problem sometimes across the board, interestingly enough, in communicating and getting the message out overall to entrepreneurs and probably more especially among minority communities. So that is clearly something we have to figure out, which leads me to the next question, because as you heard Ms. Johns refer to the new programs that were created, were any of your organizations consulted in the drafting or the development of these two programs, and by using other lenders, like CDCs, the Certified Development Companies and so on, does that help in any way, or is that still a barrier?

Mr. MITCHELL. We were—Industrial Bank, we were—and the National Bankers Association—we were not consulted. But I have to say this about the SBA, that over the years, and particularly in the last two or three years, the SBA has improved its processing times tremendously. I believe that these new programs are very much needed programs. In meeting with Ms. Johns and Michael Grant, the President of the NBA, about a month or so ago, I was very impressed with how they have changed the administration at the SBA. They do need funding so that they can eliminate or reduce some of their fees, because traditionally, they are very expensive.

Senator SNOWE. Ms. Montoya.

Ms. MONTOYA. In L.A., we had a wonderful Hispanic guy who was the number one SBA gentleman, but I understood why, and we discussed this, it is precisely because of the fact that he is culturally sensitive to the variables that happen. So, no, we were not consulted, but I understand that they are overwhelmed.

And these programs in particular, we are hearing about it through the different people, but not really because they are targeting through the banks or the banks are not coming to us. I am concerned about that. Why is it that the banks are not visiting us? I think that there is one suggestion I have. There is the famous HR one that is about the training, workforce training, that might be effective, and my suggestion was to try to get the banks to apply for this type of workforce training so we can train more bankers.

Senator SNOWE. That is a good point.

Ms. Allen.

Ms. ALLEN. We have a regional chapter in California that covers the Western Region. We have a very good, close working relationship with the SBA in San Francisco. The L.A. office has some leadership changes and we are still trying to figure out who to work with.

But unfortunately for the headquarters here, in the last two years, we have not been reached, and this is the first time I have met Marie Johns. I tried to call her, and I told her today, I said, I am glad I got to meet you. I had to come here to meet you. I hope that the SBA would be more proactive in reaching national organizations like us. I do not know about Marc, but we have absolutely been absent at the table. During President-Elect Obama's transition, I was at the table for seven meetings from the SBA to the International Trade, and all of a sudden, they just dropped dead. They were so concerned with compliance or whatever.

And they had a conference or a summit in California where I have a major chapter. I did not know about it until—when I found out, the registration was closed. So maybe with your influence, they could reach out more.

Senator SNOWE. Absolutely. That is a message we will definitely convey, if they have not already heard it right now. Absolutely. Very important.

Mr. MORIAL. In our case, our position papers were consulted, so——

[Laughter.]

We have a 12-point jobs plan. We last year had a six-point jobs plan. And we have advanced some of the ideas that the SBA has embraced in creating new, more available and accessible loan products, and we think those are important steps in the right direction.

I would again point out the guarantee fee, which means a good product, you could add an expense and a cost to it that makes it burdensome and makes it more expensive.

And secondly, just indicate the need for continued extensive outreach. Ms. Johns did share with me today that they are about to do some—take some steps toward outreach, and I think organizations like ours are just an incredible resource, because we touch 6,000 small businesses in nine cities and probably another, you know, I am sure, 5,000 to 6,000 in other communities, and people come to our organizations as trusted conduits for information. Where can I go? What can I do? Because we are not the government and we are not the bank, so people sort of look for us to say, this is a program. Maybe that one may not be so good. Why do you not check out this person at that bank, because that is the SBA lender at that bank in your community.

So we are a continuing resource for you here at the committee, for the SBA, and for everyone that wants to really, really grow our businesses.

Senator SNOWE. Thank you.

Mr. MITCHELL. If I may just add, given all the conversation, I think——

Chair LANDRIEU. We need to conclude this panel. We want to get to the third panel.

Mr. MITCHELL. Yes. I think it makes it evident, the importance of minority banks and community banks all around the country, because community banks are the ones that are really doing the lending to small businesses and that is on what I call Main Street and Urban Street, and that is where our banks operate. Thank you very much.

Chair LANDRIEU. Well, thank you, and I know that Senator Snowe will join me in opportunities to promote this outreach, potentially by the two of us doing some field hearings or conferences specifically bringing organizations like this together with the SBA, because we are very serious about making these connections.

We thank you for the work that you do. We want to make sure the Federal Government is doing its part. Thank you so much.

And we will get to the third panel. Thank you so much. Our third panel today are two representatives of the Federal Government. One is the Inspector General for the Small Business Administration, Ms. Peggy Gustafson, and our final witness today is Mr. Greg Kutz, Managing Director of Forensic Audits and Special Investigations for GAO. His report has been referenced several times today.

If you all would come forward, we thank you so much on the second panel.

Ms. Gustafson, we will start with you. We thank you for being here and for waiting patiently, both of you, for this third panel.

We are going to probably continue this hearing until ten or 15 minutes after 12:00. We will give you all time for your opening remarks. I know you prepared five minutes. If you can shorten it at all, that would be great and we will get right to questions, but please feel free. You have been very patient.

STATEMENT OF PEGGY GUSTAFSON, INSPECTOR GENERAL, U.S. SMALL BUSINESS ADMINISTRATION

Ms. GUSTAFSON. Senator Landrieu and Senator Snowe, thank you very much for the opportunity to come speak to you today.

Based on my discussions with committee staff, I am going to focus my testimony on issues we found both through the investigations and audits in the government contracting procurement area, though, of course, I am always happy to answer any questions you may have about SBA programs and issues we may have in those programs.

Now, getting right to the area of the criminal investigations that we undertake involving procurement fraud, generally, most of these cases involve people who are either making false representations in order to be accepted into a program where preference is given to those types of contractors or there are schemes set up or illegal deals, as it were, between a small company and a large com-

pany where basically the small company is simply being used as a pass-through and actually the money from the government and the work is being done by the large company, and in many instances, of course, contrary to the regulations and to the laws. And so those are most of the types of cases we see.

For example, we recently had a guilty plea where there was an 8(a) firm that was actually being managed and controlled by a nondisadvantaged individual against the regulations that specifically state how the firms are supposed to be managed and had obtained over $5 million in Federal contracts and eventually was convicted of that.

We have had an instance where there were people—there was a person claiming falsely to be a service-disabled veteran and, again, was receiving that preference and had received over $16 million in Federal contracts and has now been indicted for that fraud.

And we have had actions under the False Claims Act where companies are claiming to be in a HUBZone, Historically Underutilized Business Zone, and again receiving contracts on that. We have gotten some recoveries, including a recovery of over $1 million from one company who was falsely claiming to be in that HUBZone.

Now, many times, our ability to prosecute this type of contracting fraud is hindered by the fact that, in general, the government is not assumed to have suffered a loss in these instances, which is to say the government paid for services and they got services in return. And many times, that makes these cases very unattractive to prosecutors who are dealing with the Federal Sentencing Guidelines that are ending up with these cases resulting in very small fines, little or no jail time.

I do want to thank the committee for their hard work in getting the presumption of loss language that has been discussed briefly into the bill. I will suggest to you, as you know from my testimony and from conversations we have had, we do have legislative proposals that we hope the committee is able to take that would go even further and would actually make it—would statutorily mandate that when a contract is awarded to a company that has gotten that under false pretenses, the amount of loss is not just presumed to be the amount of the contract, which is sometimes rebuttable. They can come back and say, well, no, you got services in return. Instead, it is. It defines it as the loss and it takes away their ability to rebut that presumption.

And I think that would go a long way to getting some much more serious jail time and some much more hefty fines from these companies. A lot of times, nothing is a better deterrent than the proverbial perp walk of somebody going in cuffs, and especially if they are getting time or if it is really hitting their pocketbook, because these are big contracts. The more that you can do that, the greater impact you are going to have.

As mentioned prior in this hearing, suspension and debarment is a key tool that the government has to stop some of this activity, because if you can cut off the ability of these wrongdoers to get government contracts, you are really hitting them where it hurts.

Senator Snowe, there has been some discussion about some statistics. I will tell you that we will work with the agency to get you the statistics and make sure that we are doing apples-to-oranges

and you know exactly where these cases are, because I think there is a little confusion going on there and I just want to make sure that we will do that.

We do applaud the agency. I think they are doing a better job. I think they were doing such a not better job for a long time that there is a way to go, but I appreciate that the agency has reached out to us. We are working with them and the proof will be in the pudding. And so it will be interesting going forward to continue to have this discussion and see how we do.

To give the agency a little credit, I have to say, suspension and debarment government-wide is a widely under-used tool, so they are not the only ones who really need to get a lot better at it.

I am going to cut it short there. Again, I am happy to talk to you, look forward to talking to you about any audits.

Looking forward to April and hopefully the next hearing, because I am very appreciative of, Senator Landrieu, your commitment to doing oversight hearings. I am here when you want me and I look forward to it, so thank you very much.

[The prepared statement of Ms. Gustafson follows:]

STATEMENT OF PEGGY E. GUSTAFSON, INSPECTOR GENERAL
U.S. SMALL BUSINESS ADMINISTRATION

BEFORE THE SMALL BUSINESS AND
ENTREPRENEURSHIP COMMITTEE, UNITED STATES SENATE
MARCH 3, 2011

Introduction:

Chair Landrieu, Ranking Member Snowe, and distinguished members of the Committee, thank you for giving the Small Business Administration (SBA) Office of Inspector General (OIG) the opportunity to discuss some of our current activities.

As you know, I head an independent office established within SBA by statute to deter and detect waste, fraud, abuse and inefficiencies in SBA programs and operations. Every year, our staff of approximately 110 employees, which includes criminal investigators, auditors, attorneys, and program analysts, conducts numerous criminal investigations to identify fraud and other wrongdoing throughout the country, and issues dozens of audit reports identifying weaknesses and deficiencies in SBA programs and operations.

Based upon discussions with Committee staff, I understand that the Committee's interest in my testimony is primarily to learn about fraud in SBA preferential contracting programs (such as the Section 8(a), HUBZone, Service-Disabled Veteran-Owned (SDVO) and Woman-Owned Business Programs), and problems we have identified with SBA's management of these programs, so the Committee can assess whether these factors restrict minority access to contracting opportunities. That will be the focus of my testimony today, although I am happy to answer any questions about the SBA OIG's work in SBA loan and other programs.

Criminal and Civil Fraud Cases and Administrative Enforcement Actions

The OIG is very concerned about continued fraud and improper activity in the 8(a), SDVO, HUBZone Programs and other preferential contracting programs, identified through OIG audits and investigations and recent reports from the Government Accountability Office. Most of our investigations of procurement fraud involve false statements by those who seek to exploit SBA programs for their personal gain by either: (1) falsely claiming to meet eligibility criteria; or (2) fraudulently using an eligible business as a "pass-through" so that an ineligible company will actually perform the work and receive most of the profits. If ineligible companies improperly profit from preferential contracting through fraud and illegal conduct, legitimate companies necessarily have fewer opportunities to benefit from these programs.

For example, in one recent case, the owner of a Georgia firm pled guilty to making false statements to get into the 8(a) Program by concealing the involvement of her former employer, who was not a socially and economically disadvantaged person, in the management and operations of her firm. Her false statements resulted in SBA certifying her firm as an 8(a) company and allowing it to obtain 8(a) set-aside contracts valued at about $5.4 million.

As another example, in the SDVO program, an investigation that we participated in recently resulted in the indictment of a man for making false statements. He is alleged to have falsely claimed SDVO status for his company, resulting in the award of four set-aside contracts totaling over $16 million.

In the HUBZone program, we have investigated applicants who falsely claimed to meet the requirement to have their principal office located in an SBA-certified HUBZone. In other cases, firms have not met the requirement that 35% of its employees live in the HUBZone, but a lack of clear regulatory language hampers our ability to pursue this issue. Other cases have involved HUBZone firms not performing the required percentage of work on a contract or acting as a "pass-through" for large businesses. Working with the Department of Justice's Civil Fraud Section, we have had recent success in pursuing False Claims Act cases against several HUBZone-certified companies for falsely statements regarding their principal office location. These cases resulted in the civil recovery of $1.3 million. Recovery in these cases has been hindered, however, because, although some of these companies received millions of dollars in contracts, they spent the money and had few assets to satisfy a judgment.

As a complement to criminal prosecution and civil fraud recovery, the SBA OIG works to promote the suspension and debarment of contractors from all procurement and other non-entitlement governmental programs for fraudulent and improper conduct. From FY 2009 to today, the SBA OIG has referred twenty-six contractors for suspension or debarment. Among cases that my office has assisted on, SBA took the aggressive action last fall to suspend GTSI and two other contractors that were involved in pass-through contracts issued by the Department of Homeland Security. Although the SBA OIG commends the Agency for taking this strong action, we believe that SBA could be more proactive in pursuing debarments and other enforcement activity against those who wrongfully obtain preferential contracting benefits.

For example, the SBA OIG presented the Agency with a plan in 2010 to bring about a more robust suspension and debarment program. Although SBA has implemented portions of this plan, including the provision of additional training to Agency staff, it has not implemented critical elements of this proposal. In particular, SBA has not yet issued a notice to its employees emphasizing the importance of identifying and pursuing suspension and debarment, and has not implemented an effective program to ensure that key agency personnel, such as those who work on procurement protests and program eligibility reviews, are regularly referring potentially suspicious activity to the SBA suspension and debarment official. The SBA OIG believes that the Agency needs to change its culture so that employees understand that their mission includes not only assisting small businesses, but also ensuring accountability and integrity to prevent fraudulent and improper actions from depriving procurement opportunities for legitimate firms.

Despite our success in bringing to justice some wrongdoers who have committed fraud in SBA preferential contracting programs, one significant impediment to prosecution stems from the fact that, in these cases, there has been no financial loss to the Government. Unlike a case where a contractor has falsified invoices for goods or services that were not provided, in many cases of preferential contracting fraud the Government does obtain the particular good or service that it paid for and sought to procure.

Without an associated and definable loss to the government, criminal prosecutors are often reluctant to pursue action against these companies or, if they do pursue them, may only be

able to obtain limited sentences. For example, in one recent HUBZone case in Kentucky that we were successful in getting a prosecutor to accept, we obtained a guilty verdict, but the sentence was only a $1,000 fine and two years probation. This light sentence was based upon Federal sentencing guidelines which require that, in determining the extent of loss, a credit must be applied for any benefit (i.e., goods and services) that the Government obtains as a result of the defendant's wrongdoing.

In order to address this impediment and to enhance criminal prosecution and civil fraud recovery against those that commit fraud in obtaining or performing set-aside contracts, the SBA OIG has developed a legislative proposal to revise section 16(d) of the Small Business Act. Most significantly, this proposal would provide that in criminal or civil fraud prosecutions arising under SBA preferential contracting programs, the amount of loss to the Government would equal the amount paid on the contract. In addition, the OIG proposal would:

(1) Impose penalties for false statements not already covered by the section, including fraudulent statements made to obtain a contract set aside for SDVO companies or to obtain grants or cooperative agreements under the SBIR and STTR programs;

(2) Enhance prosecution of "pass-through" contracts by adding a section that would provide that companies that submit invoices or requests for payment on preferential contracts would be deemed to certify that they are performing the required percentage of work on the contracts, and that false certifications would result in criminal penalties;

(3) Add provisions to cover false statements made to get into an SBA program, such as the 8(a) program, or false statements made to SBA in connection with the protest of a proposed contract award; and

(4) Revise the definition in the Small Business Act of a service disabled veteran to require that a person has been determined by the Department of Veterans Affairs or the Department of Defense as being service disabled (the current definition merely covers someone with a service-connected disability, without requiring that either agency has verified this condition.)

The SBA OIG urges the Committee to take up these proposals.

Our efforts to obtain prosecution of preferential contracting fraud have also been complicated by contracting officer error. Too often, good cases are undermined by errors by contracting personnel at Federal agencies who do not comply with small business contracting requirements. We have seen errors where agencies relied on inappropriate governmental databases or company websites to determine whether the firm was eligible for a preferential award or failed to investigate suspicious discrepancies. Too often, however, we find that procurement personnel are unfamiliar with the applicable preferential contracting requirements.

To address this concern, my office, for many years, has identified a management challenge to SBA to work with the Office of Federal Procurement Policy and the various government procurement training organizations to establish robust training of all contractor personnel on preferential procurement regulations and requirements. We are encouraged that the Interagency Task Force on Federal Contracting Opportunities for Small Businesses, which SBA

is co-chairing, has recently issued a report identifying training on small business procurement as one of its key objectives.

Audits of SBA Preferential Contracting Programs

SBA OIG audits over time have identified ongoing problems with SBA's oversight and administration of its preferential contracting programs. In many cases, we have found that SBA is not devoting sufficient resources to perform effective oversight of these programs. (See SBA OIG Audit Reports Nos. 5-18 and 6-15). More effective management and steps to broaden the availability of these programs could reduce barriers to entry.

One current audit that we are close to completing shows that these problems continue. SBA undertakes on-site visits, known as surveillance reviews, to review procuring agency files to determine, among other things, whether contracting offices are properly awarding and monitoring preferential contracts consistent with applicable regulations. Although this report is still in draft, and we are waiting for comments from the Agency, generally speaking, our review found that SBA had only evaluated a limited number of procuring offices over the past seven years, and did not use a systematic, thorough, or consistent approach in identifying which offices were reviewed or which information was evaluated.

In addition, although SBA delegated its contract execution authority to procuring agencies over 10 years ago, and said that it would monitor procuring agency compliance with 8(a) requirements through its surveillance reviews, our audit of surveillance reviews found that this had not been done. Lastly, there are regulatory limits on subcontracting which serve as an important control to preclude small business set-aside contracts from becoming "pass-throughs" to large businesses. However, our audit found that the review teams generally did not evaluate whether small businesses and 8(a) firms were performing the percentage of work that is required by these regulations.

Another audit that we are currently working on involves SBA's Mentor Protégé and Joint Venture Programs. Under these programs, SBA approves large, non-disadvantaged companies to partner with disadvantaged firms in performing set-aside contracts. Past audits have found that SBA has not devoted sufficient resources to effectively prevent abuse in these arrangements, and we will determine in our current audit whether the Agency has improved its oversight. One positive development is that SBA's recent revision of its 8(a) regulations eliminated some of the ambiguities regarding mentor protégé and joint venture arrangements, and enhanced reporting requirements for these arrangements. However, we believe that more can be done to establish effective controls to prevent abuse in these programs.

SBA could also take steps to ensure that a broad range of companies benefit from the Agency's preferential contracting programs. In the 1990's, the SBA OIG issued reports raising concerns about the fact that only a small number of 8(a) companies were obtaining a disproportionate number of contracts in the program. As a result, the Agency implemented a cap on the number of sole-source contract awards that 8(a) program participants can obtain.

However, recent SBA OIG audit work found that this problem continues. An OIG review found that the growth in awards to 8(a) firms owned by Alaska Native Corporation (ANC), which are not subject to this sole-source cap, may be restricting opportunities for other

program participants and challenging SBA's oversight capabilities. Long-term 8(a) contracting trends show a continued and significant increase in obligations to ANC-owned participants, many of which were made through sole-source contracts. 8(a) obligations awarded to ANCs grew from $1.1 billion in FY 2004 (about 13 percent of 8(a) contract dollars) to $3.9 billion (about 26 percent of total 8(a) dollars) in FY 2008. However, the number of ANC owned firms that earned this 26 percent of 8(a) dollars in FY 2008 represented only 2 percent of companies performing these contracts. This growth suggests that the special advantages afforded ANC-owned firms may be limiting opportunities for other 8(a) participants.

In addition, while the 8(a) program is benefiting Alaska Natives to some extent, the OIG's review showed that a few ANC participants received a disproportionate share of the 8(a) obligations: 50 percent of Federal 8(a) obligations made to ANC participants in FY 2007 went to just 11 (or 6 percent) of the ANC firms reported by SBA to Congress that year. Further, these top 11 ANC-owned firms received 82 percent of their 8(a) obligations through sole source awards. As studies have shown that sole-source contracts do not always provide the Government with the best value, it is questionable whether providing ANCs with contracting advantages under the 8(a) program is the most cost-effective way of assisting Alaska Natives.

Our review also found that many ANC firms have clear advantages over other 8(a) program participants when competing for contracts. Since ANC-owned firms are not subject to all of the size restrictions that apply to other 8(a) participants, the ANC companies often enjoy access to capital, resources, and management expertise not available to other firms in the program. Other recent reports regarding ANC and tribally owned firms have focused on the fact that non-disadvantaged individuals have exerted considerable control over these companies and, in some cases, have improperly benefited by charging exorbitant "management" fees without providing obvious value to the ANC companies.

Conclusion

The SBA OIG will continue to investigate fraud in SBA procurement and other programs and to seek effective solutions to limit waste and inefficiencies and promote the benefits of these programs. Thank you for the opportunity to comment, and I look forward to answering any questions that you may have.

CURRICULUM VITAE
PEGGY E. GUSTAFSON
INSPECTOR GENERAL
UNITED STATES SMALL BUSINESS ADMINISTRATION

Prior to becoming the Inspector General for the Small Business Administration in September of 2009, Ms. Gustafson served as General Counsel to Senator Claire McCaskill, advising the Senator on issues relating to homeland security, government oversight, judiciary issues, and ethics. During her tenure working for Senator McCaskill, Ms. Gustafson helped write two bills that have significantly strengthened the federal offices of Inspectors General: the Inspector General Reform Act of 2008 and the legislation that created the office of the Special Inspector General for the Troubled Asset Relief Program.

From 1999-2007, Ms Gustafson served as General Counsel in the Missouri State Auditor's Office. In that capacity, managing a legal office, she worked closely with state auditors on issues of the scope of the auditors' duties, the auditors' need to access records, and all other legal issues arising in the course of the audits. She also represented the State Auditor's Office in litigation relating to fiscal notes prepared for statewide ballot initiatives, up to and including briefs before Missouri Supreme Court.

From 1995 to 1999, Ms. Gustafson served as an assistant prosecutor for Jackson County, Missouri. As a prosecutor, she tried felony criminal cases of every type, including first degree murder cases, had sole responsibility for charging and trying arson cases, and handled certain appeals. She also served as a team leader of a white collar crime trial team, and was appointed as a Special Assistant United States Attorney to work on areas of white collar crime and public corruption.

From 1993 to 1994, Peggy Gustafson served as an assistant county counselor for Jackson County, Missouri, representing the County in civil litigation, including the enforcement of county laws and the defense of county officials and correctional officers in cases arising under 42 U.S.C. Sec. 1983.

A native of Chicago, Illinois, Ms. Gustafson received her Bachelor of Arts from Grinnell College in Grinnell, Iowa in 1989, and her Juris Doctor from Northwestern University in Chicago in 1992. After law school, she was a law clerk to the Honorable Don Kennedy on the Missouri Court of Appeals.

Chair LANDRIEU. Thank you.
Mr. Kutz.

STATEMENT OF GREG KUTZ, MANAGING DIRECTOR OF FORENSIC AUDITS AND SPECIAL INVESTIGATIONS, U.S. GOVERNMENT ACCOUNTING OFFICE

Mr. KUTZ. Madam Chair, Ranking Member Snowe, thank you for the opportunity to discuss the 8(a) program. Today's testimony highlights the results of our 2010 investigation into allegations of fraud and abuse in this program.

My testimony has two parts. First, I will discuss cases of fraud and abuse, and second, I will discuss the importance of having effective fraud prevention controls.

