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SUMMARY OF LEGISLATIVE AND OVERSIGHT ACTIVITIES DURING THE 108TH CONGRESS

R E P O R T

OF THE

COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP
UNITED STATES SENATE

MARCH 30, 2005.—Ordered to be printed

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COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP

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Ms. SNOWE, from the Committee on Small Business and Entrepreneurship, submitted the following

REPORT

I. OVERVIEW

During the 108th Congress, the Committee's agenda concentrated on the highest priorities of the small business community. The Committee focused on concerns such as entrepreneurial development, healthcare, small business manufacturing, the reauthorization of the Small Business Administration, access to capital, and stock option expensing. The Committee received testimony and information about these topics from small business owners, employees, and experts from across the United States. This report summarizes the legislative and oversight activities of the Committee on these key issues of concern and interest to small businesses.

II. OVERSIGHT OF THE SMALL BUSINESS ADMINISTRATION (SBA)

A. REAUTHORIZATION OF THE SMALL BUSINESS ADMINISTRATION

At the end of the 108th Congress, Congress approved comprehensive legislation reauthorizing the SBA for Fiscal Years 2005 and 2006. The SBA reauthorization was included in Division K of the Consolidated Appropriations Act for 2005 (the Omnibus Appropriations Act, Public Law 108–447) that was approved by Congress in December 2004, and signed by President Bush on December 9, 2004. The provisions of Division K reflect the significant amount of information that the Committee collected from the hearings, roundtable and discussions held throughout the 108th Congress, and had its origins in a non-comprehensive piece of legislation (S. 1375) previously adopted by the Committee and the Senate. The Committee's objectives were to single out the SBA programs that worked

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well, identify the reasons for their superior performance, and apply those principles to programs that need improvement.

While not all of the provisions of S. 1375 are contained in the Omnibus, Division K of H.R. 4818 includes updated authorization levels, improvements to the SBA's lending and technical assistance programs, and new initiatives to assist America's 21st Century entrepreneurs. Almost all of the provisions in Division K originated in several bills previously introduced by Senator Snowe, as detailed below.

Before December 2004, the last time that Congress passed legislation providing a comprehensive reauthorization of the SBA was in 2000. That previous legislation covered Fiscal Years 2001, 2002, and 2003, and expired on September 30, 2003. In early 2003, at the beginning of the 108th Congress, the Committee began the process of reauthorizing the SBA for Fiscal Year 2004 and subsequent years. The Committee held two roundtables in 2003 regarding SBA financing programs. The first roundtable was on April 30, 2003, and addressed the SBA's 7(a) Business Loan program and the SBA's Microloan Program. The second roundtable was held on May 1, 2003, and considered the SBA's 504 Loan Program, Small Business Investment Company (SBIC) Program, and New Markets Venture Capital Program. Chair Snowe chaired these roundtables and heard commentary about the SBA's budget proposals, and about the condition of the SBA's financing programs, from a wide range of program participants, small businesses, SBA employees, and financing experts.

The Committee also held a hearing, chaired by Senator Snowe, on June 4, 2003, that included testimony from SBA Administrator Hector Barreto regarding the agency's reauthorization. This hearing provided an additional opportunity for the agency to respond to issues raised during the previous roundtable discussions, discuss the legislative package that the SBA had submitted to the Committee for review, and comment on the President's Fiscal Year 2004 budget submission.

As a result of the roundtables, hearing, and extensive preparatory work done in conjunction with small businesses, small business trade groups, and industry experts, Chair Snowe introduced the "Small Business Administration 50th Anniversary Reauthorization Act of 2003" (S. 1375), which commemorated the 50th anniversary of the SBA and provided for a three-year reauthorization of the Agency, through Fiscal Year 2006. The bill had provisions that set out authorization levels for SBA programs, improved the operation of the programs, and provided for many improvements to the internal structure and activities of the SBA. The Committee held a mark-up for S. 1375 on July 12, 2004. The Committee reported the bill out of the Committee unanimously (19–0), and it was sent to the entire Senate for consideration. S. 1375 was unanimously approved by the Senate on September 26, 2003, before the SBA's then-current authorization expired on September 30, 2003.

S. 1375 was not taken up by the House, however, during the 108th Congress, and the House was also unable to pass the comprehensive SBA reauthorization bill, H.R. 2802, that was reported out of the House Small Business Committee in 2003. Therefore, the Senate and the House approved several short-term extensions of the SBA's authorization to enable the SBA to continue functioning, and to allow the SBA's programs to continue to be used by small businesses. These extensions continued throughout Fiscal Year 2004, as the House attempted to pass its SBA reauthorization bill.