First, we receive dozens of allegations and leads related to fraud and abuse in the 8(a) program. We invested 14 of these cases, as Senator Snowe mentioned, which often included more than one firm. We found that as of January 10, these 14 ineligible firms had received $325 million of 8(a) sole source and set-aside contracts. In addition, they received $1.2 billion of other Federal contracts, including $17 million related to the Recovery Act.

The key program eligibility requirements we looked at as part of this fraud investigation, just to go over those again, include, first, firms must be owned at least 51 percent and controlled by socially and economically disadvantaged individuals. Second, the firms must have reasonable potential for success. Third, firms must perform 15 to 50 percent of the work on their own. And fourth, they must be a small business.

A few examples of the fraud and abuse that we identified include one owner misrepresenting her ethnicity; another owner failing to report joint ownership in over $4 million of real estate; another owner with a $2.5 million home on a private island, a Lamborghini, and a $450,000 yacht; another owner whose tax return showed over $1.9 million of wages and over $100,000 of tax-exempt interest income; and finally, front companies funneling 8(a) contracts to an ineligible firm that had left the program in 2001.

With respect to fraud prevention, we found some strengths and weaknesses at the SBA. For example, several strengths in the application process helped prevent three of the bogus applications that we filed from being approved. The review of these applications appropriately raised questions about our firm's income, assets, and potential for success. However, we were successful in obtaining certification for a fourth bogus firm.

Key weaknesses that we identified include SBA's lack of independent validation of key owner information, including assets and net worth. In addition, SBA often does not perform thorough annual reviews for 8(a) eligibility. For example, case file information had tax returns that showed that the firms were no longer eligible for the program. And as Ms. Gustafson said with respect to enforcement, historically, enforcement has not been necessarily an effective tool here for this program.

We have provided six recommendations to SBA to strengthen their fraud prevention controls and they have taken action on some of those recommendations, while implementation of others is in progress.

In conclusion, for just 14 cases, we identified $325 million of fraud and abuse in this program. The victims of this fraud and abuse are not only taxpayers, but legitimate socially and economically disadvantaged firms. And along the lines of the hearing today, one way to expand access to legitimate firms to the 8(a) program is to prevent the kind of fraud and abuse that we identified.

Madam Chair and Ranking Member Snowe, that ends my statement and I look forward to your questions.

[The prepared statement of Mr. Kutz follows:]

United States Government Accountability Office

GAO

Testimony

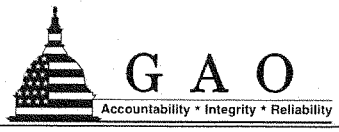
Before the Committee on Small Business and Entrepreneurship, U.S. Senate

For Release on Delivery
Expected at 10:00 a.m. EST
Thursday, March 3, 2011

8(a) PROGRAM

The Importance of Effective Fraud Prevention Controls

Statement of Gregory D. Kutz, Director
Forensic Audits and Investigative Service



GAO-11-440T

Madam Chair, Ranking Member Snowe, and Members of the Committee:

Thank you for the opportunity to discuss the results of our prior investigation of the Small Business Administration's (SBA) 8(a) Business Development Program. SBA's 8(a) program, named for a section of the Small Business Act, is a development program created to help small, disadvantaged businesses compete in the American economy and access the federal procurement market. To participate in the program, a firm must be certified as meeting several criteria, including: be a small business as defined by SBA; be unconditionally owned and controlled by one or more socially and economically disadvantaged individuals who are of good character and citizens of the United States; and show potential for success. Upon certification, firms can obtain federal contracts without competing fully and openly for the work. For example, agencies are permitted to enter into sole-source contracts after soliciting and negotiating with only one 8(a) company. They also can participate in restricted competitions for federal contracts, known as set-asides, open to only 8(a) companies. In March 2010, GAO issued two companion reports on the 8(a) program, one focused on internal control procedures and processes that SBA has implemented to ensure that only eligible firms participate in the program and one focused on fraud prevention.[1] My testimony today is based on the latter report, and addresses three issues: (1) whether ineligible firms were participating in the 8(a) program, (2) the results of our proactive testing of the application process, and (3) strengths and weaknesses in SBA's fraud prevention system.

To determine whether firms were participating in the 8(a) program through potentially fraudulent misrepresentation, we used a risk-based approach to identify firms that exhibited signs that they were not qualified for the program. We also reviewed allegations of fraud and abuse sent to our e-mail address established to receive reports about small business contracting programs. For the firms we selected for further investigation, we reviewed documentation available from SBA in the firms' official 8(a) files maintained in district offices. We conducted both announced and unannounced site visits and interviewed firm employees and executives. The selection of the 14 firms we investigated was not representative and

[1] GAO, *Small Business Administration: Steps Have Been Taken to Improve Administration of the 8(a) Program, but Key Controls for Continued Eligibility Need Strengthening*, GAO-10-353, (Washington, D.C. Mar. 30, 2010) and GAO, *8(a) Program: Fourteen Ineligible Firms Received $325 Million in Sole-Source and Set-Aside Contracts*, GAO-10-425 (Washington, D.C.: Mar. 30, 2010).

the findings from these 14 cases cannot be projected beyond those cases. To proactively test whether SBA's 8(a) application process and controls were sufficient to prevent ineligible firms from entering into the program, we established four bogus businesses and submitted falsified applications and supporting documentation to SBA. To determine what strengths and weaknesses, if any, existed in SBA's fraud prevention system, we made observations based on our case studies and proactive testing. Furthermore, we compared controls in place at the time of our review of the 8(a) program to a fraud-prevention model we developed and utilized in prior small business contracting investigations. A full description of our scope and methodology is included in appendix I of our report.[2] We also requested an update from SBA on any actions that it had taken on our recommendations. We did not validate any representations made by SBA.

We conducted our audit work and investigation from October 2008 through January 2010 in accordance with U.S. generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our objectives. We performed our investigative work in accordance with the standards prescribed by the Council of the Inspectors General on Integrity and Efficiency (CIGIE).

My testimony today summarizes our findings on each of the three issues discussed in our report. Specifically, we found that:

- ***Ineligible firms are participating in the 8(a) program.*** We identified 14 firms that received set-aside or sole-source 8(a) contracts worth $325 million through fraud or abuse. These 14 firms received another $1.2 billion in other federal obligations since entering the 8(a) program, including $17 million in awards through the American Recovery and Reinvestment Act of 2009.[3] We found evidence that shows officials at 13 of these firms misrepresented their eligibility for the program to fraudulently acquire or maintain 8(a) status and obtain

[2] GAO, *8(a) Program: Fourteen Ineligible Firms Received $325 Million in Sole-Source and Set-Aside Contracts*, GAO-10-425 (Washington, D.C.: Mar. 30, 2010).

[3] This $1.2 billion includes both non-8(a) awards, as well as 8(a) awards that these firms were eligible to receive.

federal contracts awarded with limited or no competition. Examples include underreporting adjusted net worth and serving as a "pass-through" for non-8(a) companies. In the case of a pass-through, an 8(a) firm receives the sole-source or set-aside contract, but contrary to program requirements, work is performed and managed by a non-8(a) company. We also determined that SBA staff responsible for annually assessing firm eligibility allowed 3 firms to remain in the 8(a) program and receive contracts despite clear evidence provided by company officials during annual reviews that showed they were no longer eligible. For example, SBA allowed a firm to remain certified even though the president reported a salary which substantially exceeded the threshold. Permitting ineligible firms to obtain 8(a) contracts undermines the intent of the program and deprives qualified firms from receiving targeted contracting opportunities. A description of all 14 case studies is included in Table 1 of our report.[4] Subsequent to issuing this report, we referred all 14 cases to SBA and the agency's Office of Inspector General.

- ***SBA's application process has both strengths and weaknesses.*** SBA had certain strengths in its 8(a) application process that allowed the agency to correctly determine that three of the four bogus firms from our proactive testing were not eligible for the 8(a) program. We also identified vulnerabilities that demonstrate weaknesses ineligible firms could exploit to fraudulently receive program certification. In the first of our three unsuccessful applications, SBA stated that it denied our application because the firm lacked the financial capacity to perform 8(a) contracts. For the other two cases, SBA raised concerns about our eligibility based on the presidents' adjusted net worth. The agency also questioned control of one of these firms. SBA provided us with such thorough comments that we determined we could not overcome the deficiencies and eligibility issues identified in both applications, so we abandoned them. However, we obtained 8(a) certification for one bogus firm using fabricated documentation and fictitious owner information. We consider this a vulnerability because unscrupulous firms could do the same to create front companies and funnel 8(a) contracts to themselves, circumventing eligibility requirements. A description of the scenarios and outcomes for all four bogus firm applications is included in our report.[5]

[4] GAO, *8(a) Program: Fourteen Ineligible Firms Received $325 Million in Sole-Source and Set-Aside Contracts*, GAO-10-425 (Washington, D.C.: Mar. 30, 2010).

[5] GAO, *8(a) Program: Fourteen Ineligible Firms Received $325 Million in Sole-Source and Set-Aside Contracts*, GAO-10-425 (Washington, D.C.: Mar. 30, 2010).

- ***SBA's fraud prevention system has both strengths and weaknesses.*** The 14 case studies of ineligible firms discussed above and the certification of a bogus firm show that weaknesses exist in SBA's controls for preventing, detecting, monitoring, and investigating fraud and abuse in the 8(a) program. Fraud prevention requires a system of controls which, in their aggregate, minimize the likelihood of fraud occurring while maximizing the possibility of detecting any fraudulent activity that may transpire. Fraud prevention systems set forth what actions constitute fraudulent conduct and specifically spell out who in the organization handles fraud matters under varying circumstances. A well-designed fraud prevention system should consist of three crucial elements: (1) upfront preventive controls, (2) detection and monitoring, and (3) investigations and prosecutions. For the 8(a) program this would mean effective (1) front-end controls at the application stage, (2) fraud detection and monitoring of firms already in the program, and (3) the aggressive prosecution or suspension and debarment of individuals committing fraud. In our report we describe specific strengths and weaknesses that we identified during the course of our review. For example, a strength we identified was SBA's use of certain third-party sources, such as Dun and Bradstreet and the Credit Bureaus, to verify some information about our bogus firm that was certified for the program. Nevertheless, these controls did not allow SBA to identify the fake documents we submitted. We also reported that based on our limited review there was indication that SBA staff responsible for assessing firms' continued eligibility did not always follow established program criteria during the annual review process. As mentioned previously, some of the 14 firms were determined to be ineligible after our investigators confirmed information that was concealed from SBA by firm presidents. In other cases, our review of SBA's files clearly indicated that these firms were not eligible for the 8(a) program, yet SBA failed to terminate or graduate these firms from the program.

The consequences of these control weaknesses are substantial: in just the 14 cases we investigated for this report, over $325 million in sole-source and set-aside 8(a) contracts went to ineligible firms that manipulated the current system. To a substantial degree, the steps we took to investigate these firms could be part of an effective fraud prevention program. Victims of the fraud and abuse in this program are legitimate economically and socially disadvantaged small businesses. To address the vulnerabilities we identified, our report provided six recommendations to improve SBA's ability to screen and monitor fraud and abuse within the 8(a) program. SBA agreed with five recommendations and stated that it would evaluate

our sixth recommendation related to how family members' assets are included in the assets of the 8(a) participant based upon the comments received as a result of the proposed 8(a) rule change.[6] Although SBA needs time to implement these changes, and we have not done a comprehensive follow-up on their actions, SBA has taken action on some recommendations, while according to SBA, implementation of others is in progress. For example, SBA enacted final regulation changes on February 14, 2011 which address three recommendations relating to firm eligibility requirements. The regulations provide more clarification on factors that determine economic disadvantage as it relates to total assets, gross income, retirement accounts and a spouse of an 8(a) company owner when determining the owner's ability to access capital and credit. These changes take effect on March 14, 2011. In addition, SBA officials told us that they have been evaluating the use of third-party data systems to verify firm information when conducting initial certification reviews. SBA officials also stated that they have provided forensic accounting training to all SBA staff responsible for conducting these initial certification reviews, and the agency plans to expand this training in fiscal year 2011 to all SBA field staff responsible for annual reviews. SBA officials also stated that they will revise the program's standard operating procedures to reflect the regulatory changes, to increase certain reporting requirements and to provide more detailed and concrete guidance on initiating suspensions and debarments. In addition, according to SBA, the agency has taken steps to terminate some of the firms identified in our report, and has referred other cases to the SBA Office of Inspector General.

Madam Chair, and Ranking Member Snowe, this conclndes my statement. I would be pleased to respond to any questions you or other Members of the Committee may have.

[6] Our companion report on the 8(a) program's internal controls also contained six recommendations to SBA that included providing more guidance to help ensure staff more consistently follow procedures, reassessing certain staff workload distribution, and developing more standard processes for documenting and analyzing certain program data. SBA agreed with each of the six recommendations. See, GAO, *Small Business Administration: Steps Have Been Taken to Improve Administration of the 8(a) Program, but Key Controls for Continued Eligibility Need Strengthening*, GAO-10-353.

Contacts and Acknowledgments

For additional information about this testimony, please contact Gregory D. Kutz at (202) 512-6722 or kutzg@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement.

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Biography of Greg Kutz

Mr. Kutz is the Audit Director for GAO's Forensic Audit and Investigative Services team. This team provides the Congress with high quality forensic audits and investigations of fraud, waste, and abuse, and evaluations of security vulnerabilities and other requested investigative services. This team also monitors and manages fraud, waste, and abuse tips received through GAO's fraud hotline.

In 1991, Mr. Kutz joined the Government Accountability Office after 8 years at KPMG Peat Marwick. As a Senior Executive at GAO, Mr. Kutz has testified at congressional hearings over 80 times primarily on matters related to fraud, waste and abuse and other special investigations. Mr. Kutz has been responsible for reports issued by GAO and testimony relating to credit card and travel fraud and abuse, improper sales of sensitive military and dual use technology, tax fraud and abuse, wage theft, Hurricane Katrina and Rita fraud, transit benefit fraud, Medicare and Medicaid fraud, procurement fraud, pay problems for military members, death and abuse of teenagers at private boot camps, and seclusion and restraint of disabled children in schools.

Mr. Kutz is a Certified Public Accountant (CPA), Certified Fraud Examiner (CFE), and Member of the Association of Certified Fraud Examiners Professional Standards and Practices Committee. Mr. Kutz was a 2010 Service to America Medals Finalist for Justice and Law Enforcement.

Chair LANDRIEU. Thank you very much.

I appreciate, Ms. Gustafson, your testimony as being confirmed, I guess, over a year and a half ago now——

Ms. GUSTAFSON. About so, yes.

Chair LANDRIEU [continuing]. By this committee. What would you say you found when you came into the SBA in terms of oversight for fraud and abuse and what you are finding now, I mean, in comparison to existed prior to you getting there and now? I am going to ask you the same, Mr. Kutz.

Ms. GUSTAFSON. Senator Landrieu, as you noted, I was confirmed in September. I started in October. And so what I found when I got there, I would say, is a longstanding attitude of SBA that enforcement was really kind of anathema to what their mission was, and in some ways it is because they are there to promote small businesses, make sure that the small businesses are getting the contracts and the access to capital that they need. And often, enforcement, both in the lending area and the contracting area, is contrary to that in some ways because you are—it runs counterintuitive to promoting as much as you can and encouraging as much as you can.

I have been heartened in the year and a half that I have been there by the attitude and by some of the actions that have been taken since I have been there, like the insistence that they will be serious about enforcement. I think the message from the top has been exactly the right message. I think the movement that they have done in the suspension and debarment area to really shore it up and to be not as afraid to suspend companies as they were, because I think they had had a traditional theory of unless there was a conviction, you know, they would suspend or debar you if you had been convicted of something, but before that, there was a real hesitancy, and I think they have made definite indications that they are willing to protect the government's interest before that happens, which is why suspension and debarment is there.

Again, there has been some very good movement. The right things are being said. It is a big battleship, like everything else, that takes a while to turn, and that is why I look forward to continuing the oversight of our office, to having the authorizing committees kind of keep them on their toes, because it is hard to change a culture and there is a little bit of a culture change that has to be done and seems to be being done in SBA.

Chair LANDRIEU. Mr. Kutz, you have been with the GAO since 1991, so you have got over a ten-year history—well, it would be 20 years——

Mr. KUTZ. Almost 20, unfortunately.

Chair LANDRIEU. Almost 20.

Mr. KUTZ. Yes.

[Laughter.]

Chair LANDRIEU. Getting tired——

Mr. KUTZ. I had a lot more hair when I started.

[Laughter.]

Chair LANDRIEU. I should be able to add that, at least. But over 20 years. Is your view the same as Ms. Gustafson just testified, or do you see it differently as opposed to the change over the last, let us say, ten years or so?

Mr. KUTZ. My experience with SBA only goes back three or four years, so even though my GAO experience is 20. But I would say when we started three to four years ago, the culture of advocacy versus enforcement was clearly there, and it still is to some extent. But service-disabled and HUBZone were basically self-certification, rubber stamp-type programs. HUBZone has moved forward and they are making good progress, although there are still issues, as you mentioned earlier, about The Alamo, et cetera. Eight-A had the strongest controls of the three programs that we have looked at, but as our report last year shows, there is still room to grow there. So I think they have taken some steps in the right direction, but there is still quite a ways to go.

Chair LANDRIEU. Thank you.

Senator Snowe.

Senator SNOWE. Thank you both for outstanding work. Again, it is essential we make sure that all of the taxpayers' dollars are being spent efficiently and legally, and that is the key here, and all the more so given the fact that we have enormous deficits, and so trying to exact the oversight that is essential, especially now.

But more importantly is, to the point that you were making, Ms. Gustafson, about the idea that we have to create an environment to make sure that we do not create any disincentives, whereby people or companies or organizations feel that they can utilize and take advantage of these programs illegally or unethically. So I think that this is the issue that we need to revamp, especially on the question of how we can increase the penalties, and also to exact responsibility on the part of the agencies, as well, not make it so optional in terms of whether or not they take action.

Now, on the 26 that you cited and that I referred to earlier to Ms. Johns, can you explain to me in any way at this point about the three in which they did take action, but what happened to the remaining 23?

Ms. GUSTAFSON. Yes, Senator Snowe. I do have some information on that and I think that there was some confusion about my testimony, and I apologize for that, in that the three that I was discussing that I was giving the agency credit for because they deserved credit for being out there on that was not the only subset of the 26 where action had been done.

So just—what I can give you right now, and again, I will get back to you with more specifics, of the 26 universe with more specificity, the agency has declined to do anything in six of those cases. They have suspended eight. There are two pending. They have debarred six. Two of those cases were actually debarred by somebody else while SBA was kind of deciding what to do. And two, there were warning letters sent. So there was more action taken than was, I guess, implied by——

Senator SNOWE. What generally is the reason for an agency not taking action? Too expensive, or they do not have the personnel? What is the issue here, because I am not sure that I understand, even if somebody is out of the program.

Ms. GUSTAFSON. I really think it is a mind——

Senator SNOWE. The fact that they violated the law——

Ms. GUSTAFSON. I really think it is a mindset. There is a risk aversion to doing something affirmative like suspension and debar-

ment. And again, I think it is probably government-wide. That really is not warranted, given what the suspension and debarment program is supposed to do, which is to say—it is a tool there preconviction. Before you can get to the point where you have proven somebody guilty by reasonable doubt, there are ways to protect the government's interest when you think that somebody is acting unethically or illegally, you know, doing things in opposite to the way the program is to be run, and I am kind of amazed at that.

I mean, I am kind of amazed at that because you really do need to be out there and be a stronger protector for the interests, and that is why I say I do think the current General Counsel, the Deputy General Counsel, they have been very aggressive in these matters and we as an office have been very appreciative of that, because they have reached out to us.

But again, when I talk about turning the ship, there are people who have been there who just are honestly almost terrified of the thought of getting out there and suspending or debarring people. That is the best that I can explain because I do not explain it—I cannot—I do not understand it past there.

Senator SNOWE. Right. I understand what you are saying——

Ms. GUSTAFSON. Right.

Senator SNOWE [continuing]. But that is very helpful to us in trying to determine how to proceed on those issues——

Ms. GUSTAFSON. Okay.

Senator SNOWE [continuing]. Because, clearly, action is warranted and we have to reverse that culture, any inhibition that exists in taking proactive action, frankly.

Ms. GUSTAFSON. Right.

Senator SNOWE. I mean, when you are talking—just thinking this cumulatively across government-wide, all the agencies——

Ms. GUSTAFSON. Right.

Senator SNOWE [continuing]. The millions, if not the billions, that might be out there that have been misappropriated, you know, utilized illegally.

Ms. GUSTAFSON. Exactly. Yes.

Senator SNOWE. So I appreciate your work in that regard and we would like to have those numbers that you have.

Ms. GUSTAFSON. Oh, absolutely, yes.

Senator SNOWE. You will? You will submit them?

Ms. GUSTAFSON. Yes, I will.

Senator SNOWE. Okay. Mr. Kutz, on the 14 ineligible firms, what happened within the agency? I noted in the report here, as well, that there was an indication the SBA staff who were responsible for assessing firms' continued eligibility did not always follow established program criteria during the annual review process. So what was the case? So were there existing standards and criteria by which these ineligible firms could have been initially detected?

Mr. KUTZ. Yes. I mean, someone making $1.9 million a year, based upon historical case law and now in the new regulations, I believe, would not be eligible for the program. Yet there were case files that SBA had reviewed, and in several cases had seen and we had talked to them about, and they did nothing to address those at that time. There were three of those where they knew and they left them in the program, and they got new contracts afterwards.

Senator SNOWE. Boy, that is really hard to understand. That is amazing, because, really, it was a simple effort, but you also pointed it out to them and they did nothing.

Mr. KUTZ. Right. I mean, you had deception in most cases, but in several cases, right there in the file was the information——

Senator SNOWE. It was transparent and obvious.

Mr. KUTZ [continuing]. It was there, and then even once we made them aware, they did not really take action. That gets into the culture a little bit, too, I think, of not taking aggressive action, especially when those companies that we know are ineligible got new contracts after that.

Senator SNOWE. Well, you know, that is amazing. It is like shrugging your shoulders, oh, so what? I mean, that is just unacceptable and that is very important that we address, because the bottom line is that those who are legitimate firms that should be eligible for these funds are not able to get them because somebody else is using them illegally. So it diverts the funds from the good actors because of the bad actors——

Mr. KUTZ. I agree.

Senator SNOWE [continuing]. Let alone what they are doing with taxpayers' money.

Mr. KUTZ. Yes.

Senator SNOWE. So we have to aggressively pursue this, not only in this agency, in every agency with respect to how we deal with individuals and companies inappropriately using taxpayers' dollars. It really is stunning, to be honest with you that agencies are not aggressively pursuing it.

Finally, the SBA has developed two new programs that Ms. Johns referred to. One of the programs requires lenders to maintain at least 60% of their loan portfolio in low to moderate communities, including to businesses with 50 percent of their workers residing in low to moderate communities. Is there a way of making that determination? I mean, through self-certification, is that not a prescription for more fraud?

Mr. KUTZ. Yes, that would be the same thing as a service-disabled veteran-owned small business now, with the exception that VA has that bid certification process. But the rest of the service-disabled program is still essentially self-certification, just like that, and we have seen massive potential for fraud in that program.

Senator SNOWE. Yes?

Ms. GUSTAFSON. I would just add, it is also kind of similar to the HUBZone program. One of the biggest weaknesses in the HUBZone program is there is a requirement that a certain percentage of the people in the company getting the contract live or attempt to maintain a residence in that area.