On September 21, 2004, Chair Snowe and Senator Bond introduced the "Small Business Reauthorization and Manufacturing Assistance Act of 2004" (S. 2821), which was co-sponsored by Senator Roberts. This bill would have reauthorized the SBA for Fiscal Years 2005 and 2006, and would have improved SBA programs and the management structure of the SBA. The bill contained some provisions from S. 1375, some provisions from S. 2724, a bill that Chair Snowe and Senator Bond had introduced to assist small manufacturers, and which passed the Senate by unanimous consent on July 22, 2004, a few provisions from H.R. 4062, which had been approved by the House in March 2004, and by the Senate in April 2004, and had become law on April 5, 2004, and finally a few provisions from H.R. 2802, the SBA reauthorization bill reported out of the House Small Business Committee, which had never come up for a vote by the full House.

The SBA objected to provisions in S. 2821 that continued into Fiscal Year 2004 lower 7(a) borrower fees. These lower fees were first established in H.R. 4062, passed by Congress and enacted into law in April 2004, which had been enacted to allow the 7(a) program to operate through Fiscal Year 2004, even in the face of demand for loans that in 2004 far exceeded the SBA's original predictions. The SBA opposed the continuation of lower fees because those fee levels would require some appropriations for the 7(a) program. The Senate Committee on Appropriations and a majority of the Members of the House supported appropriations and lower fees for the 7(a) program, but the SBA supported making the program a zero-subsidy program, with no appropriations.

S. 2821 did not come up for a vote in the full Senate before the 108th Congress ended. As a result, the SBA's authorization had to be extended again at the end of Fiscal Year 2004, in the Continuing Resolution that provided a short-term extension for most federal agencies. Subsequently, House Small Business Committee members and industry groups conceded the issue of zero-subsidy for the 7(a) program and higher fees for 7(a) borrowers, and struck a deal with the SBA to support a particular package of provisions for the Omnibus Appropriations Bill (P.L. 108–447). That compromise was primarily based on the provisions of S. 2821, but Chair Snowe negotiated with the SBA to improve the package of provisions. The final product of those negotiations was included as Division K of the Omnibus Appropriations bill. The final package of provisions contained almost all of the provisions of S. 2821 (and hence it contained many provisions from S. 1375, because those sections had provided the foundation of S. 2821). In addition, Division K included sections that derive from S. 1977, the Small Manufacturers Assistance, Recovery, and Trade ("SMART") Act, introduced by Senator Snowe on November 25, 2003.

B. ACCESS TO CREDIT FOR SMALL BUSINESSES

Small businesses consistently mention access to affordable credit as one of their primary concerns. The SBA has several financing programs that seek to help small businesses obtain the credit that the businesses need to operate, grow, and hire more employees.

Through the Small Business Investment Company (SBIC) program the SBA guarantees up to 66 percent of the financing of approximately 443 SBICs, which are venture capital firms that must invest all of their funds into small businesses. The SBICs obtain a portion of their funds from private investors and then obtain the SBA-guaranteed portion of their funds either through the sale of securities (in the Participating Securities SBIC program) or through the sale of debt (in the Debenture SBIC program).

In the 7(a) Business Loan Guaranty Program, which is organized under Section 7(a) of the Small Business Act, the SBA guarantees a portion of a loan that a commercial lender makes to a qualified small business (the guaranteed portion is 50 percent, 75 percent, or 85 percent of the total loan value, depending on the type of loan). Loans may be up to a maximum of $2 million, and the maximum guarantee is $1 million. To receive a 7(a) loan a small business must be unable to obtain comparable credit elsewhere from a non-SBA loan. Loans made under this program are most often for working capital, real estate, expansion, or other business expenses.

In 2004, the SBA guaranteed 76,143 7(a) loans, with a total value of approximately $12.5 billion. This was an increase of 23 percent over the 2003 total of 61,832 loans, for a total of $11.2 billion. The 7(a) program has several sub-programs or pilot programs in which loans have different features and are designed to respond to different types of financing needs. In the 7(a) Express pilot program, loans receive only a 50 percent guarantee and must be $350,000 or less, but the loan application is simpler than an application for a general 7(a) program loan. In 2003, 30,562 loans were made in the Express program, and in 2004 the number of Express loans increased by 39 percent to 42,458 loans.

One important sub-program within the 7(a) program is the International Trade Loan Program, in which small businesses can receive slightly larger guarantees, up to a maximum of $1,750,000, for loans that either support international trade or respond to competition from overseas competitors. In 2003, 1,583 loans were made in the International Trade Loan Program, and in 2004 the number of this type of loan increased by 38 percent to 2,177 loans.