Honestly, I am not sure how you enforce that. I mean, I am not sure how you go and prove beyond a reasonable doubt there has not been this attempt to maintain and where these workers are living, and do you stop them from moving or do you fire them? I mean, that is, I think, an inherent weakness when it is that kind of measure.

Senator SNOWE. I see. Yes, that kind of measure.

Ms. GUSTAFSON. Yes.

Senator SNOWE. So that probably should be adjusted and a different standard.

Any other recommendations? The SBA implemented five of the six recommendations.

Ms. GUSTAFSON. Mm-hmm.

Senator SNOWE. Have they set up an appropriate measurement for accountability and certification, and do you——

Mr. KUTZ. Yes. One of the things that the first witness mentioned is they have tightened up certain regulations that are effective, I think, March 14, and that has addressed certain more specifics about eligibility, social and economic disadvantage, et cetera, and along with additional steps being taken. So they are headed in the right direction, but again, I think 8(a) is—of the programs we have looked at at SBA, is the strongest of them from a standpoint of fraud prevention.

Ms. GUSTAFSON. If I could just——

Senator SNOWE. Well, is that all relative? So, obviously, we have got to do a lot on all these programs.

Mr. KUTZ. Well, it is relative. I mean, if you look at service-disabled government-wide, it is basically at almost zero because you have no controls. HUBZone is between three to five, maybe, on a scale of ten. And 8(a) is better than that. So that is kind of how I would assess where they are.

Senator SNOWE. Well, what could we do better, then? That is what we have to figure out, is how best to attack this problem. What would be your recommendation? In other words, to get them up to the level where they should be?

Mr. KUTZ. Well, it is program by program. Like service-disabled, one of our recommendations, which really is a government-wide one, is to have everybody utilize this VetBiz certification process. Why recreate the wheel when you have got someone already setting a process up? VA does know who is a legitimate service-disabled veteran to start. So I think SBA is trying to work with VA on that and it needs to—that is a government-wide solution rather than a stovepiped agency-specific solution.

Senator SNOWE. Right. Good point. Excellent point.

Ms. GUSTAFSON. And just to kind of build on those comments just quickly, if I may—I am sorry—but as Mr. Kutz has said, the 8(a) program has the most strict, I think, requirements to get into the program, which is to say it is an older program and there really are—the agency takes a very active role and does a lot more review before you even get into the 8(a). Where I think the agency definitely needs to do better is as the participants go along and the reviews, like the annual reviews that Mr. Kutz talked about and how they need to do a better job of those.

And if I could just quickly reference the audit that I mentioned in my written testimony on the surveillance reviews, and just very, very briefly, surveillance reviews are undertaken by the Small Business Administration of other procuring agencies to see how well those agencies are running the small business contracting part of their contracting portfolio. We were very interested to see how well—how thorough those reviews were, because, really, that is one of the few checks that SBA has kept as the procuring agencies have taken more of the execution of the contracts, of the 8(a) contracts.

The check that SBA has retained is doing these surveillance reviews. This is an audit that we have already discussed with the agency. Again, it is referenced.

We were very concerned about what we saw. I mean, we definitely think the agency needs to do a much better job at doing a very thorough risk analysis and making sure these surveillance reviews really are checking on how the 8(a) program is being administered and how these contracts are being seen. We were very disappointed in the thoroughness of these reviews or lack thereof. Some of the employees undertaking these reviews did not realize they were supposed to kind of be sure to be looking at 8(a).

So that is something that I think is really crucial for SBA. I mean, that is really one of the few checks they maintain to make sure that this program that is such a big part of government contracting and so important, especially when it comes to access to these opportunities, to make sure that this is being undertaken the correct way. So that is something that I want to point to that we are going to continue to look at and we will definitely make sure that the committee is aware of——

Senator SNOWE. Are these annual reviews required by law?

Ms. GUSTAFSON. The annual reviews of every 8(a) firm are required by law. The surveillance reviews are not. That is one of the things that the agency sets. However, the agency, when they talk about their oversight of the 8(a) program, they speak to these surveillance reviews and how this is such an important tool for them, and that is why I think it is important that they do a very thorough review and make sure that the employees undertaking these reviews—I mean, if this is how they are going to make sure the agencies are doing the 8(a) program right, then these reviews take on import, whether or not they are legally required, and they place a lot of reliance on these reviews, so they are really crucial.

Senator SNOWE. Yes. Thank you all. Thank you both very, very much.

Chair LANDRIEU. Thank you very much.

The meeting is adjourned.

[Whereupon, at 12:18 p.m., the committee was adjourned.]

APPENDIX MATERIAL SUBMITTED

Summary of Testimony – Deputy Administrator Marie Johns

- SBA's lending programs support companies that struggle with access to conventional capital.

- A study by the Urban Institute showed that women- and minority-owned small businesses are three-to-five times more likely to receive SBA loans than conventional loans.

- As a result of a tight credit market over the last two years, the overall share of SBA loans going to small business in underserved communities has decreased significantly.

- From Fiscal Year 2008 to FY10, overall SBA 7(a) lending to small businesses in underserved communities dropped nearly 5 percent—and that decline has been greater in some communities. This equates to a drop of $780 million in loans to the businesses that need them the most.

- Lower dollar loans were significantly important to helping entrepreneurs in underserved communities start and grow their businesses. Often, a small business does not need a $1 million or $2 million loan. They need $50,000 to buy new equipment, or $100,000 to renovate their building.

- SBA recently announced two new loan initiatives, **Small Loan Advantage** and **Community Advantage,** which are designed to get lower dollar loans into the hands of small business owners.
    - Small Loan Advantage is open to lenders in our Preferred Lending Program.
    - Community Advantage opens our 7(a) lending program to "mission lenders," such as Certified Development Companies (CDCs), Community Development Financial Institutions (CDFIs), and SBA-certified microlenders.

- SBA's 8(a) business development program has been critical in helping these small businesses win contracts, grow, and create jobs. To strengthen the 8(a) program even further, the SBA recently undertook the first regulatory review process in over a decade.

- SBA also recently finalized and released the Women's Contracting Rule. The rule is a critical step toward giving women-owned small businesses better opportunities to compete for federal government contracts.

Summary of Testimony: Dr. Robert Fairlie

- The rate of businesses filing for bankruptcies in the United States is more than twice as high as it was in mid 2007. Contributing to the high rate of business closings are the lingering tight credit conditions for small businesses resulting from the financial crisis.

- Research that Dr. Fairlie and others have conducted indicates that minority businesses face significant barriers to entry, growth and survival even in more favorable economic conditions.

- Minority firms are more vulnerable because they are generally smaller and have fewer resources to draw on in difficult economic times.

- The average minority-owned business has revenues of $178,000 per year, which is less than 40 percent of the level for non-minority businesses.

- Minority owned firms also hire fewer employees and have lower profit levels.

- Minority-owned businesses have substantially lower levels of financial capital invested in their businesses.

- Minority-owned businesses have an average of $3,400 of equity investments and $46,500 in loans. Non-minority owned businesses have values of equity investments and loans that are more than twice as large.

- **Half of all African-American families have less than $8,700 in total wealth, and half of all Latino families have less than $13,400. These levels of wealth are one-ninth to one-thirteenth the levels of wealth held by non-minorities ($113,800).**

- These low levels of wealth among minorities translate into fewer startups and undercapitalized businesses because an entrepreneur's wealth is often invested directly in the business or used as collateral to obtain business loans. Entrepreneurs are also frequently required by investors to invest their own money in the business as an incentive.

- Minority-owned businesses are more likely to experience loan denials, pay higher interest rates, and are less likely to apply for loans because of a fear of rejection.

- Businesses owned by minorities produce more than $1 trillion in total sales. They employ 6 million workers and have an annual payroll of $168 billion. They also create another 6 million jobs for themselves as owners.

- Restricting minority business growth ultimately limits total U.S. productivity, job creation and innovation, which are essential for getting our economy back on track.

Summary of Testimony: Marc Morial

- Small businesses have always played a critical role in the economic well-being of communities of color. Recent statistics published by the US Census Bureau show that the black-owned business grew by 60% in the 5-year period between 2002 and 2007. Within these numbers lie evidence of the role entrepreneurship plays in communities where big-business hiring has slowed to a trickle, or even frozen to a complete halt.

- Of the 1.9 million American small businesses identified by the US Census Bureau as being African-American owned, over 1.8 billion are sole proprietorships.

- African-American owned firms have proven to be an engine of job creation, with paid employment growing by 22% from 2002 through 2007, compared to less than 1% such growth for non-minority owned firms.

- Minority Business Enterprises (MBEs) face major systemic challenges that make their success an uphill battle against the odds from the moment of their inception, and at every step of the way to success. We see these challenges as falling into four primary categories:
    - Clear communication of programs that are intended to assist MBEs.
    - Access to reasonable priced capital through private-sector commercial sources
    - Access to federal contracts, either prime or subcontract opportunities.
    - Technical assistance that is provided for the many different levels of MBEs.

- The National Urban League's Entrepreneurship Center Program (ECP) enables minority entrepreneurs to take advantage of new business opportunities and qualify for financing that will lead to high-level business growth through the provision of proper management skills.
    - In 2010, the centers provided 10,911 hours of counseling and 11,242 hours of training services to 5,938 entrepreneurs. These services assisted entrepreneurs in receiving $20.19 million in new bonding, new contracts and financing during the year.

- It is time that our country set about a course of dramatic and sustained steps in support of black-owned, as well as all other minority and women owned small business enterprises. National Urban League Recommendations for Promoting the Growth of MBEs
    - Raising the cap for set-aside small business contracts from $100,000 to $500,000
    - Unbundling contracts will be helpful in allowing more small- and minority-owned businesses to have the opportunity to bid on federal contracts.
    - Increasing the federal procurement goals for small- and minority-owned businesses and the requirement of a subcontracting plan would need to include a non-federal monitoring system
    - Creation of a fund for technical and contracting assistance through the Minority Business Development Agency (MBDA).
    - Elimination of the guarantee fee on the SBA's new Advantage loan initiatives as a way to stimulate loan activity for small and minority businesses.

Summary of Testimony – Susan Au Allen

- US Pan Asian American Chamber of Commerce Education Foundation (USPAACC) was founded as a 501 (c) (3) nonprofit organization in1984 in the nation's capital, we have been serving and will continue to serve as the gateway to large corporate and government contracts, top-caliber Asian American and small/minority suppliers, key information about Asian American and small/minority businesses, and contract opportunities in the dynamic Asia-Pacific market.

- Our main goal is to work with each of our constituents to achieve successful contracting relationships and business growth in the mainstream marketplace.

- We work in key markets across the country, reaching over 15,000 Asian American-owned and other SMEs through our Regional Chapters in the West Coast, Southeast, Southwest, Midwest, Northeast, and Washington, DC-Maryland-Virginia in the National Capital Area.

- In some cases, higher sales can cost more cash and so more cash is needed to run the business. For others, when sales slow dramatically because of the recession, they need cash to make up the shortfall, maintain payroll and wait.

- While some 8(a) companies may find small business loans attractive, many banks continue to be reluctant to lend because there is still a lot of risk. Unlike the manufacturing sector that have collaterals for a loan, small businesses in the service sector do not.

- Contract Bundling encourages a mindset among federal contract evaluators that large and recognizable companies are more reliable and should be awarded contracts over small or medium sized companies.

- Giving incentives to agencies, their contracting team, or the Primes for giving opportunities to new businesses will reduce or avoid complacency and remedy this ongoing problem. Changing the way business is done with suppliers will also mean scrutiny and accountability.

- We believe there should be a program to provide the next-level of training, that actually links mid-tier companies to potential opportunities, and helps to transition soon-to-graduate 8(a) companies into the open marketplace when they are no longer eligible for set-asides.

- The quality of the Request for Proposals should be addressed. Oftentimes, they are not clear, contain inconsistencies, had to be pulled back and reissued.

- A small business' past performance is crucial to the bidding process. If experience on the commercial or private side were to be equally valued and taken into consideration, then it would help level the playing field for small businesses to enter the federal marketplace.

- Insourcing limits new opportunities for small businesses and takes existing contracts away from them.

- Expand 8(a) Mentor-Protégé Program (MPP). Including, having a program that puts mid-sized companies and small businesses together to foster and grow. Graduated 8(a) firms would be a good source of Mentors.

Summary of Testimony: Martha Montoya

- Martha Montoya is the President of several enterprises including, Los Kitos Produce, in the business of getting fruit from the farm to the store shelf, Los Kitos Entertainment a syndicated cartoon strip and content provider, and El Mundo Newspaper, the largest and oldest Hispanic newspaper in Washington State. Ms. Montoya is also Procurement Chair and Board Member at the U.S. Hispanic Chamber of Commerce.

- Currently 95% of Hispanic businesses do not fit the lending profile of banks, are too small for private equity funds, receive minimal attention from venture capital firms, and yet are the fastest growing segment of the entire country.

- Given the alarming lack of capital available for Hispanic entrepreneurs, Martha strongly encourages the Committee to ask economic policy agencies and regulators such as the Federal Reserve and the Treasury to focus their effort on supporting minority small business entrepreneurs through their Community Reinvestment Act obligations, so they in turn will request the banks to deploy those funds into the communities, and particularly into rural areas.

- **Community Reinvestment Act funding could serve as a vehicle for the following reasons and actions:**
    - Equity funds for local banks, investment funds and others with more flexibility to deploy funds and with a higher level of patience for their returns.
    - Large scale banks to deploy the CRA funding themselves and work while training the next generation of bankers.
    - Request minimum 25% of the CRA funding to go to rural areas. It will motivate and unlock creativity in our rural areas and growth.
    - Match CRA funding with local financial tools from SBA and others to take away the burden of infrastructure capital yet create sustainable jobs for the next 2-5 years.
    - Inform, inform and inform through our publications and media outlets. HR 2727, known as the "Financial Transparency Restoration Act". Requiring banks and financial institutions to publish a statement of financial condition at the end of each fiscal quarter in a newspaper of general paid circulation published in a city or county within each market area in which the financial institution is located.

- **Training** – smaller banks and financial institutions need to implement Workforce training to better serve our communities. However if the proposed H.R. 1 passes, for the Fiscal Year 2011 Continuing Resolution (CR), it will eliminate all funding, over $3.6 billion, for the Workforce Investment Act (WIA) in Program Year 2011 and a $175 million rescission of Prior Year funds.

Summary of Testimony: Peggy Gustafson

- As Inspector General of the SBA, Peggy heads an independent office established by statute to deter and detect waste, fraud, abuse and inefficiencies in SBA programs and operations. Every year, Peggy's staff of approximately 110 employees conducts numerous criminal investigations to identify fraud and other wrongdoing, and issues dozens of audit reports identifying weaknesses and deficiencies in SBA programs and operations.

- The Committee's interest in Peggy's testimony is primarily to learn about fraud in SBA preferential contracting programs (such as the Section 8(a), HUBZone, Service-Disabled Veteran-Owned (SDVO) and Woman-Owned Business Programs).

- Most of OIG investigations of procurement fraud involve false statements by those who seek to exploit SBA programs for their personal gain by either: (1) falsely claiming to meet eligibility criteria; or (2) fraudulently using an eligible business as a "pass-through" so that an ineligible company will actually perform the work and receive most of the profits.

- **8(a) example of fraud**, the owner of a Georgia firm pled guilty to making false statements to get into the 8(a) Program by concealing the involvement of her former employer, who was not a socially and economically disadvantaged person, in the management and operations of her firm. Her false statements resulted in SBA certifying her firm as an 8(a) company and allowing it to obtain 8(a) set-aside contracts valued at about $5.4 million.

- **HUBZone example of fraud**, applicants falsely claimed to meet the requirement to have their principal office located in an SBA-certified HUBZone. In other cases, firms have not met the requirement that 35% of its employees live in the HUBZone, **but a lack of clear regulatory language hampers OIG's ability to pursue this issue.**

- **SDVO example of fraud**, an investigation that OIG participated in recently resulted in the indictment of a man for making false statements. He is alleged to have falsely claimed SDVO status for his company, resulting in the award of four set-aside contracts totaling over $16 million.

- **Despite OIG's success in bringing to justice some wrongdoers who have committed fraud in SBA preferential contracting programs, one significant impediment to prosecution stems from the fact that, in these cases, there has been no financial loss to the Government.** Unlike a case where a contractor has falsified invoices for goods or services that were not provided, in many cases of preferential contracting fraud the Government does obtain the particular good or service that it paid for and sought to procure.

- In order to address this impediment and to enhance criminal prosecution and civil fraud recovery against those that commit fraud in obtaining or performing set-aside contracts, the OIG has developed a legislative proposal to revise section 16(d) of the Small Business Act. Most significantly, this proposal would provide that in criminal or civil fraud prosecutions arising under SBA preferential contracting programs, the amount of loss to the Government would equal the amount paid on the contract.

Summary of Testimony: Mr. Gregory D. Kutz

- Gregory Kutz is the Director of the GAO's Forensic Audits and Investigative Service team, which provides Congress with forensic audits and investigations of fraud, waste, and abuse in federal programs.

- Mr. Kutz's testimony summarizes the findings of GAO's recent investigations of the SBA's 8(a) Business Development Program and in particular, the agency's efforts to prevent fraud in the program. Specifically, his testimony focuses on three issues highlighted in a March 2010 report on the 8(a) program:
  (1) whether ineligible firms are able to participate in the 8(a) program:
  (2) the results of GAO's proactive testing of the 8(a) application process, and;
  (3) the strengths and weaknesses of the SBA's fraud prevention system.

- **Ineligible firms are participating in the 8(a) program:** GAO identified 14 firms that received set-aside or sole-source 8(a) contracts worth $325 million as a result of fraud and abuse in the program; these 14 firms received another $1.2 billion in other federal obligations since entering the 8(a) program, including $17 million in awards through the *Recovery Act*. Officials at 13 of the companies misrepresented their eligibility for the program by underreporting their net worth or serving as "pass-through's" for non-8(a) firms seeking federal contracts. In several cases, SBA staff responsible for assessing firm eligibility allowed these companies to remain in the 8(a) program despite clear evidence provided by company officials that disproved their eligibility.

- **SBA's application process has both strengths and weaknesses:** During their evaluation of the application process for entry into the 8(a) program, GAO found that SBA performed well, preventing 3 of the 4 GAO created "dummy companies" from fraudulently entering the program. The one dummy company that did gain entry into the program did so by providing fabricated documents.

- **SBA's fraud prevention system has both strengths and weaknesses:** GAO recommended that the SBA take a number of steps to improve their fraud prevention and detection efforts, including the following:
  (1) create effective front-end controls during the application process;
  (2) improve fraud detection and monitoring of firms already in the program, and;
  (3) pursue aggressive prosecution or suspension and debarment of individuals committing fraud.

- Since the release of GAO's report, SBA has taken steps to address a number of these issues, including the clarification of the factors determining economic disadvantage relating to total assets, gross income, retirement accounts and a spousal assets. These changes will be fully implemented by March 14, 2011.

U.S. Census Bureau News

U.S. Department of Commerce • Washington, D.C. 20233

FOR IMMEDIATE RELEASE
TUESDAY, FEB. 8, 2011

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CB11-24
Press Kit

Census Bureau Reports the Number of Black-Owned Businesses Increased at Triple the National Rate

From 2002 to 2007, the number of black-owned businesses increased by 60.5 percent to 1.9 million, more than triple the national rate of 18.0 percent, according to the U.S. Census Bureau's Survey of Business Owners. Over the same period, receipts generated by black-owned businesses increased 55.1 percent to $137.5 billion.

"Black-owned businesses continued to be one of the fastest growing segments of our economy, showing rapid growth in both the number of businesses and total sales during this time period," said Census Bureau Deputy Director Thomas Mesenbourg.

These new data come from the *Survey of Business Owners: Black-Owned Businesses: 2007*. The survey provides detailed information every five years for black-owned businesses, including the number of firms, sales and receipts, number of paid employees and annual payroll.

Data are presented by geographic area (nation, state, county, city and metro area), industry and size of business. Preliminary national and state data were released in July 2010.

In 2007, nearly four in 10 black-owned businesses operated in the health care and social assistance; and repair, maintenance, personal and laundry services sectors. The retail trade and health care and social assistance sectors accounted for 27.4 percent of black-owned business revenue.

Among states, New York had 204,032 black-owned businesses and accounted for 10.6 percent of the nation's black-owned businesses, followed by Georgia, with 183,874 black-owned businesses (9.6 percent) and Florida, with 181,437 (9.4 percent).

Among counties, Cook, Ill., had the most black-owned businesses, with 83,733, accounting for 4.4 percent of all the nation's black-owned businesses. Los Angeles followed with 59,680 (3.1 percent) and Kings, N.Y., with 52,705 businesses (2.7 percent).

(more)

Editor's note: The data can be accessed at <http://www.census.gov/econ/sbo/>.

Among cities, New York had the most black-owned businesses, with 154,929 (8.1 percent of all the nation's black-owned businesses), followed by Chicago, with 58,631 (3.1 percent), Houston, with 33,062 (1.7 percent) and Detroit, with 32,490 (1.7 percent).

Other highlights:

- Of the 1.9 million black-owned businesses in 2007, 106,824 had paid employees, an increase of 13.0 percent from 2002. These businesses employed 921,032 people, an increase of 22.2 percent; their payrolls totaled $23.9 billion, an increase of 36.3 percent. Receipts from black-owned employer businesses totaled $98.9 billion, an increase of 50.2 percent from 2002.

- In 2007, 1.8 million black-owned businesses had no paid employees, an increase of 64.5 percent from 2002. These nonemployer businesses' receipts totaled $38.6 billion, an increase of 69.0 percent.

- The number of black-owned businesses with receipts of $1 million or more increased by 35.4 percent to 14,507 between 2002 and 2007.

The Survey of Business Owners defines black-owned businesses as firms in which blacks or African-Americans own 51 percent or more of the equity, interest or stock of the business. Additional reports from the survey highlighting other minority- and veteran-owned businesses will be issued over the next year. Subsequently, separate publications will be issued highlighting additional characteristics of all businesses and their owners.

-X-

The Survey of Business Owners is conducted every five years as part of the economic census. The 2007 survey collected data from a sample of more than 2.3 million businesses. Data collected in a sample survey are subject to sampling variability, as well as nonsampling errors. Sources of nonsampling errors include errors of response, nonreporting and coverage. More details concerning the SBO survey design, methodology and data limitations can be found at <http://www.census.gov/econ/sbo/methodology.html>.

U.S. Census Bureau
Survey of Business Owners

Black-Owned Businesses: 2007

Census Bureau Economic Data
Released on Feb. 8, 2011

United States Census Bureau

Presenters

Host	Stan Rolark
Survey uses	Marc H. Morial President and Chief Executive Officer National Urban League
Survey findings	Thomas L. Mesenbourg, Jr. Deputy Director and Chief Operating Officer U.S. Census Bureau
Survey uses	Ivonne Cunarro Chief, Knowledge Management Unit Minority Business Development Agency

Resources for Today's News Conference

Come to www.census.gov and click on the icon at the top left corner to obtain –

- Today's PowerPoint Presentation
- News Release
- Link to Survey of Business Owners Home Page
- Link to Guidance on Accessing SBO Data in the American FactFinder

Separate News Releases for the Ten Metropolitan Areas With the Largest Black Population

- Atlanta
- Chicago
- Dallas
- Detroit
- Houston
- Los Angeles
- Miami
- New York
- Philadelphia
- Washington, DC

About the Survey

- Part of the Economic Census taken every 5 years for years ending in "2" and "7"
- The only comprehensive, regularly collected data for businesses and business owners by
  - Minority status
    - Race
    - Ethnicity (Hispanic origin of any race)
  - Gender
  - Veteran status

Business Ownership by Race

- Categories of ownership are based on the race of the person or persons who owned 51% or more of the stock or equity in the business in 2007.

- "Black-owned" is defined as any firm with Black or African American owners holding a 51% or larger stake in the business.

NATIONAL URBAN LEAGUE

"Over a Century of Service"

- Founded in 1910, headed since 2003 by Marc Morial, former mayor of New Orleans and president of the U.S. Conference of Mayors.
- Mission: economic empowerment for historically underserved urban communities.
- Long partnership with the Census Bureau and the Minority Business Development Agency.
- Business data used to identify opportunities and design efficient services to assist Black entrepreneurship.
- More than 100 affiliates in 36 states and DC serving more than 2 million people.
- 12-Point Jobs Plan to boost employment through business growth.

A Look at the 2007 Statistics for Black-Owned Businesses in the United States

Black-Owned Businesses Compared to All U.S. Businesses by Employer Status: 2007

	Black-owned businesses		All U.S. businesses	
	Firms (number)	Sales and receipts ($ billions)	Firms (number)	Sales and receipts ($ billions)
All firms[1]	1,921,881	137	27,110,019	30,176
Employer firms	106,824	99	5,752,668	29,203
Nonemployer firms	1,815,057	39	21,357,351	973

[1] Includes firms with paid employees and firms with no paid employees.
Note: Detail may not add to total because of rounding.

Black Business Ownership Increased at Triple the National Rate: 2002 to 2007

	Black-owned firms in 2007 (number)	% change for Black-owned firms, 2002 – 2007	% change for all U.S. firms, 2002 - 2007
All firms[1]	1,921,881	60	18
Employer firms	106,824	13	4
Nonemployer firms	1,815,057	65	22

[1] Includes firms with paid employees and firms with no paid employees.
Note: Detail may not add to total because of rounding.

Black Business Revenues Increased Faster than National Rates: 2002 to 2007

	Black-owned firms' sales and receipts in 2007 ($ billions)	% change for Black-owned firms' sales and receipts, 2002 –2007	% change for all U.S. firms' sales and receipts, 2002 –2007
All firms[1]	137	55	34
Employer firms	99	50	34
Nonemployer firms	39	69	27

[1] Includes firms with paid employees and firms with no paid employees.
Note: Detail may not add to total because of rounding.

United States Census Bureau

Black-Owned Businesses and Their Proportion of All U.S. Firms by Employer Status: 2002 to 2007

	% of U.S. businesses that are Black-owned	
	Year 2007	Year 2002
All firms[1]	7.1	5.2
Employer firms	1.9	1.7
Nonemployer firms	8.5	6.3

[1] Includes firms with paid employees and firms with no paid employees.

Distribution of Firms by Receipts Size of Firm: 2007

Receipts size	% of Black-owned firms	% of all U.S. firms
Less than $50,000	87	65
$50,000 to $99,999	6	10
$100,000 to $249,999	4	10
$250,000 to $499,999	1	5
$500,000 to $999,999	1	4
$1,000,000 or more	1	5

Note: Detail may not add to total because of rounding.

Distribution of Employer Firms by Employment Size of Firm: 2007

Employment size	% of Black-owned firms	% of all U.S. firms
0 to 4 employees[1]	69	61
5 to 9 employees	16	18
10 to 19 employees	8	11
20 to 49 employees	5	7
50 employees or more	2	4

[1] Includes firms with payroll at any time during 2007. Employment reflects the number of paid employees during the March 12 pay period.
Note: Detail may not add to total because of rounding.

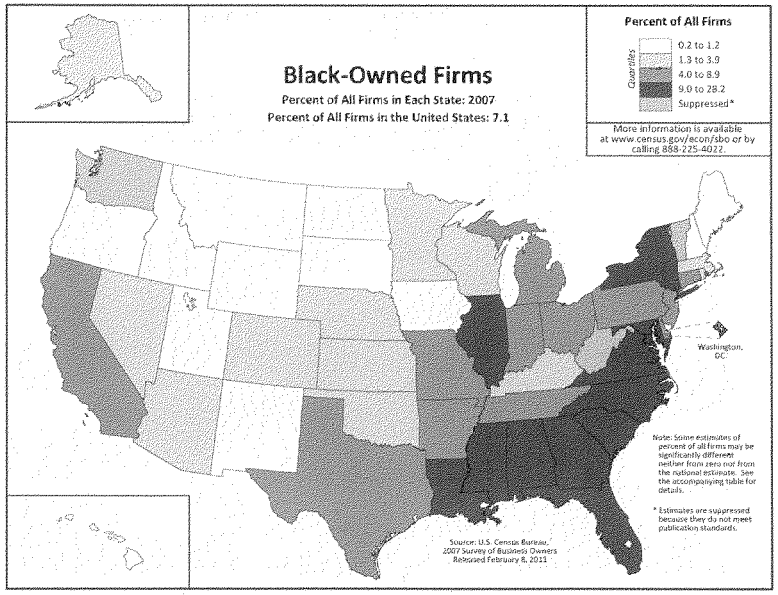
Industries With the Highest Number of Black-Owned Firms: 2007

Business sectors	Firms (number)	% of all Black-owned firms
Total for all sectors	1,921,881	100
Health care and social assistance	365,140	19
Repair and maintenance and personal and laundry services	358,332	19
Administrative and support and waste management and remediation services	216,742	11

Industries With the Largest Receipts For Black-Owned Firms: 2007

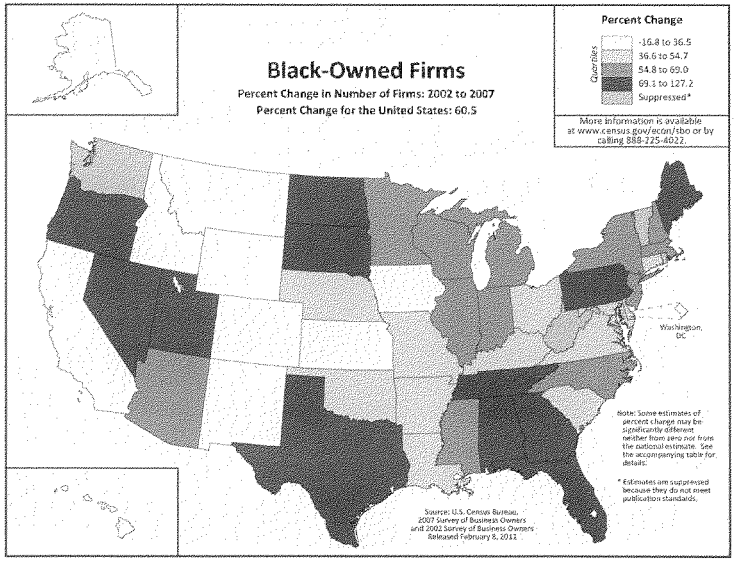
Business sectors	Sales and receipts ($ billions)	% of all Black sales and receipts
Total for all sectors	137	100
Retail trade	21	15
Health care and social assistance	17	12
Wholesale trade	15	11
Construction	13	10
Professional, scientific, and technical services	13	10

Black-Owned Firms by State: 2007



United States Census Bureau

Percent Change in the Number of Black-Owned Firms by State: 2002 to 2007



United States Census Bureau

www.census.gov/econ/sbo Feb. 8, 2011

States With the Largest Percentage of Black-Owned Firms: 2007

States and equivalent area	Black-owned firms in 2007 (number)	% of firms in state that are Black-owned	% change for Black-owned firms in state, 2002 – 2007
District of Columbia	15,774	28	29
Georgia	183,874	20	103
Maryland	102,135	19	47
Mississippi	40,613	18	62
Louisiana	59,906	16	49

Large Counties With the Highest Percentage of Black-Owned Firms: 2007

Counties and equivalent areas with a population of at least 500,000	Black-owned firms in 2007 (number)	% of firms in county that are Black-owned	% change for Black-owned firms in county, 2002 – 2007
Prince George's, MD	39,685	55	40
DeKalb, GA	28,959	40	49
Baltimore city, MD	14,644	35	50
Bronx, NY	38,726	35	64

Large Cities With the Highest Percentage of Black-Owned Firms: 2007

Cities with a population of at least 500,000	Black-owned firms in 2007 (number)	% of firms in city that are Black-owned	% change for Black-owned firms in city, 2002 – 2007
Detroit, MI	32,490	64	66
Memphis, TN	19,895	38	70
Baltimore, MD	14,644	35	50
Atlanta, GA	15,738	31	87
Washington, DC	15,774	28	29

Accessing SBO Results

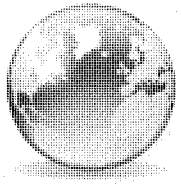
- SBO Web site: www.census.gov/econ/sbo
- For access to prepackaged data products and the ability to build custom tables, visit American FactFinder (AFF), the Census Bureau's online, self-service data access tool at www.factfinder.census.gov

SBO Release Schedule

Data	Release date
Preliminary Company Summary - Estimates of Business Ownership by Gender, Ethnicity, Race, and Veteran Status	July 13, 2010
- Hispanic-Owned Businesses	September 21, 2010
- Women-Owned Businesses	December 7, 2010
- Black-Owned Businesses	February 8, 2011
- American Indian- and Alaska Native-Owned Businesses	March 11, 2011
Series of five releases with additional information by geographic sublevels, detailed industry, size of firm, detailed Asian and Native Hawaiian and Other Pacific Islander groups, veteran status, plus business and owner characteristics data	April through June 2011

United States Census Bureau

U.S. Department of Commerce
Minority Business Development Agency



African-American-Owned Firms Outpace Growth of Non-Minority-Owned Firms

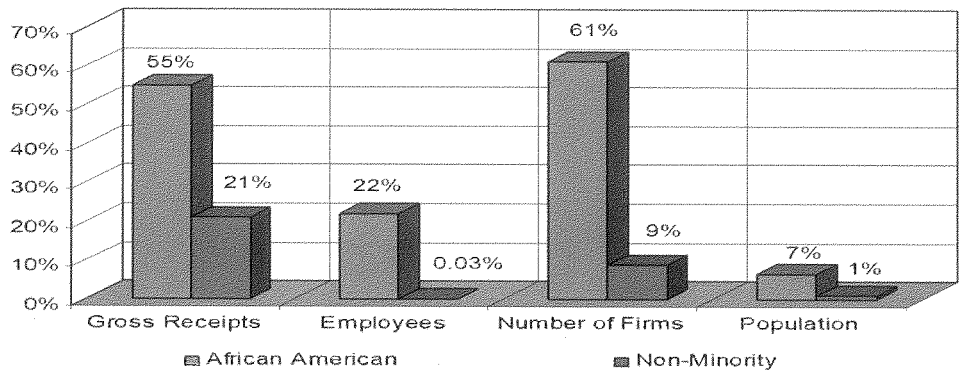
Ivonne Cunarro, Chief Knowledge Management Officer

U.S. DEPARTMENT OF COMMERCE
MBDA
MINORITY BUSINESS DEVELOPMENT AGENCY

The Big Picture

- The African-American business community continues to grow in number at a fast rate, yet their true economic potential is still unrealized.
- The fast growing trend of African-American-owned firms continued into the most recent five year period outpacing once again the growth of non-minority-owned firms in gross receipts (55% African-American growth), employment (22%) and number of firms (61%), between 2002 and 2007.
- African-American-owned firms are also an engine of job creation, with paid employment growing by 22% from 754,000 workers to 921,000 workers, compared to less than 1% growth for non-minority-owned firms.
- Average employment per firm with employees also went up from 8 employees per African American firm with employees in 2002 to 9 employees per firm with employees in 2007.

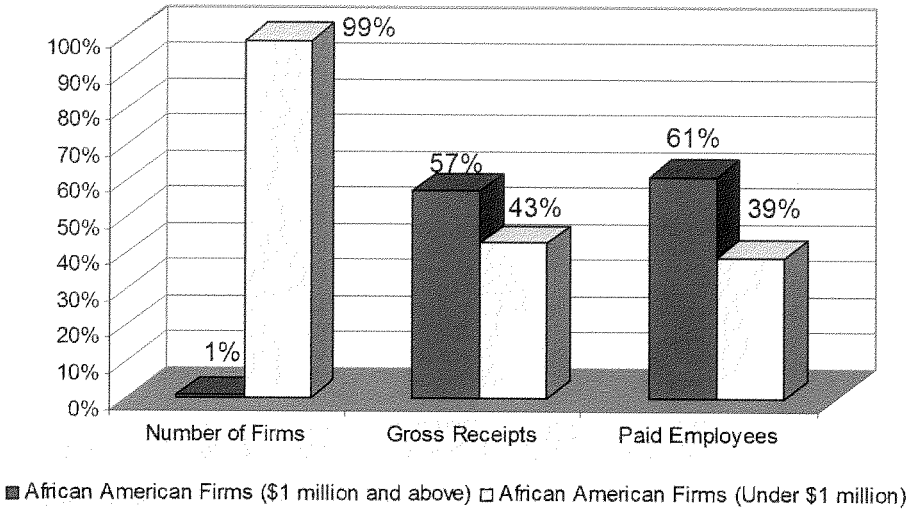
African-American-Owned Firms Outpace Growth of Non-Minority-Owned Firms



Upside of $1 Million Plus Firms

- While smaller in number, African American firms with receipts of $1 million or more generate a much larger percentage of all African American revenues and paid employment than firms with receipts under $1 million.
- African American firms with receipts of $1 million or more represented 1 percent of all the African American firms but generated 57 percent of all African American firms' gross receipts and 61 percent of all their paid employment.
- There were 14,500 African American firms which generated gross receipts of $1 million or more in 2007. These firms generated combined gross receipts of $79 billion and employed 565,000 workers.
- Average gross receipts of African American firms generating sales of $1 million or more grew **by 19 percent from $4.6 million per firm in 2002 to $5.4 million in 2007**.

African-American-Owned Firms With $1 Million and Above in Sales



Entrepreneurial Parity

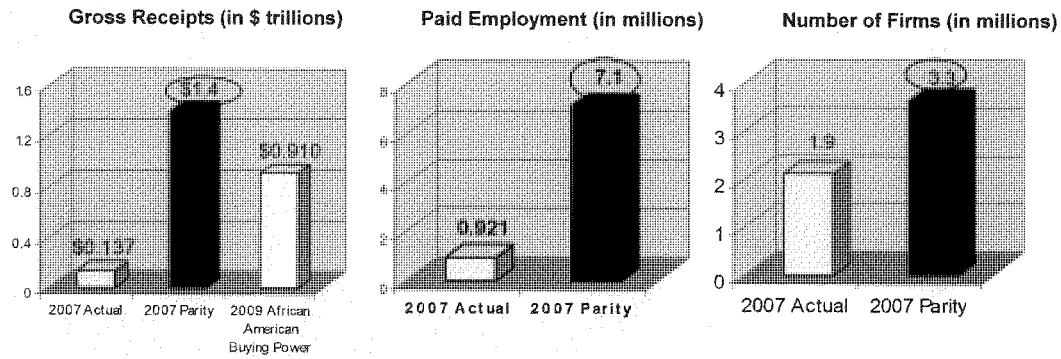
- At MBDA, we measure entrepreneurial parity of minority-owned firms. Unfortunately, there is still an entrepreneurial parity gap between African American firms and the share of the African American adult population, which is 12 percent.

- If African-American-owned firms would have reached parity with their share of the adult African American population in 2007, there would have been 3.3 million firms (instead of 1.9 million) generating $1.4 trillion in gross receipts (instead of $138 billion), and creating 7.1 million jobs (instead of 921,000).

- The faster growing African-American population increased by 7% during this period, compared to only 1% growth for non-minorities. We have to encourage further the growth of African American firms to keep up with the growth of the population.

- In addition, the African American population had an estimated purchasing power of about $910 billion, larger than the 2009 estimated purchasing power of all but 16 countries worldwide, including Australia ($824 billion), Taiwan ($717 billion) and the Netherlands ($654 billion).

Entrepreneurial Parity Remains Elusive for African American Businesses



The Downside

U.S. DEPARTMENT OF COMMERCE
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MINORITY BUSINESS DEVELOPMENT AGENCY

- While African-American-owned firms outpaced the growth of non-minority-owned firms in gross receipts (55% African-American growth), employment (22%) and number of firms (61%), only 6 percent of these firms (107,000) had paid employees and just 14,500 had revenues greater than $1 million.
- In addition, the average gross receipts for African-American-owned firms decreased by 3 percent from $74,000 in 2002 to $72,000 in 2007, well below that of non-minority-owned firms ($490,000).
- There are approximately 1.9 million sole proprietorships in the African-American business community. MBDAs goal is to help grow those in emerging industries and with the potential for size and scale, as well as encourage job creation among these firms.
- As the African-American population increases in the U.S., the success of the African-American business community becomes critical for job creation.

Minority-Owned Firms Gross Receipts

Average Gross Receipts		
African-American-owned businesses	**Minority-owned businesses**	**Non-minority-owned businesses**
$72,000	$179,000	$490,000

The Future

- MBDA is committed to making sure the growth and competitiveness of the minority business community continues to be a national priority.
- MBDA is creating the foundation for the next generation of $100 million minority-owned firms capable of employing the growing minority and U.S. population, expanding our tax base, and securing our position as a global leader.
- In fiscal year 2010, MBDA assisted minority owned firms in accessing more than $3.8 billion in contracts and financings, and creating more than 6,200 jobs.
- To grow more minority-owned firms to size and capacity, MBDA encourages minority businesses to consider growth by mergers and acquisition, joint ventures and strategic partnerships.

Contacting MBDA Public Affairs

For more information, please contact:

- Email: public_affairs@mbda.gov
- Phone: 202.482.6272

Questions?

Key Upcoming Releases from the U.S. Census Bureau

- 2007 SBO for American Indian- and Alaska Native-Owned Businesses (March)
- 2010 Census Redistricting Files (February – March)

Contact Information

- U.S. Census Bureau
  Public Information Office
  Phone: 301.763.3030

- National Urban League
  Media Relations
  Phone: 212.558.5433

- Minority Business Development Agency
  Public Affairs Office
  Phone: 202.482.6272

Introductory Comment for Compelling Interest Submission for the Hearing Record

Discriminatory barriers -- caused by both present-day discrimination in the private sector and the continuing effects of past discrimination in the private sector -- continue to persist, impeding the ability of small minority-owned business to gain access to the federal contracting marketplace on fair and equal footing with non-minority-owned businesses. These barriers also continue to prevent small minority-owned firms from realizing their full economic potential.

Accordingly, I am submitting for the record, as Attachment A to my testimony, a document entitled *The Compelling Interest for Race- and Gender Conscious Federal Contracting Programs: An Update to the May 23, 1996 Review of Barriers for Minority and Women-Owned Businesses.* This report is a thorough analysis of some of the extensive body of evidence generated in the last 15 years, all of which has been submitted to Congress. It clearly describes the discriminatory barriers that continue to hinder the success of minority-owned businesses. The report shows that these barriers deny many minority entrepreneurs equal access to sources of capital critical to business survival and expansion, as well as deny them equal access in other economic areas, including access to information about contracting opportunities, high bonding requirements, and higher costs from suppliers. This report, in our view, contains a significant amount of information that helps demonstrate the continued need for the contracting and capital programs that SBA operates which are aimed at providing minority-owned business the ability to gain a foothold in the federal contracting arena.

Compelling Interest for Race- and Gender-Conscious Federal Contracting Programs: An Update to the May 23, 1996 Review of Barriers for Minority- and Women-Owned Businesses

I. Introduction

Barriers to access to capital for minority- and women-owned small businesses must be viewed in the broader context in which these firms conduct business. As detailed below, race and gender discrimination — of which discrimination in access to capital is just one example — remain a significant obstacle for minority and women entrepreneurs, and federal programs continue to have a critical role in addressing it.

In *Adarand Constructors, Inc.* v. *Peña*, 515 U.S. 200 (1995) (*Adarand III*), the Supreme Court held that federal race-conscious classifications "are constitutional only if they are narrowly tailored measures that further compelling governmental interests." *Id.* at 227. In *United States* v. *Virginia*, 518 U.S. 515 (1996), the Court made clear that gender-conscious classifications must be substantially related to an important governmental objective.

Following *Adarand*, the government recognized that, in order to establish a compelling interest to support its race-conscious procurement programs, it must show with specificity how race discrimination and its effects diminished contracting opportunities for minorities. In 1996, the Department of Justice summarized and published in the Federal Register[1] an extensive body of evidence — including Congressional reports and hearings, academic research, state and local government disparity studies and testimony — which identified discriminatory practices affecting racial minorities that act as barriers to their participation in federal contracting. This evidence helped explain the compelling interest behind Congress's adoption of race-conscious contracting programs, such as the Small Business Administration's 8(a) program and the Department of Transportation's Disadvantaged Business Enterprise (DBE) program. A year later, this same document was presented to Congress and entered into the Congressional record.[2]

Since *Adarand*, a number of federal courts have cited that document when holding that Congress had a compelling interest justifying its race-conscious procurement programs.[3]

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[1] *The Compelling Interest for Affirmative Action in Federal Procurement: A Preliminary Survey*, 61 Fed. Reg. 26,050 (May 23, 1996). This report summarized more than 50 documents and 30 congressional hearings between 1980 and 1996.

[2] *Unconstitutional Set-Asides: ISTEA's Race-Based Set-Asides After* Adarand*: Hearing Before the Subcomm. on the Constitution, Federalism, and Property Rights of the S. Comm. on the Judiciary*, 105th Cong. 27-80 (1997). See also 144 Cong. Rec. S1493 (daily ed. Mar. 6, 1998) (statement of Sen. Lieberman).

[3] *Western States Paving Co.* v. *Washington State Dep't of Transp.*, 407 F.3d 983, 991-993 (9th Cir. 2005) (quoting *Adarand III*, 515 U.S. at 223); *Adarand Constructors, Inc.* v. *Slater* (*Adarand VII*), 228 F.3d 1147, 1167-1176 (10th Cir. 2000), cert. dismissed, 534 U.S. 103 (2001); *id.* at 1176 ("[W]e conclude that the evidence cited by the government and its amici, particularly that contained in *The Compelling Interest*, 61 Fed. Reg. 26,050, more than satisfies the

(continued...)

Specifically, these courts recognized that the vast body of evidence before Congress, much of which was summarized in the Department of Justice's 1996 memorandum, provided a "strong basis in evidence for [Congress's] conclusion that [race-conscious] remedial action was necessary."[4]

Since 1996, a significant body of new data has been generated that bears directly on the inquiry of whether race- and gender-conscious[5] procurement and business development programs remain necessary. This includes: Congressional hearings and reports that address the barriers faced by minority- and women-owned businesses; government-produced and government-sponsored reports on the characteristics and dynamics of minority- and women-owned small businesses; academic literature by social scientists, economists, and other academic researchers that focuses on the manner in which various forms of discrimination act together to restrict business opportunities for minorities and women; and disparity studies commissioned by state and local governments to determine whether there is evidence of racial discrimination in their contracting markets. Much of this evidence is already before Congress; additional evidence is discussed in this statement and submitted along with it.[6]

(...continued)
government's burden of production regarding the compelling interest for a race-conscious remedy."); see also *Sherbrooke Turf, Inc.* v. *Minnesota Dep't of Transp.*, 345 F.3d 964, 970 (8th Cir. 2003). In 2008, the Court of Appeals for the Federal Circuit invalidated the contracting program authorized under 10 U.S.C. § 2323, holding that the evidence before Congress was not sufficiently current to provide the compelling interest necessary to support the program. *Rothe Dev. Corp. v. U.S. Dep't of Def.*, 545 F.3d 1023 (Fed. Cir. 2008). This memorandum responds to that decision, demonstrating that Congress does currently have ample evidence to demonstrate that race-conscious contracting programs are narrowly tailored to serve a compelling government interest and that gender-conscious programs are substantially related to an important governmental objective.