In the Certified Development Company (CDC) loan program, also known as the 504 Loan Program (it is organized under Section 504 of the Small Business Investment Act of 1958), the SBA guarantees 40 percent of a financing package supplied to a small business to purchase either real estate or capital equipment. To obtain a 504 loan, a small business works with a CDC, a non-profit community development organization, to construct an appropriate financing package. The CDC provides a loan for 40 percent of the total financing package, and the SBA guarantees 100 percent of this portion of the total package; a commercial bank, separate from the CDC, provides a commercial loan that funds 50 percent of the financing package, and the SBA guarantees no portion of this commercial loan. Finally, the small business is required to contribute 10 percent of the total financing package. In Fiscal Year 2003, 5,542 loans were made in the 504 loan program, for a total of $3.14 billion, and in 2004 the program increased in size by 26 percent, with 7,769 loans being approved, for a total of $3.9 billion, according to the SBA.

One focus of the SBA during the 108th Congress was to increase the number of SBA-guaranteed loans made to minorities and to women. From 2003 to 2004, among women and minority entrepreneurs, total 7(a) and 504 loan volumes increased by 27 percent. In 2003, women entrepreneurs received 14,221 SBA loans. In 2004, the numbers increased by 25 percent to 17,829 SBA loans. The increase was dramatic among loans to minorities as well. In 2003, African Americans received 3,482 SBA loans. In 2004, the number increased by 30 percent to 4,530 SBA loans. In 2003, Hispanics received 5,525 SBA loans. In 2004, the number increased by 30 percent to 7,157 SBA loans. In 2003, Asian Americans received 8,743 SBA loans. In 2004, the number increased by 30 percent to 11,349 SBA loans. In 2003, Native Americans received 737 SBA loans. In 2004, the number increased by 2 percent to 753 SBA loans.

In order to improve the SBA programs, Chair Snowe included in S. 1375 and in the Omnibus Appropriations Bill many provisions that would enhance the accessibility, attractiveness, and convenience of the financing programs for small business borrowers and for lenders. Of particular note is a provision that increased the maximum loan size for 504 loans, so as to allow small businesses, especially those in manufacturing that wish to purchase expensive machinery, or those located in regions in which real estate prices have increased dramatically, to obtain larger loans that reflect the increased costs of doing business.

C. SMALL BUSINESS REVITALIZATION ACT (S. 2193)

The ability of small businesses to access credit through the SBA's 7(a) program during Fiscal Year 2004 was hampered by a funding shortfall in the program. During Fiscal Year 2003 approximately $11.2 billion in 7(a) loans were approved (when $1.8 billion in STAR loans are included). The SBA's budget request for Fiscal Year 2004 was only for a program size of $9.3 billion, a reduction of almost $2 billion from the previous year. The SBA's Administrator, Hector Barreto, testified at the Committee's June 4, 2003 hearing on the SBA's Budget request for Fiscal Year 2004. In response to questioning from Chair Snowe regarding the potential inadequacy of the SBA's budget request for the 7(a) program, Mr. Barreto testified that the Administration felt its budget request would be sufficient to meet demands in the 7(a) program, both for large loans and for small loans. Moreover, at the Committee's April 30, 2003, roundtable on the 7(a) program, the SBA representative, the employee responsible for administering the SBA's Office of Capital Access, which manages the 7(a) program, assured the Committee that the Agency was confident that its Fiscal Year 2004 budget request was sufficient, even though 7(a) lenders at the roundtable insisted the demand would be much greater than the requested budget could finance.

On the express assurance of Administrator Barreto and the SBA, therefore, the appropriations bill that Congress enacted for Fiscal Year 2004 contained only enough funds for a 7(a) program of up to $9.55 billion in loans (in fact, the SBA had requested only enough funds to provide for a program of $9.3 billion, but Congress allocated more than was requested, thus allowing a program of $9.55 billion). Congress appropriated $79 million to the SBA for 7(a) guarantees in Fiscal Year 2004, and also allowed the SBA to carryover from Fiscal Year 2003 to Fiscal Year 2004 $22 million in funds and to apply the carried-over funds to 7(a) guarantees in the latter year. With this total amount of $101 million, and with a subsidy rate at the beginning of Fiscal Year 2004 of 1.06 percent, the program began the year with a total capacity of $9.55 billion. In Fiscal Year 2004, however, demand continued at the same pace it had reached in Fiscal Year 2003; thus, it was immediately clear that demand would outstrip available resources in the program, notwithstanding the SBA's predictions.