[4] *Adarand VII*, 228 F.3d at 1174-1175 (holding that "the government has met its initial burden of presenting a 'strong basis in evidence' sufficient to support its articulated, constitutionally valid, compelling interest"); see also *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 204 (2009) (Opening Statement of the Hon. James L. Oberstar, Chairman and Rep. from Minnesota) ("Since *Adarand*, every federal court that has reviewed the DOT's DBE program has found it to be constitutional.").

[5] Although gender-conscious remedial programs were not the focus of the 1996 memorandum, which addressed the impact of the *Adarand III* decision and therefore dealt with the race-conscious provisions at issue in that decision, the present memorandum addresses both kinds of programs. See 15 U.S.C. 637(m)(2) (giving agencies the authority to "restrict competition for any contract for the procurement of goods or services by the Federal Government to benefit small business concerns owned and controlled by women" under certain circumstances).

[6] Between 2006 and the end of 2009, Congress conducted thirty-six separate hearings concerning public procurement and minority- and women-owned business enterprises. See
(continued...)

This memorandum summarizes a sample of the extensive body of evidence generated since 1996 and builds on the evidence already before Congress at that time. That evidence clearly shows that discriminatory barriers continue to impede the ability of minority- and women-owned businesses to compete with other firms on a fair and equal footing in government contracting markets. Indeed, significant discrimination, in arenas such as access to capital and employment, limits the formation of these businesses in the first instance.[7]

As in 1996, these barriers "are real and concrete, and reflect ongoing patterns and practices of exclusion, as well as the tangible, lingering effects of prior discriminatory conduct."[8] The evidence discussed below confirms that many of the barriers identified more than a decade ago remain just as significant today. The government has a compelling interest in race- and gender-conscious federal procurement programs where necessary to ensure that it does not "perpetuat[e] the effects of racial discrimination in its own distribution of federal funds" and thereby become a "'passive participant' in a system" of racial or gender exclusion.[9] *Adarand Constrs, Inc.* v. *Slater*, 228 F.3d 1147 (10th Cir. 2000).

II.

Discriminatory Barriers to Contracting Opportunities for Minority- and Women-Owned Businesses

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(...continued)
Appendix A for a list of Congressional hearings addressing this subject. Appendix B contains a list of academic studies and reports cited herein. Appendix C contains a list of recent disparity studies conducted by state and local governments.

[7] For these reasons, some metrics that have been used to measure discrimination in government procurement programs – such as bidders' lists or lists of registered contractors – likely understate the true continuing effects of discrimination.

[8] 61 Fed. Reg. at 26,051.

[9] The Supreme Court has recognized and approved the government's compelling interest in avoiding becoming a "passive participant" in marketplace discrimination. As the Supreme Court stated in *City of Richmond* v. *Croson Co.*, 488 U.S. 469, 492 (1989), for example:

> [I]f the city could show that it had essentially become a "passive participant" in a system of racial exclusion practiced by elements of the local construction industry, we think it clear that the city could take affirmative steps to dismantle such a system. It is beyond dispute that any public entity, state or federal, has a compelling interest in assuring that public dollars, drawn from the tax contributions of all citizens, do not serve to finance the evil of private prejudice.

Difficulties exist for any person interested in developing and sustaining a business that can compete for government contracts. First, a would-be business owner generally needs both experience and financial resources to create a viable enterprise. The practical experience needed to succeed in the government contracting market is often gained through prior employment in the targeted field, an informal apprenticeship in a family-run business, or membership in a professional trade union. The needed financial resources may come from personal wealth, commercial business loans, venture capital, or personal loans. And once a business is formed, access to working capital remains critical to both sustain and grow the business. Equally important is access to fair contracting opportunities, which means fair treatment by prime contractors and private sector customers, business networks, financial institutions, suppliers and bonding providers.

These are significant barriers, and they pose potential barriers to business formation and success for all businesses, regardless of the race or gender of their owners. But the evidence sampled in this memorandum shows that these barriers are substantially more difficult for businesses owned by minorities and women to overcome because of the widespread and systematic impact of race and gender discrimination that still exists in the economy generally and in the government contracting market specifically. The evidence shows that these barriers – whether the result of intentional discrimination or other activity that nonetheless perpetuates discrimination — often: (1) prevent minorities and women from forming businesses by denying them needed access to both experience and capital;[10] and (2) deprive minority- and women-owned businesses of fair access to contracting opportunities because of ongoing discrimination by prime contractors, business networks, financial institutions, suppliers, and bonding providers.

These types of disadvantages are in many ways precisely what the federal programs — like the U.S. Small Business Administration's 8(a) and Women Owned Small Business programs and the Department of Transportation's Disadvantaged Business Enterprise program — are designed to address. Each of these programs is designed to eliminate discriminatory barriers and help the development of small disadvantaged firms to enable them to gain a foothold in federal procurement contracting. In this way, the firms first gain access to relatively small contracting opportunities, which can then lead to success in larger federal contracts and the economy as a whole.

A. *Statistical Evidence Demonstrates the Existence of Discrimination.*

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[10] *Business Start-Up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 1 (2008) (statement of the Hon. John F. Kerry, Chairman and Sen. from Massachusetts) (explaining that the disparity between minority- and women-owned businesses on the one hand, and non-minority-owned businesses on the other, is "not due to any lack of motivation or determination on behalf of minorities and women," but is instead "due to the tremendous hurdles women and minorities must face each day to gain fair and adequate access to venture capital, credit and business and technical training").

1. *There Are General Disparities Between Minority- And Women-Owned Businesses Relative To Their Non-Minority, Male-Owned Counterparts.*

A primary objective of programs that consider race or gender as a factor in government contracting is to encourage and support the formation and development of minority- and women-owned businesses. This effort is a means to help remedy the effects of discrimination that have inhibited such business formation and success.[11] The most recent government statistics on minority- and women-owned businesses illustrate the disproportionately small share of the market these businesses currently occupy. For example, using data from the *2002 Survey of Business Owners*,[12] the U.S. Small Business Administration's Office of Advocacy prepared a report in 2007 entitled *Minorities in Business: A Demographic Review of Minority Business Ownership*.[13] The report analyzed information on minorities in the work force and minority-owned businesses, including statistics about the minority population, their labor force participation, age, education, occupation, work schedules, average personal and household income, business ownership, and business dynamics. The report focused on the growth of minority-owned businesses over recent years in relation to the growth of the minority populations in America during the same time period. Additionally, it analyzed revenue created by minority businesses in comparison to that created by non-minority-owned businesses. The report showed:

- Minorities (defined in the study as either Hispanic, Black, American Indian or Alaska Native, Asian, Native Hawaiian or other Pacific Islander) made up roughly 32% of the population, but owned only approximately 18% of firms.[14]

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[11] *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 2 (2007) (statement of the Hon. John F. Kerry, Chairman and Sen. from Massachusetts) ("These programs to help minority and disadvantaged firms access Federal contracts are needed to help these firms break into the Federal market."); see also *id.* at 1-2 ("[W]hile the numbers of minority-owned businesses hold promise for the future, and obviously that growth is important, it is clear that much more needs to be done to encourage and strengthen the minority business community and to guarantee the opportunities within it. The potential for small business growth and entrepreneurship has simply not been fully tapped and barriers continue to exist for many minority business owners.").

[12] Census Bureau, *2002 Survey of Business Owners, Advance Report on Characteristics of Employer Business Owners: 2002*, available at http://www.census.gov/econ/census02/sbo/intro.htm (last visited April 29, 2010). This survey provides economic and demographic characteristics for the owners of businesses with paid employees operating in the United States and is the first survey requesting information about business owners since the 1992 Characteristics of Business Owners (CBO) survey.

[13] Ying Lowrey, *Minorities in Business: A Demographic Review of Minority Business Ownership*, 298 U.S. Small Business Administration (2007).

[14] *Id.* at 1, 3.

- Blacks constituted 11.8% of the total U.S. population, but owned only 5.0% of all firms, and accounted for less than 1% of total receipts.[15]

- Hispanics constituted 13.5% of the total population, but owned only 6.55% of all firms, and accounted for only 2.48% of total receipts.[16]

- More than half of Black-owned businesses had less than $10,000 in business receipts in 2002, compared with one-third of White-owned firms.[17]

- On average, a non-minority-owned employer firm (*i.e.*, a firm with one or more employees) had more than $1.6 million, while a Black-owned employer firm had just $696,158 in sales.[18]

- On average, for every dollar that a White-owned firm made, Pacific Islander-owned firms made about 59 cents, Hispanic-, Native American-, and Asian-owned businesses made about 56 cents, and Black-owned businesses made 43 cents.[19]

- Minority women owned 29% of Black employer firms and 47% of Black non-employer firms; non-minority women owned 17% of White employer firms and 31% of White non-employer firms.[20]

A 2006 report produced by the Minority Business Development Agency also finds that, while minority-owned businesses grew in number at a fast pace between 1997 and 2002, their growth in gross receipts and paid employment lagged behind the growth in number of firms.[21] In fact, the report finds that the gap between the share of gross receipts generated by minority businesses and the share of the minority population slightly widened during that period.[22] This disparity "underscores the opportunity gap that still exists in the U.S. economy."[23]

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[15] *Id.* at 1.

[16] *Ibid.* Similarly, while Asian-owned firms accounted for 4.8% of all nonfarm businesses in the United States, these firms accounted for only 2.0% of nonfarm business employment and a scant 1.4% of their receipts. Census Bureau, *Survey of Business Owners – Asian-Owned Firms: 2002: Summary of Findings*, available at http://www.census.gov/econ/sbo/02/asiansof_all.html (last visited April 29, 2010).

[17] Ying Lowrey, *Minorities in Business: A Demographic Review of Minority Business Ownership*, 298 U.S. Small Business Administration 8 (2007).

[18] *Id.* at 7.

[19] *Id.* at 2.

[20] *Id.* at 4.

[21] U.S. Department of Commerce, Minority Business Development Agency, *The State of Minority Business Enterprises, An Overview of the 2002 Survey of Business Owners* (2006).

[22] *Id.* at 12.

[23] *The Minority Business Development Agency: Enhancing the Prospects for Success:*

(continued...)

Additional data from the Census Bureau's *2002 Survey of Business Owners* show that women-owned businesses account for just a fraction of the receipts of all non-farm businesses in the United States. For example, in 2002, there were 6.5 million women-owned firms in the United States, which accounted for 28.2% of all non-farm business in the United States but just 4.2% of their receipts.[24] Only 1.8% of women-owned firms had receipts of more than $1 million, and less than 0.1% had more than 500 employees.[25]

Government reports also show that minority-owned firms experience a higher failure rate than that of non-minority owned firms. For example, data based on the 1997 Survey of Minority-Owned Business Enterprises (SMOBE) show that, between 1997 and 2001, the survival rate for non-minority-owned employer establishments was 72.6%.[26] The survival rate of all minority-owned employer establishments was about 4 percentage points lower.[27] The survival rates for specific minority-owned employer establishments were as follows:

- Asian and Pacific Islander-owned employer establishments: 72.1%.[28]

(...continued)
Hearing Before the H. Subcomm. on Commerce, Trade, and Consumer Protection of the H. Comm. on Energy and Commerce, 111th Cong. (2009) (statement of David A. Hinson, National Director, Minority Business Development Agency) (testifying on the disparities between the minority population and the gross receipts generated by minority-owned businesses).

[24] Census Bureau, *Survey of Business Owners - Women-Owned Firms: 2002*, available at http://www.census.gov/econ/sbo/02/womensof.html (last visited April 29, 2010).

[25] Elaine Reardon, Nancy Nicosia and Nancy Y. Moore, *The Utilization of Women-Owned Small Businesses in Federal Contracting*, Kauffman-RAND Institute for Entrepreneurship Public Policy 14, 17 (2007). A report issued by the House Small Business Committee Democratic Staff shows that the federal government's failure to meet its own procurement goals of 5% contracting to women-owned businesses represented a cost of *$6 billion* in lost contracting opportunities for women-owned businesses in FY 2003. House Small Business Committee Democratic Staff, *Scorecard V: Dramatic Gains in the Federal Marketplace Fail to Result in Small Business Contracts* (2004) (noting that only 2.89% of contracts awarded throughout the entire federal government in FY 2003 went to women-owned businesses). For FY 2004, the estimated loss was *$5.5 billion*. *Id.* at 12. Contracts awarded to women-owned small businesses throughout the entire federal government in FY 2004 amounted to 3.03%; by 2008, that amount had increased very little, to 3.39%. Small Business Administration, *FY 2004 Official Goaling Report*; Small Business Administration, *Fiscal Year 2004: Small Business Prime Contract Goaling Achievements* (both documents available at http://www.sba.gov/aboutsba/sbaprograms/goals/index.html (last visited April 29, 2010)).

[26] Ying Lowrey, *Dynamics of Minority-Owned Employer Establishments, 1997-2001*, 251 U.S. Small Business Administration 10 (2005).

[27] *Ibid.*

[28] *Ibid.* Note, however, that Asian-American firms exhibited a slightly higher rate of contraction than non-minority owned firms (23% in comparison to 21%). *Ibid.* Also, a study of
(continued...)

- Hispanic-owned employer establishments: 68.6%.[29]
- American-Indian and Alaska Native-owned employer establishments: 67.0%.[30]
- African-American-owned employer establishments: 61.0%.[31]

Black-owned employer establishments also had the lowest expansion rate (26%) of all minority business groups.[32] Moreover, Black-owned firms and, to a lesser extent, Latino-owned firms, had lower sales, hired fewer employees, and had smaller payrolls than White- owned firms.[33]

A number of Congressional hearings have addressed disparities in business formation and success between minority-and women-owned businesses, on the one hand, and businesses owned by their non-minority, male counterparts,[34] on the other, as well as the specific barriers that minority- and women-owned businesses continue to face.[35] The evidence presented at these

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(...continued)
the survival rate of Asian American firms in SBA's 8(a) program has shown that it is not statistically different from the business survival rates of other MBEs in the program. See Asian American Justice Center, *Equal Access: Unlocking Government Doors for Asian Americans: Public Contracting Laws and Policies* 28 (2008).

[29] Ying Lowrey, *Dynamics of Minority-Owned Employer Establishments, 1997-2001*, 251 U.S. Small Business Administration 10 (2005).

[30] *Ibid.*

[31] *Ibid.*

[32] *Id.* at 20.

[33] Robert W. Fairlie, *Minority Entrepreneurship*, The Small Business Economy, produced under contract with the SBA, Office of Advocacy 74 (2005).

[34] See, *e.g.*, *Opportunities and Challenges for Women Entrepreneurs: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 3 (2008) (statement of the Hon. John F. Kerry, Chairman and Sen. from Massachusetts) (finding generally that "women-owned businesses still lag behind their male counterparts in important areas," and finding specifically that "[w]omen-owned firms have lower revenues and fewer employees than their male-owned counterparts"); *Expanding Opportunities for Women Entrepreneurs: The Future of Women's Small Business Programs: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 2 (2007) (statement of the Hon. John F. Kerry, Chairman and Sen. from Massachusetts) (stating that "women owned small businesses still continue to have markedly lower revenue and fewer employees than firms, even comparable ones, owned by men"); *Access to Federal Contracts: How to Level the Playing Field: Field Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 4-8 (2007) (statement of the Hon. Benjamin L. Cardin, Sen. from Maryland).

[35] See, *e.g.*, *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs*

(continued...)

hearings shows that the disparities between the minority share of the business population and its share of business sales and receipts "are adverse, very large, and statistically significant."[36] Moreover, these disparities have been observed in all 50 states and the District of Columbia for all minority groups and for women.[37]

These studies and data of course provide a snapshot of firms at a particular period of time. But the data show that minority-and women-owned firms continue to have only limited success both in the larger economy and in the federal procurement market.

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for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship, 110th Cong. (2007); *Access to Federal Contracts: How to Level the Playing Field: Field Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. (2007); *Expanding Opportunities for Women Entrepreneurs: The Future of Women's Small Business Programs: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. (2007); *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. (2008); *Business Start-Up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training: Hearing Before the H. Subcomm. on Economic Development, Public Buildings, and Emergency Management Staff of the H. Comm. on Transp. and Infrastructure*, 110th Cong. (2008); *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. (2009).

[36] *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 19 (2008) (statement of Jon Wainwright, Vice President, NERA Economic Consulting); see also *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 26-34 (2007) (statement of Jon Wainwright, Vice President, NERA Economic Consulting).

[37] *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 25 (2008) (statement of Jon Wainwright, Vice President, NERA Economic Consulting); see also *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 328 (2009) (statement of Jon Wainwright, Vice President, NERA Economic Consulting) (testifying that minority- and women-owned construction and construction-related professional service businesses earned on "average almost 25 percent lower than their non-minority male counterparts, again even when other attributes are held constant," and that the disparities are even larger for African American-, Native American-, and non-minority women-owned businesses).

2. *Discrimination Is A Basis For Identified Disparities Between Minority- And Women-Owned Businesses And Their Non-Minority, Male-Owned Counterparts.*

The findings outlined above are mirrored by the numerous studies commissioned by state and local governments that have identified stark and continuing disparities between the availability of minority- and women-owned businesses and the utilization of such businesses in state and local government procurement. The Supreme Court has held that such significant disparities can support an inference of "discriminatory exclusion."[38]

A list of approximately 70 recently conducted disparity studies is attached.[39] The studies show that "minority-owned businesses and women-owned businesses throughout the nation continue to face large disparities in almost every aspect of business enterprise activity that can be quantified"[40] in a pattern of discriminatory barriers that is repeated across the nation. Moreover, the findings confirm that the disparities "are symptoms of discrimination in the labor force that, in addition to its direct effect on workers, reduce[s] the future availability of [minority- and women-owned businesses] by stifling opportunities for minorities and women to progress through precisely those internal labor markets and occupational hierarchies that are most likely to lead to entrepreneurial opportunities."[41] The disparities identified in these state and local government studies "demonstrate the nexus between discrimination in the job market and reduced entrepreneurial opportunities for minorities and women."[42] Past hearings have identified similar disparities that exist in the federal contracting market.[43]

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[38] *Croson*, 488 U.S. at 509.

[39] See Appendix C for a complete listing of these studies. The studies document evidence from 25 states and the District of Columbia, including: Alaska, Arizona, California, Colorado, Connecticut, Florida, Georgia, Idaho, Illinois, Kansas, Maryland, Massachusetts, Minnesota, Missouri, Nevada, New Jersey, New York, North Carolina, Ohio, Oregon, Pennsylvania, Tennessee, Texas, Virginia, Washington, and suburban Washington, D.C. Eighteen of these studies focus on disparities state-wide: Alaska, Arizona, California, Colorado, Idaho, Illinois, Kansas, Kentucky, Maryland, Minnesota, Missouri, Montana, Nevada, New Jersey, North Carolina, Oregon, Pennsylvania, and Virginia. See, *e.g.*, *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. (2009) (citing more than 20 disparity and utilization studies throughout); *Business Start-Up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. (2008) (citing more than 12 different studies throughout).

[40] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 326 (2009) (statement of Jon Wainwright, Vice President, NERA Economic Consulting).

[41] National Economic Research Associates, Inc., *Race, Sex and Business Enterprise: Evidence from Memphis, Tennessee* 100 (2008).

[42] *Ibid.*

[43] *Expanding Opportunities for Women Entrepreneurs: The Future of Women's Small*

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Academic research using a variety of publicly available statistical data confirms that these disparities remain large and statistically significant even when minority- and women-owned businesses are compared with otherwise similar (with respect to characteristics such as industry, geography, etc.) male- and nonminority-owned firms.[44] In reaching these conclusions, researchers controlled for factors such as industry, geography, education, age, and labor market status — even though minority- and women-owned businesses face demonstrable barriers to achieving parity in these areas — thus demonstrating that the remaining disparities likely result in large part from discrimination. Recent independent research has also concluded that the gap that exists between minority business owners and their non-minority counterparts "has not in any way been caused by a lack of effort on the part of minority entrepreneurs," but rather results in part because "discriminatory conditions that previously existed were deep and pervasive and have not been fully reversed."[45] In addition, some disparities are likely to be greater than data

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Business Programs: Hearing Before the S. Comm. on Small Business and Entrepreneurship, 110th Cong. 2 (2007) (statement of the Hon. John F. Kerry, Chairman and Sen. from Massachusetts) (stating that firms owned by women "account for less than 3 percent of all Federal contracts even though they comprise 30 percent of all privately-held firms," and describing this as "an unacceptable ratio"); *Full Comm. Hearing to Consider Legislation Updating and Improving the SBA's Contracting Programs Before the H. Comm. on Small Business*, 110th Cong. 3 (2007) (statement of the Hon. Steve Chabot, Ranking Member and Rep. from Ohio) ("Despite the extra assistance from the SBA, small businesses owned by socially and economically disadvantaged individuals [and] women * * * do not receive their fair proportion of contracts to sell goods and services to the federal government."); *Federal Contracting: Removing Hurdles for Minority-Owned Small Businesses: Hearing Before the Subcomm. on Government Management, Organization, and Procurement of the House Comm. on Oversight and Government Reform*, 110th Cong. 3 (2007) (statement of the Hon. Edolphus Towns, Chairman and Rep. from New York) ("Although procurement provides the federal government with a potentially powerful tool for promoting minority opportunities and counteracting discrimination, there continues to be disparity in the allocation of government contracts to minority firms.").

[44] Congress heard the results of academic studies that were based on data taken from the 2002 Survey of Business Owners (SBO) and the Public Use Microdata Sample (PUMS), which are both produced by the Census Bureau; the Current Population Surveys (CPS), which is produced jointly by the Census Bureau and the Bureau of Labor Statistics; and the Survey of Small Business Finances (SSBF), which is produced by the Federal Reserve Board and the SBA. See *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 30-34 (2007) (statement of Jon Wainwright, Vice President, NERA Economic Consulting); see also *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 328 (2009) (statement of Jon Wainwright, Vice President of NERA Economic Consulting).

[45] Boston Consulting Group, *The New Agenda for Minority Business Development* 14

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show; because the age and size of minority- and women-owned businesses may themselves have been limited by discrimination, current statistics likely understate the number and size of minority- and women-owned firms that might exist once the effects of discrimination no longer stifle their creation and expansion.[46]

Qualitative evidence from minority and women business owners gathered from surveys, interviews, and presented via Congressional testimony overwhelmingly support these findings.[47] For example, minorities and women business owners often report that they "encounter significant barriers to doing business in the public and private sector market[s], as both prime contractors and subcontractors," that are greater than those faced by their non-minority and non-female counterparts.[48] Minorities and women report that they "often suffer from stereotypes about their suspected lack of competence and are subject to higher performance standards than similar White men," and that they "encounter discrimination in obtaining loans and surety bonds; receiving price quotes from suppliers; working with trade unions; obtaining public and private sector prime contracts and subcontracts, and being paid promptly."[49] Indeed, Congress has repeatedly recognized that there is overwhelming evidence that shows that "considerable

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[46] *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 66-67 & n.2 (2008) (Statement of Anthony W. Robinson, President, Minority Business Enterprise Legal Defense Fund). Congress also heard testimony that discriminatory barriers impede the ability to measure the actual business capacity of MBEs because "[m]any, if not all, 'capacity' indicators are themselves impacted by discrimination. Therefore, it is not good social science to limit availability measures by factors such as firm age, revenues, or numbers of employees." *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 375 (2009) (statement of Jon Wainwright, Vice President, NERA Economic Consulting) "[F]ocusing on the 'capacity' of businesses in terms of employment, revenue, bonding limits, number of trucks, and so forth is simply wrong as a matter of economics because it can obscure the existence of discrimination. A truly 'effective' discriminatory system would lead to a finding of no 'capacity,' and under the 'capacity' approach, a finding of no discrimination." *Id.* at 376; see also *id.* at 10, 325 (*Rothe* court "made several serious errors in its economic reasoning, concluding, for example that factors such as firm size should be factored into study estimates of DBE availability"), 371 (proper statistical analysis "should not control for the variables affected by the behavior sought to be isolated").

[47] See, *e.g.*, *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 33-34 (2007) (statement of Jon Wainwright, Vice President, NERA Economic Consulting).

[48] *Ibid.*

[49] *Ibid.*

discrimination" exists throughout the federal contracting market that affects small minority- and women-owned businesses across the racial and ethnic spectrum.[50]

B. *Discrimination Affects the Formation and Development of Minority-And Women-Owned Businesses.*

The 1996 report prepared by the Department of Justice identified discrimination in two sectors of the national economy that accounted, at least in part, for diminished opportunities for minorities to form their own businesses: (1) discrimination by employers, which prevented minorities from acquiring necessary technical skills; and (2) discrimination by lenders, which prevented minorities from accessing much-needed capital to develop and sustain a business.[51] Discrimination in these same sectors of the economy persists and remains a significant barrier to the formation of viable businesses by minorities and women.

1. *Discrimination by Employers Results in a Lack of Human Capital.*

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[50] *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 1-2 (2008) (statement of the Hon. William Lacy Clay, Chairman and Rep. from Missouri) ("There has been a large body of evidence concerning discrimination. Court cases, legislative hearings, quantitative studies and anecdotal reports detail the considerable discrimination based on race and national origin that confronts minority contractors in all parts of the country and in virtually every industry. The discrimination is not limited to one particular minority group, instead, evidence shows businesses owned by African-Americans, Latinos, Asians, Pacific Islanders and Native Americans all must overcome discriminatory practices in order to grow and prosper."); see also *Opportunities and Challenges for Women Entrepreneurs: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 3 (2008) (statement of the Hon. John F. Kerry, Chairman and Sen. from Massachusetts) ("In reviewing the last 20 years, it is disturbing to see that the issues that were hindering women entrepreneurs from achieving their full potential 20 years ago are still barriers today."); see also *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 204-205 (2009) (statement of the Hon. James L. Oberstar, Chairman and Rep. from Minnesota) ("The Committee has also received volumes of evidence, both empirical and anecdotal, about the discrimination that continues to impact minority and women business owners across this nation. This data demonstrates that it is difficult for small and disadvantaged businesses to compete — discrimination impacts minority and women owned businesses at many points in the contracting process, including obtaining credit, bonding, and insurance."); *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 309 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT) (noting that states and localities had reported to DOT that discrimination against women and minorities persists).

[51] *The Compelling Interest for Affirmative Action in Federal Procurement: A Preliminary Survey*, 61 Fed. Reg. 26,050 (May 23, 1996).

Discrimination in the workplace may take many forms. It can be intentional and overt, as when employers purposefully treat employees and would-be employees differently based on their race or gender[52] or when others in the business community explicitly state their preference *not* to work with minorities and women.[53] It can involve explicit harassment by employers or co-workers that gives rise to a hostile work environment[54] or can take a more subtle, yet no less

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[52] See, *e.g.*, *EEOC* v. *Area Erectors, Inc.*, No. 1:07-cv-02339 (N.D. Ill. May 27, 2009) (construction company settling lawsuit for $630,000 where group of African-American employees were terminated because of their race); *EEOC* v. *Marjam Supply Co.*, No. 7:03-cv-5413 (S.D.N.Y. April 14, 2009) (building materials supplier settling lawsuit for $495,000 where African-American employees were subjected to differential discipline and termination); *EEOC* v. *Michigan Seamless Tube*, No. 2:05-cv-73719 (E.D. Mich. June 5, 2007) (steel tubing company settling lawsuit for $500,000 after refusing to hire a group of African Americans who were former employees of its predecessor company); *EEOC* v. *S & Z Tool & Die Co.*, No. 1:03-cv-2023 (N.D. Ohio Aug. 16, 2006) (metal manufacturing firm settling lawsuit for $850,000 where it refused to hire women and African-American applicants because of their gender and race, respectively); *EEOC* v. *Optical Cable Corp.*, No. 7:00-cv-00757 (W.D. Va. Feb. 20, 2002) (fiber-optic cable manufacturer settling lawsuit for $1 million after failing to hire African-American applicants for a ten year period, and assigning women to lower-paying positions than their similarly situated male counterparts); *EEOC* v. *Landis Plastics, Inc.*, No. 5:00-cv-01874 (N.D.N.Y. Dec. 8, 2000) (settling lawsuit for $782,000 after discriminating against women on the basis of gender in the assignment of jobs and in promotions).

[53] See, *e.g.*, *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 39 (2007) (statement of Anthony W. Robinson, President, Minority Business Enterprise Legal Defense and Educational Fund) (relating experience of an African-American business owner who was told by a potential business partner that he "[doesn't] like doing business with you people"); see also *Women in Business: Leveling the Playing Field: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 42 (2008) (statement of Kerstin Forrester, President, Stonebridge Precision Machining & Certified Welding) (testifying that when she first purchased her business, two former customers told her "outright that they would not do business with a woman," and that one engineer told her that "machining was nothing that a woman could understand").

[54] See, *e.g.*, *EEOC* v. *Brand Energy Solutions, LLC*, No. 2:08-cv-00305 (S.D. Tex. May 30, 2009) (construction contractor settling sexual harassment and retaliation lawsuit for $175,000 where female employee was forced to quit her job when company failed to take appropriate remedial action after she was subjected to repeated unwelcome physical contact, sexual advances and comments, and threatening behavior); *EEOC* v. *Ceisel Masonry, Inc.*, No. 06-cv-2075 (N.D. Ill. May 22, 2009) (construction company settling lawsuit for $500,000 where Hispanic employees were called racially derogatory terms by their supervisors and routinely exposed to racist graffiti); *EEOC* v. *Talbert Building Supply, Inc.*, No. 1:08-cv-00707 (M.D.N.C. May 26, 2009) (North Carolina lumber and hardware retailer settling race discrimination lawsuit for $80,000 where employee was subjected to explicit racial slurs as well as racial jokes and

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damaging, form.[55] It can result from practices that, although facially neutral, unjustifiably and disproportionately exclude groups of employees or applicants based on their race, national origin or sex.[56] Regardless of the form, race and gender discrimination in the workplace have a devastating effect on the ability of minorities and women to develop and sustain their own businesses. In particular, they result in a marked decrease in human capital — the experience necessary to create a viable new business in today's markets.

This historical discrimination in employment limited — and continues to limit — the advancement of minorities and women to higher level positions in the workforce, and thus their opportunity to gain the skills, experience, and business contacts necessary to develop a successful business model. Among other things, historical discrimination prevented many

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derogatory stereotypes about African Americans on an almost daily basis for two years); *EEOC* v. *Wheeler Construction, Inc.*, No. 2:07-cv-01829 (D. Ariz. March 5, 2009) (construction company settling lawsuit for $325,000 where Mexican employees were harassed based on their national origin).

[55] See, *e.g.*, CRA International for the San Mateo County Transit District and thePeninsula Corridor Joint Powers Board, *Measuring Minority- and Women-Owned Construction and Professional Service Firm Availability and Utilization* 95 (2008) (discussing study in which researchers sent fictitious resumes that included randomly assigned "white- and black-sounding" names to help-wanted ads in Boston and Chicago, and finding that resumes with "white-sounding" names received 50% more callbacks for interviews than did the resumes with "black-sounding" names); see also *Section 15: Race and Color Discrimination*, EEOC Compliance Manual, § 15-I (2006), available at http://www.eeoc.gov/policy/docs/race-color.html (last visited April 29, 2010) (citing a 2003 study in Milwaukee finding that Whites with a criminal record received job call-backs at a rate more than three times that of Blacks with the same criminal record, and even at a rate higher than Blacks *without* a criminal record; a 2003 study in California finding that temporary agencies preferred White applicants three to one over African American applicants; and a 2002 study in Boston and Chicago finding that résumés of persons with names common among Whites were 50 percent more likely to generate a request for an interview than equally impressive résumés of persons with names common among Blacks); cf. *Women in Business: Leveling the Playing Field: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 44 (2008) (statement of Sharon Green, President, Custom Copper and Slate, Ltd.) (testifying to her experience that decision making officials prefer talking to a man, not a woman, regarding construction projects).

[56] 42 U.S.C. Sec. 2000e-2(k)(1)(A) (prohibiting employment practices that have a disparate impact on the basis of race, color, religion, sex or national origin); see, *e.g.*, *Griggs* v. *Duke Power Co.*, 401 U.S. 432 (1971) (recognizing that "good intent or absence of discriminatory intent does not redeem employment procedures or testing mechanisms that operate as 'built-in headwinds' for minority groups and are unrelated to measuring job capability"); *EEOC* v. *Dial Corp.*, 469 F.3d 735, 742-743 (8th Cir. 2006) (upholding district court's finding that a physical strength test had an unlawful disparate impact on female employees).

minorities and women from forming businesses and passing them on to their children; as a result, many would-be minority and female business owners of today never had the opportunity to work in a family-run business and thus gain skills to develop a successful business in today's markets.[57] Indeed, minority business owners state that they face an initial barrier stemming from a lack of familiarity about running a business.[58]

Academic research confirms that the lingering effects of discrimination can extend across generational lines. For example, one researcher found that black business owners face three different hurdles in comparison to their white counterparts: they are less likely to inherit businesses, and thus need to raise their own capital to start a business; they are less likely to be employed by family members who own small businesses, thus missing out on gaining first-hand business experience; and they are less likely to have family members who own small businesses, thus lacking ready access to business mentors.[59] Thus, not only are minorities statistically less likely to start a business due to historical and current patterns of lower self-employment, they are also less likely to have had the opportunity to learn the skills necessary to run a successful business.[60] As one researcher concluded, "the lack of prior work experience in family businesses among future black business owners, perhaps by restricting their acquisition of general and specific business human capital, limits the successfulness of their businesses relative to whites."[61] Women business owners have also reported fewer opportunities to learn the skills necessary to run successful businesses.[62]

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[57] *Business Start-Up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 3 (2008) (statement of Margaret Henningsen, Vice President, Legacy Bank) (explaining that many would-be minority entrepreneurs are first generation entrepreneurs who "do not have the benefit of family members handing down a business or providing them with the necessary training and coaching that is so crucial for business success").

[58] *Access to Federal Contracts: How to Level the Playing Field: Field Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 71 (2007) (statement of Wayne Frazier, Sr., President, Maryland-Washington Minority Contractors Association) (testifying that the majority of minority business owners do not have family members who have owned a business, and therefore have little if any understanding of how to run a business).

[59] Robert W. Fairlie and Alicia M. Robb, *Why are Black-Owned Businesses Less Successful Than White-Owned Businesses? The Role of Families, Inheritances, and Business Human Capital*, 25 Journal of Labor Economics 289, 295 (2007) (Table 2).

[60] Michael Hout and Harvey S. Rosen, *Self-Employment, Family Background and Race*, 35 Journal of Human Resources 670-692 (2000).

[61] Robert W. Fairlie and Alicia M. Robb, *Why are Black-Owned Businesses Less Successful Than White-Owned Businesses? The Role of Families, Inheritances, and Business Human Capital*, 25 Journal of Labor Economics 289, 308 (2007).

[62] For example, one researcher testified before Congress that, based on a national study by the Center for Women's Business Research, women business owners of fast-growth companies reported that, unlike their male counterparts, role models and mentors "[weren't] really available to them." *Women in Business: Leveling the Playing Field: Roundtable Before*

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Current discrimination in hiring and promotions by employers can also severely limit the opportunities for minorities and women to build the human capital necessary for future business success. In 2008, women comprised 46.5% of the U.S. labor force, yet held only 15.2% of US Fortune 500 directorships.[63] In addition, although women account for 51% of all workers in high-paying management, professional, and related occupations, of the top ten occupations of women workers, senior manager and middle manager did not make the list.[64] At a recent workshop on transition points in women's careers (*e.g.*, moving into more senior levels and assuming leadership roles) held by the National Academies Committee on Women in Science, Engineering, and Medicine (CWSEM), several women's professional societies referred to surveys and studies in which women identified their work environments as hostile.[65] Such conditions act as a barrier to advancement – or even continued employment – within a company.

Thus, minorities and women often lack equal access to the two central means of gaining the experience needed to operate a business. A history of discrimination in employment opportunities provided significantly fewer opportunities for minorities and women to develop businesses to pass on to their children or to teach their children business-development skills.[66] And the continued discrimination by employers and would-be business partners against minorities and women severely limits their development of those skills and their entry into the

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the S. Comm. on Small Business and Entrepreneurship, 110th Cong. 8 (2008) (statement of Teri Cavanagh, Principal, Teri Cavanagh and Associates).

[63] Ernst & Young, *2008 Catalyst Census of Women Board Directors of the Fortune 500*, at 1. *Quick Stats on Women Workers, 2008,* United States Department of Labor, available at http://www.dol.gov/wb/stats/main.htm (last visited, April 29, 2010). See also Siri Terjesen, Ruth Sealy and Val Singh, *Women Directors on Corporate Boards,* 17 Corporate Governance: An International Review 325, 320-337 (2009). In addition, in 2008, only 15.7 % of corporate officers of Fortune 500 companies were women. Ernst & Young, *2008 Catalyst Census of Women Corporate Officers and Top Earners of the Fortune 500*, at 1. A study controlling for organization and director characteristics found that women directors are less likely than men to be on the executive committee and more likely to be on the public affairs committee. See Craig A. Peterson and James Philpot, *Women's Roles on U.S. Fortune 500 Boards: Director Expertise and Committee Memberships*, 72(2) Journal of Business Ethics 177, 179 (2007).

[64] *Quick Stats on Women Workers, 2008,* United States Department of Labor, available at http://www.dol.gov/wb/stats/main.htm (last visited, April 29, 2010).

[65] *Opportunities and Challenges for Women Entrepreneurs: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 56 (2008) (statement of Cat Shrier, Ph.D., P.G. Watercat Consulting LLC).

[66] Robert W. Fairlie, *Minority Entrepreneurship,* The Small Business Economy, produced under contract with the SBA, Office of Advocacy 97 (2005) (identifying one of the major barriers to minority-owned business as relatively disadvantaged family business backgrounds which "appear to limit entry and success in small business").

business markets today.[67]

2. *Discrimination Limits Access To Capital.*

Access to financial capital is absolutely essential for business formation and development.[68] However, lack of access to capital is the most frequently cited obstacle among minority and women business owners to developing and growing their businesses.[69] A critical question, then, is the extent to which their lack of equal access to capital, which can prevent minority- and women-owned businesses from forming, developing, and succeeding in today's markets, is a result of discrimination in lending practices.[70]

Numerous studies that address the question have reached the same conclusion: minority and women small business owners routinely face discrimination in the lending market. Relying on data from the *National Survey of Small Business Finances* (SSBF), Jon Wainwright, Vice President, NERA Economic Consulting, found that "African-American-owned firms, Hispanic-owned firms, and to a lesser extent other minority-owned firms are substantially and statistically significantly more likely to be denied credit than are White-owned firms," even when controlling for firm size and credit history.[71] Other researchers have made similar findings.[72] One study

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[67] See, *e.g.*, *supra* notes 59-62.

[68] See, *e.g.*, *Opportunities and Challenges for Women Entrepreneurs: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 110 (2008) (report by the National Association of Women Business Owners Procurement Task Force, submitted by Gayle Waldron, President & Owner, The Management Edge, asserts that "[a]ccess to capital has been, and remains, a critical issue for emerging and growing businesses, particularly those owned by women and minorities").

[69] *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 20 (2008) (statement of Jon Wainwright, Vice President, NERA Economic Consulting); see also Robert W. Fairlie, *Minority Entrepreneurship*, The Small Business Economy, produced under contract with the SBA, Office of Advocacy 97 (2005) (identifying one of the major barriers to minority-owned businesses as relatively low asset levels, which limit business entry and lead to higher rates of business closure, lower sales and profits, and less employment).

[70] *Business Start-Up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 3 (2008) (statement of Jon Wainwright, Vice President, NERA Economic Consulting).

[71] *Id.* at 4.

[72] See, *e.g.*, David G. Blanchflower, Phillip B. Levine, and David J. Zimmerman, *Discrimination in the Small-Business Credit Market*, 85(4) Review of Economics and Statistics 930, 942 (2003) (finding that "loan denial rates are significantly higher for black-owned firms that for white-owned firms even after taking into account differences in an extensive array of measures of creditworthiness and other characteristics"); Lloyd Blanchard, Bo Zhao, and John

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concluded that personal wealth plays an important role in predicting loan turndown rates, but that even *after* controlling for personal wealth, large differences in loan turndowns between African-American-, Hispanic-, and Asian-owned small businesses relative to those of whites remain.[73] Minority business owners who *do* receive loans often are required to pay higher interest rates on their loans than are charged to comparable white business owners.[74]

Indeed, the U.S. Small Business Administration recently concluded that the restrictions minorities face in gaining access to credit are "consistent with prejudicial discrimination against African-American and Hispanic firm owners."[75] The same has been found for women-owned firms.[76] Given their personal experience, or that of their colleagues, in being denied credit for

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Yinger, *Do Credit Market Barriers Exists for Minority and Women Entrepreneurs?* 14 Center for Policy Research, Maxwell School, Syracuse University, Working Paper No. 74 (2005) (finding that African-American- and Hispanic-owned firms face a higher probability of loan denial than that of white-owned firms even when controlling for a number of relevant variables); Myron Quon, *Discrimination Against Asian American Business Enterprises: The Continuing Need for Affirmative Action in Public Contracting*, Asian American Policy Review 41, 43, 46 (2008) (mentioning a study showing that Asian-American owned firms are denied loans at a rate 50% higher than white-owned companies and pay higher interest rates than comparable white-owned firms); Susan Coleman, *Access to Debt Capital for Women and Minority Owned Small Firms: Does Educational Attainment Have an Impact,* 9(2) Journal of Developmental Entrepreneurship 127, 132-133 (2004) (finding that firms owned by African-American, Hispanic, and Asian men were significantly more likely to be denied their most recent loan requests than white men); Jonathan Taylor, *Income and Wealth Transfer Effects of Discrimination in Small Business Lending*, 32(3/4) Review of Black Political Economy 87, 88-90 (2005) (finding evidence that African-American business owners face a higher probability of loan denial).

[73] Ken Cavalluzzo & John Wolken, *Small Business Loan Turndowns, Personal Wealth, and Discrimination*, 78(6) Journal of Business 2153, 2170 (2005).

[74] *Business Start-Up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 4 (2008) (statement of Jon Wainwright, Vice President, NERA Economic Consulting); see also *ibid.(*Testimony of Margaret Henningsen, Founder Legacy Bank)(discussing her bank's successful business serving minority entrepreneurs who had been denied loans by larger financial institutions); see also David G. Blanchflower, Phillip B. Levine, and David J. Zimmerman, *Discrimination in the Small-Business Credit Market*, 85(4) Review of Economics and Statistics 930, 941 (2003) ("Even among a sample of firms with no past credit problems, black-owned firms pay significantly higher interest rates.").

[75] Karlyn Mitchell & Douglas K. Pearce, *Availability of Financing to Small Firms Using the Survey of Small Business Finances*, 257 U.S. Small Business Administration 46 (2005).

[76] *Business Start-Up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 4 (2008) (statement of Jon Wainwright, Vice President, NERA Economic Consulting).

perceived discriminatory reasons, many minority and women business owners expect to be turned down and simply do not apply for financing.[77]

In addition to the academic and government-commissioned studies discussed above, numerous disparity studies conducted by state and local governments have also concluded that minorities and women face discrimination in the lending market. For example, one study found that African-American-, Hispanic-, and female-owned businesses reported loan denial rates of 47%, 39%, and 26%, respectively, in contrast to 21% for non-minority male-owned firms, even after controlling for creditworthiness and other related variables.[78] A disparity study conducted for San Mateo County, using data from the 1998 and 2003 Survey of Small Business Finances (SSBF), concluded that loan denial rates are much higher for similarly situated minority firms than for non-minority firms — both at the national level and for the Pacific region.[79] At the national level, African-American- and Hispanic-owned firms that did receive loans received much smaller amounts than non-minority-owned firms.[80] Moreover, the minority-owned firms receiving loans paid higher interest rates than did non-minority-owned firms.[81]

There is also evidence that minority- and women-owned businesses are less likely to secure outside investment revenue. The results from a 2001 study prepared for the U.S. Small Business Administration show that women-led firms received just 4.1% of all venture capital investments in 1998.[82] This suggests that women may be left behind in the asset creation process, limiting their opportunities to develop and grow their businesses. The study also states that "[m]inority women seeking capital may have greater barriers than white women or minority men."[83] One possible cause for the disparity between the access to outside capital of male-owned and female-owned firms is the "gender dominance" in the venture capital industry[84] and

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[77] *Opportunities and Challenges for Women Entrepreneurs: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 14 (2008) (statement of the Center for Women's Business Research). The Center concluded that the "expectation of being turned down is especially prevalent among women business owners of color." *Ibid.*; see also David G. Blanchflower, Phillip B. Levine, and David J. Zimmerman, *Discrimination in the Small-Business Credit Market*, 85(4) Review of Economics and Statistics 930, 942 (2003) (finding that concerns about being turned down due to prejudice or discrimination prevent more African-American-owned firms from applying for loans).

[78] Griffin & Strong, P.C., *City of Atlanta Disparity Study: Executive Summary* 7 (2006).

[79] CRA International, *Measuring Minority- and Women-Owned Construction and Professional Service Firm Availability and Utilization* 82 (2008).

[80] *Id.* at 85.

[81] *Ibid.*

[82] Candida G. Brush et al., *An Investigation of Women-Led Firms and Venture Capital Investment* 14 (2001).

[83] *Id.* at 16.

[84] *Women in Business: Leveling the Playing Field: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 10-11 (2008) (statement of Laila Partridge, CEO, Cover4me) (explaining that women are not well-represented in venture capital firms and

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the perception among many women and minorities that venture capitalists focus on pre-existing relationships or networks to which women and minorities do not have access.[85]

Without access to traditional sources of financing, minority- and women-owned businesses are often forced to forgo opportunities or rely on higher cost capital to support their businesses.[86] For example, a survey conducted by Women Impacting Public Policy showed that 66% of the respondents, women-owned businesses, relied on bank financing that was backed by home equity loans and 49% used credit card financing.[87] Another 36% received their funding from family and friends.[88] And while some business owners may be able to rely on personal wealth to fund and support their businesses, research shows that the lower median net worth of African-American households compared to white households (*e.g.*, $6,166 v. $67,000 in 2005, based largely on the net worth of homes owned by the households) translates into lower levels of start-up capital among African-American business owners than among white business owners.[89]

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therefore they lack an opportunity to develop relationships with firms looking to invest in small businesses); see *id.* at 10 ("Having spent 10 years in venture capital and working with larger firms, you * * * never see women in those firms."); see also *Expanding Opportunities for Women Entrepreneurs: The Future of Women's Small Business Programs: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 114 (2007) (statement of Ann Marie Ameida, President and CEO, Association of Women's Business Centers) (explaining that "the majority of venture capital deals are made through referrals via a fairly closed system of networks" to which women business owners do not have access).