On December 23, 2003, the SBA informed the Senate and House Small Business Committees that the SBA would be instituting a $750,000 cap for 7(a) loans, effective January 8, 2004. The SBA informed the Committees on Tuesday, January 6, that the SBA was immediately shutting down the 7(a) loan program, for an undetermined amount of time.

On January 8, 2004, Chair Snowe sent a letter to Administrator Barreto in which she noted that the SBA had provided notice to the Committee on December 23, 2003, of its intention to impose a cap on 7(a) loans as of January 8, 2004. This notice of December 23, 2003 was required under Section 7(a)(24) of the Small Business Act, which provides that the SBA must notify the Committee at least 15 days before "making any significant policy or administrative change affecting the operation of the loan program under this subsection." The letter of January 8, 2004 noted that the SBA had violated this statutory requirement by shutting down the program on or around January 5, 2004. Chair Snowe also noted that, while regrettable, the violation should not stand in the way of an immediate resumption of the program.

The SBA stated that between 500 and 1,000 loan applications were rejected because of the shutdown, with a total value of approximately $1 billion. Of these applications, approximately 250 were for loans larger than $750,000. The SBA sent these applications back to the small businesses that submitted them, and told the small businesses to re-submit the applications when the program re-opened. Those applications above $750,000 were then rejected by the SBA. Thus, at least 250 small businesses had loan applications rejected simply because the SBA moved the deadline for larger loans forward by several days.

The SBA claimed that it was required to shut the program down because the OMB would not allow the SBA to exceed $3.33 billion in 7(a) loan guarantees by January 31, 2004 until appropriators authorized additional funds. The SBA stated that, as of December 22, 2003, it had already approved $2.8 billion in 7(a) loan guarantees since the beginning of Fiscal Year 2004, and that between December 23, 2003, and early January 2004, it had received more than $500 million in applications, putting the program at the level of $3.33 billion at the beginning of January.

After the SBA reopened the 7(a) loan program on January 14, 2004, following its temporary shutdown, the SBA prohibited any loans larger than $750,000, instead of the normal $2 million, and prohibited "piggyback" loans, which combine commercial and 7(a) portions.

Small businesses and lenders stated to the Committee that the loan restrictions significantly hindered the ability of small businesses to obtain sufficient capital, and they expressed their strong desire to remove the loan restrictions.

In spring 2004 the SBA submitted a legislative proposal to Congress that, if enacted, would have given the SBA the authority to annually set the fees in the 7(a) program and to set the guarantee rates for 7(a) loans, i.e., the percentage of each loan that is guaranteed. Currently, a 7(a) loan of any size (normally, up to $2 million, if no additional loan cap is in place) may have a 75 percent guarantee, and loans of up to $350,000 can be made either at a 75 percent guarantee or a 50 percent guarantee. Loans of $150,000 or less may have a guarantee of up to 85 percent. The 50 percent guarantee loans are "SBA Express" loans.

SBA personnel explained that, although the details were not specified in the SBA's proposed legislation, the SBA would phase-in a requirement that, by FY 2007, every 7(a) loan would have to be made with a 50 percent guarantee (e.g., as SBA Express loans). The SBA would also increase fees for lenders and borrowers, at the SBA's own discretion, to give the 7(a) program a zero subsidy.

The Committee believed the language the SBA provided was significantly flawed because, among other things, (1) the SBA would have unfettered authority to set fees and guarantee rates; (2) small businesses with lesser credit quality could be excluded from the program by the lower guarantee percentage; and (3) the 15-day notice provision would be eliminated, so that the SBA would have no requirement to notify Congress.

Lenders use Express loans, with a 50 percent guarantee, primarily for loans of under $100,000; like credit card loans, these loans can be made by the lenders by reference to the borrower's credit score, rather than an evaluation of the borrower's collateral. Collateral is generally used for larger loans, which therefore are not made based on credit scores. The evaluation of collateral make the larger loans more work-intensive for lenders. Thus, lenders generally do not use Express for loans larger than $100,000.

Lenders informed the Committee that, if the SBA were to require that all loans up to $2 million were made at a 50 percent guarantee, the lenders would generally not make loans larger than $100,000, except for the small businesses with the best credit. The lenders stated that changing the guarantee rate from 75 percent to 50 percent would exclude a large number of small businesses, those with lesser credit quality or those that are just starting and do not have a credit history, from the program.