[85] *Business Start-Up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 4 (2008) (statement of Donald T. Wilson, President and CEO, Association of Small Business Development Centers); see also *Women in Business: Leveling the Playing Field: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 11 (2008) (statement of Laila Partridge, CEO, Cover4me) (explaining that the people who funded her business were people who knew her, had worked with her, and who understood what she could do).

[86] *Business Start-Up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 1 (2008) (statement of Don O'Bannon, Chairman, Airport Minority Advisory Council (AMAC)).

[87] *Opportunities and Challenges for Women Entrepreneurs on the 20th Anniversary of the Women's Business Ownership Act: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 31-32 (2008) (statement of Ann Sullivan, Women Impacting Public Policy).

[88] *Ibid.*

[89] Robert W. Fairlie and Alicia M. Robb, *Why are Black-Owned Businesses Less Successful Than White-Owned Businesses? The Role of Families, Inheritances, and Business Human Capital*, 25 Journal of Labor Economics 289, 309-311 (2007).

These findings are borne out in a 2008 report published by the Minority Business Development Agency, which examined many of the challenges faced by minority-owned businesses that contribute to their lower survival rates when compared to non-minority businesses.[90] The report found that "a greater proportion of minority businesses operating in 2002 used more expensive sources of capital, such as credit cards, to start or acquire the business, compared to non-minority businesses. Minority firms were also less likely to use bank loans to start, acquire, expand or finance capital expansions of the business compared to non-minority firms."[91] Differences in capital usage between minority firms and non-minority firms still existed when data were segregated for firms with gross receipts of $500,000 or more.[92] The findings suggest minority-owned firms may be faced with a larger financial burden when starting and expanding their businesses because credit cards often carry higher costs compared to business loans that generally have more favorable terms.[93]

Finally, Congressional hearings provide specific examples of how lending discrimination plays out in the real world. Testimony from minority and women business owners has provided egregious examples of racial and gender discrimination by lenders. For example, one minority contractor with solid financial data was denied a loan only to have one of his white employees take the same financial data to the same loan officer, receive a loan, and be told that he was "the kind of businessman [the bank was] looking for."[94] After that experience, the contractor never went into a bank without a white employee accompanying him. Other testimony revealed that some women business owners are repeatedly asked to have a man co-sign their business loan applications, even when the men are not affiliated with the business and have lower credit scores or lower personal incomes than the women seeking the loans.[95] According to one witness, after a female applicant in that situation explained to the loan officer that her husband had no involvement with her company or the construction industry and that he had a lower credit score than the applicant, the loan officer nonetheless stated that the bank would be "a lot more

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[90] U.S. Department of Commerce, Minority Business Development Agency, *Characteristics of Minority Businesses and Entrepreneurs, An Analysis of the 2002 Survey of Business Owners* (2008).

[91] *Id.* at 54.

[92] *Id.* at 26-27.

[93] *Id.* at 54.

[94] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 311 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT).

[95] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 299 (2009) (statement of Joann Payne, President, Women First National Legislative Committee); see also *Opportunities and Challenges for Women Entrepreneurs: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 25 (2008) (statement of Margot Dorfman, CEO, U.S. Women's Chamber of Commerce) (relaying experience of woman business owner who was told she would need her husband to co-sign her loan application because the lender did not believe that the applicant had a higher salary than her husband).

comfortable with a man's name on the application."[96]

C. *Discrimination Limits Access To Contracting Markets.*

Even when women and minorities are able to form and develop businesses, they often continue to experience discrimination that impedes their ability to compete equally for government contracts.[97] This discrimination takes many forms, including discrimination by prime contractors, exclusion from business networks, and discrimination by bonding companies and suppliers.[98]

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[96] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 299 (2009) (statement of Joann Payne, President, Women First National Legislative Committee).

[97] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 309 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT) ("The Department believes strongly that, while substantial progress has been made, discrimination and its effects continue to exist today and to distort contracting opportunities for DBEs."); *Opportunities and Challenges for Women Entrepreneurs: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 8 (2008) (statement of Virginia Littlejohn, Co-Founder and CEO, Quantum Leaps, Inc.) ("Access to federal procurement remains a huge area of underachievement, and is one of the biggest structural impediments to the economic advancement of women owned businesses in the US.").

[98] See *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 27 (2007) (statement of Jon Wainwright, Vice President, NERA Economic Consulting) (discussing findings from thousands of surveys and interviews that show that, throughout the country, and within both the public and private sector marketplaces, minorities report similar instances of negative stereotyping regarding their qualifications, double standards about their performance, and discrimination by bonding companies and suppliers); *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 28 (2008) (statement of Jon Wainwright, Vice President, NERA Economic Consulting) (concluding that "minorities and women reported that they still encounter significant barriers to doing business in the public and private sector market places, as both prime contractors and subcontractors" and "continued operation of federal, state, and local efforts to ensure equal access to the public contracting process is essential to the competitive viability of minority-owned and women-owned business enterprises."); *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 223 (2009) (statement of Julie Cunningham, President and CEO, Conference of Minority Transportation Officials) (testifying that "discrimination is still a serious problem" and citing "use of antiquated 'old boy networks,' exclusion of DBEs from business opportunities, discrimination in credit lending, bonding and insurance, attempts to induce DBEs

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1. *Discrimination By Prime Contractors Creates Obstacles.*

Discrimination by prime contractors poses a very significant and continuing obstacle to contracting for minority- and women-owned businesses. In the past, evidence before Congress has shown that "minority-owned firms are seldom or never invited to bid on projects that do not contain affirmative action requirements."[99] This remains true today for both minority- and women-owned firms.[100] A recent study that included surveys and interviews of hundreds of Disadvantaged Business Enterprises (DBEs) found general agreement among them "that without the use of affirmative remedies such as the USDOT DBE Program, minorities and women would receive few if any opportunities [— either as prime contractors or as subcontractors[101] —] on government contracts."[102] That study's author testified before Congress that, through his research, he has repeatedly found that contractors who use minority- and women-owned businesses on projects with goals "rarely use [those businesses] — or even solicit them — in the absence of such goals."[103]

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to act fraudulently as 'fronts' and discriminatory application of procurement and contracting rules"); see also *id.* at 328 (statement of Jon Wainwright, Vice President, NERA Economic Consulting).

[99] 61 Fed. Reg. at 26,058.

[100] *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 86 (2008) (statement of Anthony Brown, Chair, Government Affairs Committee of the AMAC, Senior Associate Partner, MGT of America) ("I can say in the many offices that I have held in airports, it has been very frustrating when you have contracts that are of a particular size and you will come in contact with very qualified, very capable minority business owners who have been limited in their abilities and their business's ability to grow, not due to their vision, not due to their hard work, not due to their ability, but simply due to the fact that no one will give them the opportunity to do the work because of what their racial or ethnic background is or their sex.").

[101] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 331 (2009) (statement of Jon Wainwright, Vice President, NERA Economic Consulting) ("In general, minorities and women reported that they still encounter significant barriers to doing business in the public and private sector market places, as both prime contractors and subcontractors.").

[102] *Ibid.*; see also *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 27 (2007) (statement of Jon Wainwright, Vice President, NERA Economic Consulting).

[103] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 331 (2009) (statement of Jon Wainwright, Vice President, NERA Economic Consulting)

The discriminatory attitudes of some prime contractors towards minority- or women-owned firms are demonstrated by prime contractors who cynically use minority- or women-owned firms to get lower prices from non-minority subcontractors, or even to win the prime contract itself, with no intention of ever actually using the minority- or women-owned firms. In "bid shopping," a prime contractor solicits a bid for subcontract work from minority- or women-owned firms in order to qualify for a contract goal, but then, rather than using the minority-or women-owned business, shares those bids with non-minority subcontractors so the non-minority businesses can submit a lower bid.[104] In Pima County, Arizona, for example, 19% of Caucasian women business owners and 25% of Hispanic business owners experienced pressure to lower quotes on a bid because of bid shopping by prime contractors.[105]

Another questionable practice is the "bait and switch," in which a contractor commits to using a minority- or woman-owned business to win a contract that contains race- or gender-conscious goals for subcontractors, but then never actually gives the minority- or woman-owned firm the promised work. For example, after receiving a complaint from a DBE owner who alleged that a large prime contractor had used the DBE to secure a contract without generating work for the DBE, the DOT investigated and learned that the prime contractor had falsely represented to the DOT that it had met its DBE requirements.[106] Another time a DBE alleged that it had been included on the prime's original contract but was replaced by a non-DBE contractor *after* the contract had been awarded to the prime.[107] A number of state and local

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[104] For example, one witness testified before Congress that a Hispanic construction subcontractor was informed by a large majority owned prime contractor that they would use him on a job to fulfill a contract goal, but they in fact "shopped" his bid to a much larger majority subcontractor and removed the minority subcontract from the contract. *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 60 (2008) (statement of Anthony Brown, Chair, Government Affairs Committee of the AMAC, Senior Associate Partner, MGT of America). The subcontractor also reported that, based on his 25 years of experience in the industry, he feels "there is significant racial animus against Hispanic owned companies." *Ibid.* See also *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 43 (2007) (letter from Rita Baslock, President, Max Electric, Inc.).

[105] D. Wilson Consulting Group, *A Comprehensive Study of the Pima County MWBE Program* 9-11 (2008).

[106] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 313 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT).

[107] *Ibid.* See also *Expanding Opportunities for Women Entrepreneurs: The Future of Women's Small Business Programs: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 57 (2007) (statement of Wendi Goldsmith, President,

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disparity studies have concluded that this practice is a major problem facing minority- and women-owned businesses.[108]

The prevalence of discrimination comes starkly into focus in jurisdictions that recently have discontinued race-conscious programs. For example, Congress heard testimony that less than a year after Michigan discontinued its affirmative action contracting program, the percentage of state-funded highway construction projects performed by DBEs *fell to zero*, even though their participation in the federal program was 13%.[109] Other states also experienced dramatic decreases in the participation of minority- and women-owned businesses when race- and gender-conscious remedies were abandoned.[110] Indeed, research shows that the disparity in

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Bioengineering Group) ("In many cases, small firms are recruited onto teams to help win work as called for in contract solicitations. We appear in the proposals, often at great expense to the small and minority and women-owned businesses due to the work related to researching and compiling proposal materials, only to never actually receive work under the contract. I cringe to recount how many times that happened to my firm and to tally how much money, namely hundreds of thousands of dollars my firm involuntarily contributed in order to help other firms win and perform work, while we received none or sometimes a token amount."); see also *Access to Federal Contracts: How to Level the Playing Field: Field Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 172 (2007) (statement of Women Impacting Public Policy (WIPP)) (explaining that prime contractors often list women-owned business on their bid, but then revert to using "the same old subcontractors they have used in other bids" after winning the contract).

[108] See, *e.g.*, CRA International for the San Mateo County Transit District and the Peninsula Corridor Joint Powers Board, *Measuring Minority- and Women-Owned Construction and Professional Service Firm Availability and Utilization* 139 (2008) (finding that, in many cases, minority- and women-owned businesses were considered by prime contractors bidding for government jobs merely "for cosmetic purposes related to compliance with suggested or required good faith efforts"); Mason Tillman Associates, Ltd., *State of New Jersey Construction Services Disparity Study, 2000-2002* at 2-34 (2005) ("Many [minority and women business owners] reported that prime contractors have purposely used tactics to circumvent the [DOT DBE program's 'good faith effort'] requirements. For example, some prime contractors will seek to obtain [minority- and women-owned] business names and certification numbers without intending to use them on their projects."). One DBE in New Jersey explained that majority-contractors frequently get a minority business to bid on a project just "so they can say they [have] a minority bid" but do not actually consider subcontracting with the minority-owned firm. *Id.* at 2-36.

[109] *The Department of Transportation's Disadvantaged Business Enterprise Programs: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 301 (2009) (statement of Joann Payne, President, Women First National Legislative Committee).

[110] In Idaho, for example, the rate of minority- and women-owned business participation remained steady at just above 6% from 2004 through 2006 under a goal-based program. When Idaho switched to a race-neutral program in 2007, their participation rate dropped to below 4%.
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contracting between minority- and majority-owned businesses is "markedly greater in jurisdictions where there [is] no goals program in place."[111] Joann Payne, President of Women First National Legislative Committee, told Congress that based on "history and present DBE participation percentages on state funded projects," absent race- and gender-conscious remedies, "participation [in government contracting] of women and minority owned businesses will drop nationally to approximately 2[%]."[112]

Academic studies have also found that the presence of race- and gender-conscious programs significantly improves minority- and women-owned businesses' ability to develop and participate in government contracting. For example, one study found that the gap between white and minority self employment rates narrowed during the 1980s "when affirmative action programs were implemented by many public sector jurisdictions."[113] The same study found that the gap began to widen again when the number of race-conscious contracting programs was reduced after the Supreme Court's decision in *Croson*,[114] and then narrowed again after 2000 once courts began to declare race-conscious contracting programs constitutional.[115] Another study found similarly that when race-conscious "programs are removed or replaced with race-neutral programs the utilization of minorities and women in public construction declines rapidly."[116] That study concluded that affirmative action programs appear to work but have not

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Ibid. The same thing happened in California: DBE participation in federally funded contracts was 9% between 2002 and April 2006, but dropped to less than 5% in May 2006 after the state discontinued setting DBE goals. *Ibid.* The participation rate for women-owned businesses was just 0.1%. *Ibid.*

[111] *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 3 (2007) (statement of Anthony W. Robinson, President, Minority Business Enterprise Legal Defense and Educational Fund).

[112] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 302 (2009) (statement of Joann Payne, President, Women First National Legislative Committee).

[113] David G. Blanchflower, *Minority Self-Employment in the United States and the Impact of Affirmative Action Programs*, National Bureau of Economic Research, Working Paper 13972, at 17 (2008).

[114] *City of Richmond* v. *J.A. Croson, Co.*, 488 U.S. 469, 492 (1989) (holding that the City of Richmond had failed to demonstrate a compelling interest to justify its race-conscious contracting program).

[115] David G. Blanchflower, *Minority Self-Employment in the United States and the Impact of Affirmative Action Programs*, National Bureau of Economic Research, Working Paper 13972, at 17 (2008).

[116] David G. Blanchflower and Jon Wainright, *An Analysis of the Impact of Affirmative Action Programs on Self-Employment in the Construction Industry*,National Bureau of Economic Research, Working Paper 11793, at 24 (2008) ("The evidence we have available to us suggests that very rapidly after the race and gender conscious programs were removed the utilization of

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yet achieved their objectives "because they have not been allowed to work by non-minority contractors and by the courts."[117]

Congress has also heard testimony reporting a general "unwillingness [by prime contractors] to use minorities and women on jobs where there is no [minority- or women-owned business contracting] goal" even though "[t]here are a significant number of minority/women small business contractors who have the capability and proven experience to perform."[118] One witness testified that many prime contractors maintain a "mentality of exclusion" with respect to subcontractors, and explained that contractors exhibiting this mentality believe that "minority- and women-owned businesses don't belong at the table."[119]

DOT's recent experience in administering its DBE program provides further evidence of the lasting effects of discrimination in contracting and the continuing need for race- and gender-conscious programs to address those effects. DOT's program requires states to use the "best evidence available to estimate the DBE participation they could expect to obtain if there were a nondiscriminatory level playing field."[120] This "evidence-based estimate" then becomes the state's goal for DBE participation.[121] States are required to "achieve as much as possible of that annual goal through * * * 'race-neutral' means," including "[o]utreach, technical and bonding

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firms owned by women and minorities collapsed."); see also Insight Center for Community Economic Development, *The Impact of State Affirmative Procurement Policies on Minority- and Women- Owned Businesses in Five States, Best Practices, Imperfections, and Challenges in State Inclusive Business Programs* iv (2007) (concluding that "when affirmative procurement policies end or are interrupted, MBEs and WBEs do not grow as fast as similar businesses in other states" and that these "slower business growth rates are not usually made up later, indicating the importance of the consistent presence of affirmative procurement programs").

[117] *Ibid.*

[118] *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 43 (2007) (letter from Rita Baslock, President Max Electric, Inc.).

[119] *How Information Policy Affects Competitive Viability in Minority Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 85 (2008) (statement of Anthony Brown, Chair, Government Affairs Committee of the AMAC, Senior Associate Partner, MGT of America).

[120] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 308 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT); see also 49 C.F.R. 26.

[121] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 308 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT).

assistance, unbundling of contracts, and small business programs."[122]

What DOT found is that, between 2004 and 2008, states that received federal transportation dollars had to resort to race-conscious measures to meet their DBE participation goals 81% of the time.[123] The magnitude of this finding was not lost on DOT officials: "This means that, eight out of ten times, [DOT funding] recipients, if denied the availability of race-conscious goals, would have left unremedied the effects of discrimination on small, disadvantaged business."[124] Perhaps even more revealing is that "in 69 percent of these cases, the race-conscious component of the goal was needed to make up the majority of the entire overall goal."[125] These facts led DOT to conclude that "in the absence of race-conscious goals, the gap between a level playing field and the reality facing DBEs trying to find work with [DOT funding] recipients would have been significantly larger."[126]

That conclusion was proven in jurisdictions that have suspended the use of race-conscious measures. These jurisdictions have experienced declines in DBE participation and have not been able to meet their participation goals. For example, Congress heard testimony that after jurisdictions discontinued the use of race-conscious measures, following the Ninth Circuit's decision in *Western States Paving Co.*,[127] the results were striking. Arizona's DOT set overall goals of 9.1% in 2007 and 9.9% in 2008, but only achieved 3.8% and 3.1%, respectively; California's DOT set goals of 10.5%, 10.5% and 13.5% for 2006-2008, but was only able to achieve 8.2%, 6.6% and 4.6% participation by DBEs during those years; Sound Transit in

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[122] *Ibid.*

[123] *Id.* at 309.

[124] *Ibid.*

[125] *Ibid.*

[126] *Ibid*; see also *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 292 (2009) (statement of Don O'Bannon, Chairman, Airport Minority Advisory Council) ("One study found that DBE participation dropped to virtually zero on federally-assisted contracts during a time when the program was enjoined. Researchers stated that 'it appears that the mere fact of adopting a DBE program — whether or not goals are being set on any given contract — increases DBE participation.'").

[127] *Western States Paving Co., Inc.* v. *United States and Washington State Dep't of Transp.*, 407 F.3d 983 (9th Cir. 2005). In *Western States Paving Co.*, the court concluded that DOT's race-conscious contracting program — the Transportation Equity Act for the 21st Century — is constitutional on its face. The evidence before Congress established a compelling interest for the program, *id.* at 991-993, and — because race-conscious measures are used only when race-neutral means prove ineffective, and are employed in a flexible manner for a limited duration — the program is narrowly tailored, *id.* at 993-996. But the court determined that the program was unconstitutional as applied in Washington state because – the court concluded – the State failed to proffer "evidence of discrimination within its own contracting market and * * * thus failed to meet its burden of demonstrating that its DBE program is narrowly tailored." *Id.* at 1003.

Washington state set goals of 15% in 2007 and 13% in 2008, but only achieved 8.6% and 6.8% participation; Portland's airport set goals of 7.3% and 4% for the years 2007 and 2008, but only achieved 2% and 1.1% participation in those years.[128] From the reduction in the use of DBE programs following the *Western States Paving Co.* decision, DOT concluded that without the ability to use race conscious measures, states that are DOT funding recipients cannot, in many cases, "ensure [that] their Federally-assisted contracting programs provide nondiscriminatory access to business opportunities on a level playing field, as defined by their overall goals."[129] One DBE contractor "told State officials, since 'there's no DBE participation goal, our phones have stopped ringing . . . we don't get calls any more.'"[130]

These data — which reveal the significant downturn in contracts and dollars won by minority- and women-owned firms when race- and gender-conscious programs are eliminated — demonstrate more than just that these programs present opportunities. They establish that without such programs, minority- and women-owned firms are left with significantly less business than they actually can perform. When race- and gender-conscious programs are in place, minority- and women-owned firms secure, and perform, many more contracts than they secure without such programs. This certainly demonstrates that the amount of business these firms can handle is not defined by their success when these programs are not in place; rather, their capacity to perform work outstrips what they are hired to do in the absence of goals and in any event expands as contracts become available to them.

The evidence before Congress also contains many examples of blatant and egregious discrimination against minorities and women:

- One Alaskan-Native construction specialty contractor was regularly told by a prime contractor that he was only hired because he is a minority.[131] The prime contractor also

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[128] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 310 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT). See also *id.* at 31 (statement of Joann Payne, President, Women First National Legislative Committee) (noting that in Idaho, the rate of minority- and women-owned business participation remained steady at just above 6% from 2004 through 2006 but dropped to below 4% in 2007 and that DBE participation in federally funded contracts was 9% between 2002 and April 2006, but dropped to less than 5% in May 2006).

[129] *Id.* at 310 (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT).

[130] *Ibid.* A DOT official relayed additional stories of DBE contractors following the *Western States Paving Co.* decision: one DBE contractor reported a 50% drop in calls following the decision; and a woman business owner reported that "where there are no goals, I can tell you that the fax machines stop . . . the next day I got no faxes, the phone didn't ring, asking for my bid. I used to get maybe 20 faxes a day . . . now I might get three a week." *Ibid.*

[131] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 292-293 (2009)

(continued...)

explicitly expressed his view that "minority businesses [are] not qualified."[132] At this same job site, the Alaskan Native's "company's equipment was regularly turned on during the night, causing the batteries to die and the project to be delayed. No non-minority contractors experienced this problem."[133]

- A Hispanic contractor was told by a general contractor that he "did not want any Mexicans on the job."[134] On other job sites, that same Hispanic contractor "has been called 'Wetback,' 'brown like s**t,' 'dumb Mexican,' 'little Mexican,' [and] 'my little Mexican friend.'"[135]

- A DBE owner in Delaware had a disagreement with one of her prime contractors, who insisted on speaking with her male foreman whenever he called her office.[136] Despite the male foreman's insistence that the prime needed to speak with his female boss, the prime called the boss's home — *and left a message for her husband*, who was not involved in the project.[137] In the message to the husband, the prime explained that he wanted to resolve the issue through a meeting but that "we don't have to have your wife

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(statement of Don O'Bannon, Chairman, Airport Minority Advisory Council).

[132] *Ibid.*

[133] *Ibid.*

[134] *Ibid.*

[135] *Ibid.*; see also *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 311 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT) (relaying incident where a Hispanic contractor "was not allowed to provide a proposal on a private contract because of ethnicity").

Congress has heard many other reports of direct discrimination by prime contractors against minorities. One minority contractor reported not being given a seat at the table for a presentation to a general contractor during which the general contractor "joked and laughed about the fact that he believed he had a way of 'getting around' the DBE ordinance." *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 294 (2009) (statement of Don O'Bannon, Chairman, Airport Minority Advisory Council). An African-American contractor reported that he encounters people who assume he does not understand fairly simple work-related matters because of his race. *Id.* at 293. Another minority contractor reported encountering the attitude, among other contractors, that "minorities are better-suited to be janitors or plumbers than architects." *Id.* at 294. That contractor also reported "that his firm gets less credit than non-minority owned firms when projects are successful, and disproportionate criticism when projects are not successful." *Ibid.*

[136] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 299 (2009) (statement of Joann Payne, President, Women First National Legislative Committee).

[137] *Id.* at 299-300.

involved."[138] When the prime finally met with the female owner of the company, the first thing he said to her was "I am sorry this has taken so long but I don't like dealing with women."[139]

Similar evidence of discrimination by prime contractors against minorities and women is recounted in local disparity studies. For example, when a female contractor attempted to collect money she was owed on a subcontract from the prime contractor, the prime contractor refused to pay her, saying "no woman [should] make that kind of money."[140]

Another particularly egregious example of discrimination by a prime contractor occurred

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[138] *Id.* at 300.

[139] *Ibid.* Another woman told of an instance "when a project's resident engineer [would not] speak to [her] on the job site but direct[ed] all his comments to the (male) foreman standing two feet to [her] left." *Id.* at 299. Similarly, another woman reported getting calls asking for the man in charge; the caller simply hung up after finding out that the person in charge was a woman. *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 214 (2009) (statement of Katherine M. Cloonen, President and Owner, JK Steel Erectors, Inc.). Cloonen also reported that when she was starting out, she was not taken seriously and was sent the worst workers from the union. *Ibid.* Other women complained that they frequently encounter people who assume that they are "fronts" for the man who really owns the business. *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 293, 299 (2009) (statement of Joann Payne, President, Women First National Legislative Committee & statement of Don O'Bannon, Chairman of the Airport Minority Advisory Council).

[140] Mason Tillman Associates, Ltd., *State of New Jersey Construction Services Disparity Study, 2000-2002*, Vol. 1 at 2-11 (2005); see also BBC Research & Consulting for the Washington Suburban Sanitary Commission, *WSSC 2005 Disparity Study – Summary and Recommendations*, § 3 at 17 (2005) (African-American business owner in the Washington, D.C., area reported that he lost work when a client learned of his race; officials in charge of the project indicated that they loved his company's proposal but then used a white-owned company instead after learning that his firm was minority-owned); MGT of America, Inc., *The City of Phoenix Minority-, Women-Owned and Small Business Enterprise Program Update Study* 6-22 (2005) (minority contractor reported that "[t]here have been incidents where I've been on the job site and the General [Prime Contractor] won't talk to me, they will go to the white foreman and talk to the foreman"); Washington Suburban Sanitary Commission by BBC Research & Consulting, *WSSC 2005 Disparity Study – Summary and Recommendations*, § 4 at 21 (2005) (Hispanic owner of a construction firm recounting experience where three white men at an industry conference pointed to his friend, an African-American man, and started making racist comments and using racial slurs); University of Minnesota Disparity Study Research Team, *Analysis of Essex County Procurement and Contracting: Final Report* 91 (2005) (recounting racially and gender motivated harassment experienced by minorities and women at job sites).

on a government contract in Iraq. Worldwide Network Services (WWNS), an African-American-owned firm, was awarded a subcontract to perform communications work on two security-related contracts for DynCorp International.[141] DynCorp was initially satisfied with WWNS's work and rated it as "exceptional" and "very good."[142] But in 2005, DynCorp began discriminating against and exhibiting racial animus toward WWNS in a number of ways, including: excluding WWNS from planning meetings, failing to respond to WWNS's requests for information and assistance, refusing to provide WWNS employees with security badges they needed in order to perform their work, and refusing to make or process payments on WWNS's invoices.[143] These actions "effectively put WWNS * * * out of business."[144] The jury found that DynCorp's conduct was motivated by racial animus. DynCorp's IT manager referred to WWNS as "kaffirs," a derogatory term for black South Africans, and also made many other derogatory comments.[145]

2. *Discrimination By Business Networks Limits Opportunities.*

As the Department of Justice explained in 1996, access to informal business networks is essential to survival in contracting because these networks "serve as conduits of information about upcoming job opportunities and facilitate access to the decisionmakers."[146] These same networks and contacts "can help a business find the best price on supplies, facilitate a quick loan, foster a relationship with a prime contractor, or yield information about an upcoming contract for which the firm can prepare — all of which serve to make the firm more competitive."[147]

Race- and gender-conscious contracting programs have helped some women and minorities break into these networks. Indeed, a DOT official recently testified before Congress that "possibly the most important function" the DBE program has performed over the last 30 years "is to address the lack of access by minority and women contractors to these crucial

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[141] *Worldwide Network Services, LLC* v. *DynCorp International, LLC*, No. 1:07-cv-627, Doc. 459 at 6 (E.D.V.A. Sept. 22, 2008).

[142] *Id.* at 6-7.

[143] *Id.* at 7-8.

[144] *Id.* at 8.

[145] *Id.* at 7.

[146] 61 Fed. Reg. at 26,059. See also *Expanding Opportunities for Women Entrepreneurs: The Future of Women's Small Business Programs: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 57 (2007) (statement of Wendi Goldsmith, President, Bioengineering Group) ("It is virtually impossible to win work through a competitive process without a level of comfort that comes through personal relationships, * * * long-term relationships — going to school together, working together or what have you.").

[147] 61 Fed. Reg. at 26,059; see also *Expanding Opportunities for Women Entrepreneurs: The Future of Women's Small Business Programs: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 57 (2007) (statement of Wendi Goldsmith, President, Bioengineering Group) (discussing the importance of networks).

informal networks."[148] The official explained that the program requires prime contractors, who may not normally socialize with minority or female contractors, to make an effort to involve minority- and women-owned firms as subcontractors.[149] This, the official explained, "is a very beneficial way of introducing prime contractors to DBEs and, hopefully, beginning to create business relationships that will lead to opportunities for DBEs to get the work they need to succeed."[150]

But progress for minorities and women attempting to break into established business networks has been slow, and more work needs to be done.[151] Opening business networks to minority- and women-owned businesses "doesn't happen by accident and * * * doesn't happen without help."[152] DOT still considers lack of access to business networks and to the information those networks provide to be "[o]ne of the most important barriers to participation [in contracting]" that minorities and women face.[153]

Many minorities and women still find themselves excluded from informal business networks today. Congress has heard a significant amount of testimony about the continued prevalence of "old boys' networks" and the difficulty minority and women business owners face in attempting to break into these networks.[154] Likewise, many state and local disparity studies

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[148] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 312 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT).

[149] *Ibid.*

[150] *Ibid.*

[151] Anthony Brown, Chair of the Government Affairs Committee of the AMAC, testified about the importance of "help[ing] majority firms move beyond their established networks to give previously excluded businesses the opportunity to prove themselves." *How Information Policy Affects the Competitive Viability of Small and Disadvantaged Business in Federal Contracting: Hearing Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 58-59 (2008) (statement of Anthony Brown, Chair, Government Affairs Committee of the AMAC, Senior Associate Partner, MGT of America). But Brown said effecting this change is "hard" because of "[t]he mentality of exclusion can exist in contractors and public contracting officials." *Id.* at 55.

[152] *Id.* at 59.

[153] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 311 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT).

[154] *Opportunities and Challenges for Women Entrepreneurs: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 15 (2008) (statement of the Center for Women's Business Research) ("Acceptance into industry networks is often difficult, especially for women of color. Even when they join the meetings, they are not welcomed nor are they part of the activities."); *id.* at 18 (statement of Lisa Dolan, President, Securit) ("[B]eing in a male-dominated field in security, I am usually the only woman at the table and not taken seriously."); *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the*

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reveal that minorities and women still face barriers to participation in business networks.[155]

When minority- and women-owned businesses are excluded from business networks, they are cut off from information and decision-makers and, as a result, are placed at a serious disadvantage. As one minority business owner told Congress: "One of the major problems that we face is the overall inability to have access to decision makers as we are unable to gain access to their many formal and informal networking activities." [156] A DOT official relayed to

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Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship, 110th Cong. 43 (2007) (letter from Rita Baslock, President, Max Electric, Inc.) ("MBEs experience difficulty breaking into old-boy networks of general contractors. Because of the monetary and time consumption of the construction business for small businesses, many small minority and women subcontractors do not have the social connections, money, or time to effectively network in the old boy system."); *Women in Business: Leveling the Playing Field: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 43 (2008) (statement of Kerstin Forrester, President and Owner, Stonebridge Precision Machining & Certified Welding) ("There is still very much an 'old boys' network in place."); *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 208 (2009) (statement of Gilbert Aranza, CEO, Stars Concessions, Ltd.) ("I wish I could report that the Good Ol' Boy Network no longer exists, but I am afraid that I run up against it all the time."); *id.* at 312 (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT) (quoting one business owner as stating, "An Idaho Hispanic contractor described the network there as 'white guys that have been running around with the same white guys that have controlled the money * * * for [many] years.'"). See also Michael Bonds, *Looking Beyond the Numbers, The Struggles of Black Businesses to Survive: A Qualitative Approach*, 37 Journal of Black Studies 581, 595 (2007) (concluding that "racism seems to play a major role in limiting African American business opportunities"); *id.* at 598 ("Black business owners expressed their frustration with their inability to break in to the old boys' network, being denied business loans, having to constantly prove themselves to White business owners, or being held to a higher performance standard than Caucasian firms.").

[155] For example, a New Jersey disparity study found that both "new and established minority and women business owners report difficulties breaking into the contracting network." Mason Tillman Assocs., *State of New Jersey Construction Services Disparity Study, 2000-2002*, Vol. 1 at 2-25 (2005). That study also found that some minority- and women-owned businesses that "have been in been in operation for more than 20 years * * * are still excluded from job opportunities because they are not included in the social and business networks with those in positions of power in their respective fields." *Ibid.* Another study reported that many female and some minority business owners interviewed "were especially vocal about the 'good ole boy' system." CRA International for the San Mateo County Transit District and the Peninsula Corridor Joint Powers Board, *Measuring Minority- and Woman-Owned Construction and Professional Service Firm Availability and Utilization* 140 (2008).

[156] *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the*
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Congress minority and women business owners' concern about lack of access to important information: "There's still very much an old boy network . . . and if you're not an old boy, you're not in that network [and] there's a lot of information you don't get."[157]

In some places, minorities are still excluded from the social clubs that are a primary site for business networking.[158] More commonly, exclusion of minorities and women may be the result of non-minority contractors being comfortable with existing homogeneous networks, rather than overt discrimination.[159] That is one reason why programs that require majority-owned businesses to reach outside of their comfortable networks are so essential. If a contractor has a positive experience with a minority- or women-owned business, that may, over time, open the door to a continuing business relationship. That is precisely what has happened for Katherine M. Cloonen, the president and owner of JK Steel Erectors, Inc., who told Congress that the DBE

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Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship, 110th Cong. 46 (2007) (letter from Bobby E. Henderson, President, Anlab Environmental).

[157] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 311 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT); *ibid.* (relating comment from a DBE firm owner, who noted that the "number one thing [that] puts DBEs at a disadvantage is lack of access to decision makers, who maybe . . . go out to drinks every once in a while . . . or see each other on the golf course"); *id.* at 311-312 (relating comment from a trade association representative, who stated: "Lots of things get done with back slapping and who knows who and if you're not in that group you might as well not come to the party."); see also MGT of America, *Broward County Small Disadvantaged Business Enterprise (SDBE) Study* 6-97 (2001) (quoting a business owner explaining that white owners enjoy certain advantages because "[t]hey play golf together and their kids go to the same schools").

[158] Chuck Covington, CEO of People's Transit, told Congress that in Michigan, where he does business, the Eagles Club is a primary hub for networking. *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 5 (2009). This club has an unwritten rule excluding African Americans. *Ibid.* Covington said the club's rule "sickens" him, "[b]ut the fact that it impacts my ability to conduct business is reprehensible." *Ibid.* Summarizing the problem, Covington said, "If people do business with the people they are comfortable with, and if I am denied opportunities to sit down and get to know people — based on nothing more than my race — it automatically puts me and my business at a disadvantage." *Ibid.*

[159] *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 15 (2007) (statement of Professor Candida Brush, Paul T. Babson chair-professor of entrepreneurship, Babson College) ("[W]e know from what is called the theory of homophily that people like to do business with people who are like themselves. So if you have this very homogeneous group, if you happen to be different in some way, it is going to be hard for you to get over that barrier.").

program has allowed her to slowly break into business networks.[160]

3. *Discrimination In Bonding And By Suppliers Burdens Disadvantaged Firms.*

Many contracts, both public and private, require bidders to secure a surety bond. Accordingly, success in contracting depends not only upon a firm's ability to do the work at a good price, but also on the firm's ability to obtain quality services from bonding companies. Any discrimination that exists in the bonding market makes fulfilling this requirement much more difficult for minority- and women-owned firms.[161]

A surety bond is required "[b]efore any contract of more than $100,000 is awarded for the construction, alteration, or repair of any public building or public work of the Federal Government."[162] As the Department of Justice explained in 1996,[163] our country's history of discrimination often lands minority- and women-owned businesses in a vicious cycle: they cannot get bonding because they lack experience, yet they cannot get experience because they lack bonding.[164] A 2006 report of the National Association of Women Business Owners

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[160] *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 213-214 (2009) (statement of Katherine M. Cloonen).

[161] See, *e.g.*, *The Department of Transportation's Disadvantaged Business Enterprise Programs: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 2 (2009) (statement of the Hon. James L. Oberstar, Chairman and Rep. from Minnesota) ("This data demonstrates that it is difficult for small and disadvantaged businesses to compete – discrimination impacts minority and women owned businesses at many points in the contracting process, including obtaining credit, *bonding*, and insurance.") (emphasis added).

[162] 40 U.S.C. 3131.

[163] 61 Fed. Reg. at 26,060.

[164] See, *e.g.*, *Access to Federal Contracts: How to Level the Playing Field Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 132 (2007) (statement of Randy McRae) ("[B]onding has been a cruel Catch-22 for [DBEs]. These struggling firms either can't afford a bond or can't persuade bonding companies to guarantee their performance. But without a bond, they can't bid on many jobs in the public or private sector, limiting their growth."); *id.* at 48 (statement of Wayne Frazier, Sr., President, Maryland-Washington Minority Contractors Association) ("Small businesses dealing with the Federal Government cannot get surety bonding. Again, no financing, no bonding, no contract, no award, no way to compete."); *The Department of Transportation's Disadvantaged Business Enterprise Program: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 311 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT) (relating comment from a female contractor in California who stated that "minorities and women have a much harder time getting capital, getting bonding, getting insurance ... in bonding ... women are still asked to have their husbands sign at the bank"); see also Washington Suburban Sanitary Commission by BBC Research & Consulting, *WSSC 2005 Disparity Study – Summary and Recommendations*, § 4 at 19-20 (2005)

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Procurement Task Force, which was submitted to Congress, concludes that "[b]onding requirements and other financial tests can impose an insurmountable barrier to [women-owned small businesses] seeking federal contracts."[165] Where prime contractors set the bonding requirement at an unnecessarily high level, moreover, it effectively excludes a greater percentage of minority- and women-owned businesses because those businesses are more commonly unable to secure the necessary levels of bonding due to the variety of discriminatory barriers that have been discussed thus far.[166]

Moreover, their inability to secure bonding prevents minority- and women-owned businesses from growing their companies to the point where they can take on the role of prime contractor. One congressional witness explained: "You have to have proof that you are capable and have the capacity to deliver to large scale-projects if, in fact, you want to be a prime. As a result of the inability to be bonded, you end up being a subcontractor, which limits your growth opportunities."[167]

State and local disparity studies also identify bonding requirements as a major obstacle to success for minority- and women-owned businesses. For example, one study found that "[o]btaining sufficient bonding (or bonding at all) is frequently cited as a major barrier" to

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(minority business owner reported that MBE firms get charged a higher rate for the same bonding as compared to white competitors).

[165] *Opportunities and Challenges for Women Entrepreneurs on the 20th Anniversary of the Women's Business Ownership Act: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 67 (2008) (report of the NAWBO Procurement Task Force, February 2006).

[166] *How Information Policy Affects Competitive Viability in Minority Contracting Before the Subcomm. on Information Policy, Census, and National Archives of the H. Comm. on Oversight and Government Reform*, 110th Cong. 92 (2008) (statement of Anthony Brown, Chair, Government Affairs Committee of the AMAC, Senior Associate Partner, MGT of America); *The Department of Transportation's Disadvantaged Business Enterprise Programs: Hearing Before the H. Comm. on Transportation and Infrastructure*, 111th Cong. 311 (2009) (statement of Joel Szabat, Acting Assistant Secretary, Transportation Policy, DOT) ("Several California [DBE] contractors mentioned that prime contractors often imposed higher bonding or insurance requirements than the state required, blocking them from participation.").

[167] *Women in Business: Leveling the Playing Field: Roundtable Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 26 (2008) (statement of Eydie Silva, Executive Director, State Office of Minority and Women Business Assistance); see also Kevin O'Brien, Ph.D., Bernard Goitein, Ph.D., and Camden Bucey, *Disparity Study for the City of Peoria* 32, 36 (2004) (concluding that lack of access to bonding was a factor that helped to explain why, from 1992-2001, no African-American-owned business in Peoria was able to obtain a contract as a prime contractor in any of the City's 136 contracting projects; and there was only one project where a women-owned business was the prime contractor).

contracting for minority- and women-owned businesses.[168] Specifically, that study concluded that "[m]inority firms often have difficulty obtaining bonding because they lack the experience bonding companies require."[169]

Discrimination by suppliers is also still a problem. If a supplier charges minority- or women-owned businesses a higher price than it charges a majority-owned business, then the minority- and women-owned firms will have to include the higher price of supplies in their bid. This in turn limits the minority- and women-owned businesses' ability to compete.[170] The problem has a significant effect on minority- and women-owned businesses. For example, a disparity study in Memphis, Tennessee, found that 21.6% of the minority- and women-owned businesses surveyed stated that they had experienced at least one instance of discrimination by a supplier in the last five years.[171] Another study found that women-owned businesses reported "that they were often given a higher price for materials than their male-owned counterparts, and they believe that the higher prices were related to their gender."[172]

Congress has also heard testimony about supplier discrimination. One egregious example occurred in Michigan: An African-American employee of a minority-owned business obtained a quote of $613 per tire for 16 new tires.[173] The minority business owner discovered that a white business associate had paid only $400 per tire.[174] He then called the supplier and "put on a white voice" and was quoted $400.[175] Congress also heard about an African-American mechanical contractor who solicited a quote for equipment from his non-minority-owned supplier which he then included in his bid.[176] He then received a fax from the supplier that was intended for his

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[168] Pennsylvania Advisory Comm. to the U.S. Comm'n on Civil Rights, *Barriers Facing Minority- and Women-Owned Bus. in Pa.* 18 (2002) .

[169] *Id.* at 19.

[170] See National Economic Research Associates, Inc., *Race, Sex, and Business Enterprise: Evidence from Memphis, Tennessee* 103 (2008) (concluding that "discrimination by commercial customers and suppliers against [minority- and women-owned businesses] operates to increase input prices and lower output prices for" those businesses).

[171] *Id.* at 259.

[172] CRA International for the San Mateo County Transit District and the Peninsula Corridor Joint Powers Board, *Measuring Minority- and Woman-Owned Construction and Professional Service Firm Availability and Utilization* 139 (2008).

[173] *The Department of Transportation's Disadvantaged Business Enterprise Programs: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 217 (2009) (statement of Chuck Covington, CEO, People's Transit).

[174] *Ibid.*

[175] *Ibid.*

[176] *Minority Entrepreneurship: Assessing the Effectiveness of SBA's Programs for the Minority Business Community: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 110th Cong. 39 (2007) (statement of Anthony W. Robinson, President, Minority Business Enterprise Legal Defense and Educational Fund).

non-minority-owned competitor, quoting the competitor a lower quote.[177] When the minority business owner requested the lower price quote provided to his competitor, the supplier responded that it reserved the right to provide better pricing to their better customers.[178] Obviously — as a minority business owner testified — "no businessperson, no matter how talented, can succeed if they are paying a race-based mark-up on supplies."[179]

III.

Conclusion

The discussion above surveys only a portion of the evidence that demonstrates that the race- and gender-based barriers facing minority-and women-owned firms still exist. While some progress has been made, the U.S. Small Business Administration's 8(a) and Women-Owned Small Business programs, the DOT's Disadvantaged Business Enterprise program, and similar programs are still critical to prevent the federal government from becoming a "passive participant" in a system infected by race and gender discrimination. The government's obligation to ensure that tax money is spent fairly and equally requires these programs.

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[177] *Ibid.*

[178] *Ibid.* See also Mason Tillman Assocs., *State of New Jersey Construction Services Disparity Study, 2000-2002*, Vol. 1 at 2-7 (2005) (African-American business owner reported that one supplier demanded that she pay up front or pay a certain amount of money down before checking her business's credit rating; the supplier openly stated that the reason for this requirement was that his business was minority-owned and the supplier claimed to have "had prior experience with a minority vender that had not paid them").

[179] *The Department of Transportation's Disadvantaged Business Enterprise Programs: Hearing Before the H. Comm. on Transp. and Infrastructure*, 111th Cong. 218 (2009) (statement of Chuck Covington, CEO, People's Transit).

Appendix A

Congressional Hearings Between 2006 and 2010
Addressing Public Procurement and Minority- and Women-Owned Business Enterprises

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- *Infrastructure Investment: Ensuring an Effective Economic Recovery Program: Hearing Before the H. Comm. on Transportation and Infrastructure*, 111th Cong. (2009)
- *The Federal Aviation Administration Reauthorization Act of 2009: Hearing Before the H. Subcomm. on Aviation of the H. Comm. on Transportation and Infrastructure*, 111th Cong. (2009)
- *Full Committee Hearing on the State of the SBA's Entrepreneurial Development Programs and Their Role in Promoting an Economic Recovery: Hearing Before the H. Comm. on Small Business*, 111th Cong. (2009)
- *Full Committee Hearing on Oversight of the Small Business Administration and its Programs: Hearing Before the H. Comm. on Small Business*, 111th Cong. (2009)
- *The Department of Transportation's Disadvantaged Business Enterprise Programs: Hearing Before the H. Comm. on Transportation and Infrastructure*, 111th Cong. (2009)
- *The Role of Small Business in Recovery Act Contracting: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 111th Cong. (2009)
- *Trends Affecting Minority Broadcast Ownership: Hearing Before the H. Judiciary Comm.*, 111th Cong. (2009)
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- *Doing Business with the Government: The Record and Goals for Small, Minority and Disadvantaged Businesses: Hearing Before the H. Comm. On Transportation and Infrastructure*, 111th Cong. (2009)
- *Minority Entrepreneurship: Evaluating Small Business Resources and Programs: Hearing Before the S. Comm. on Small Business and Entrepreneurship*, 111th Cong. (2009)

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Appendix B

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Appendix C

A Sample of State and Local Government Disparity Studies

Alabama

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Alaska

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Arizona

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California

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Colorado

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- *Race, Sex, and Business Enterprise: Evidence from Denver, Colorado*, Prepared by NERA Economic Consulting for the City and County of Denver, Colorado (2006)

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Connecticut

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Florida

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Georgia

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Idaho

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Illinois

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Iowa

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Kansas

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Kentucky

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Maryland

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Massachusetts

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Minnesota

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Missouri

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Montana

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Nevada

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New Jersey

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Virginia

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Washington

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