The Committee held a roundtable meeting of approximately 25 representatives of small businesses and lenders on February 25, 2004, to discuss the SBA's proposal. Every participant at the meeting, except the SBA, expressed concerns about the SBA's proposal. Some of these were strong objections: the representatives of community bankers stated that the proposal would be a "nonstarter" for the 5,000 U.S. community banks, and the American Bankers Association and other 7(a) lenders, represented by the National Association of Government Guaranteed Lenders (NAGGL), also stated that they were strongly opposed to the SBA's proposal. The small business representatives, especially the U.S. Chamber of Commerce, stated they were opposed to the proposal. No participant in the meeting, other than the SBA, supported the SBA's proposal.

In response to the loan cap that the SBA had established, and to the prohibition on piggyback loans, Chair Snowe introduced a bill, the "Small Business Loan Revitalization Act," (S. 2193), on March 10, 2004, to adjust fees paid by lenders so as to allow the remaining appropriated funds in the 7(a) program to be used to fund an increased program size for the remainder of Fiscal Year 2004. Instead of a program size of $9.55 billion, S. 2193 would have allowed the 7(a) program to have a maximum size of approximately $12.5 billion for the year. An almost identical bill, H.R. 4062, was introduced in the House on March 30, 2004. S. 2193 was not passed in the Senate, so after H.R. 4062 was passed in the House on March 31, 2004, Chair Snowe called up H.R. 4062 for consideration in the Senate, and it was passed by the unanimous consent of the Senate on April 1, 2004. After being signed by President George W. Bush, it became law on April 5, 2004. The new law allowed the 7(a) program to have a program size of $12.5 billion for Fiscal Year 2004, and allowed the $750,000 loan cap to be removed, and piggyback loans to be permitted. Until January 2004, the SBA had permitted piggyback loans, but had never charged an additional fee for those loans. H.R. 4062 re-instituted piggybacks and, for the first time, imposed an additional fee that applied to piggybacks.

D. OTHER EFFORTS TO IMPROVE SMALL BUSINESSES' ACCESS TO CAPITAL

Chair Snowe, along with Senator Bond and Senator Pryor, also introduced a bill to improve small businesses' access to credit by increasing the amount of financing available to small businesses, and by improving the terms of the financing that is available. This bill, the "Small Business Credit Liquidity Act of 2003" (S. 1713), was introduced on October 3, 2003. The bill would have allowed the SBA to examine whether it wished to develop a program to authorize private-sector loan poolers to pool small business loans and securitize the loans. The loans thus pooled would not have been loans that already had partial or full SBA guarantees; they would have been made, originally, outside of the SBA's own loan and venture capital programs.

In addition, the bill specifically noted that it was not requiring the SBA to implement such a program, but was merely authorizing the SBA to examine the feasibility of such a program, and to report back to Congress before implementing any such program. If the SBA wished, it could then implement a program to achieve these goals. The use of Federal appropriations to fund any such program was specifically forbidden by the legislation; any such program would have had to have been self-supporting, through fees charged in the program.

This proposal was first suggested by the SBA in its Budget Proposal for Fiscal Year 2004, but after provisions allowing the SBA to examine the possibility of beginning such a program were included in S. 1375, the SBA switched course and opposed the idea (in other words, the Agency opposed even being given the authority to examine the issue). The provision was removed from S. 1375 before S. 1713 was introduced. S. 1713 was referred to the Committee, but was not passed during the 108th Congress.

Chair Snowe and Senator Hagel introduced S.1967, the "Interest on Business Checking Act of 2003", on November 25, 2003. This bill would have allowed financial institutions to pay interest on business checking accounts, which has been prohibited since the Great Depression. It would have benefited small businesses, who currently do not receive interest for the funds they hold in checking accounts, and would also have benefited small depository institutions, which would be better able to compete with larger depository institutions.

The bill did not progress through the Senate Banking Committee during the 108th Congress, but the House approved, by a 418–0 vote, an amendment to H.R. 1375, a regulatory-reduction bill in the House, that was almost identical to the text of S. 1967.

E. THE SBA'S ACCOUNTING ISSUES

The General Accounting Office (GAO), which is now named the Government Accountability Office issued a report in January 2003 ("Small Business Administration: Accounting Anomalies and Limited Operational Data Make Results of Loan Sales Uncertain") that identified serious deficiencies in the SBA's accounting for its sales of loans. These accounting problems affected more than just the loan sales; because the SBA did not properly account for the loans that had been sold in the sales, or for the Agency's loan loss reserve accounts, many of the Agency's financial accounts were inaccurate.

After the GAO's report identified errors in the SBA's accounting, the SBA's outside auditors, Cotton & Co., admitted that their audit opinions regarding the SBA for fiscal years 2000 and 2001 might be "materially incorrect." Cotton & Co. withdrew their prior certification that the SBA's accounting was satisfactory, or accurate, for those two fiscal years. The SBA hired outside consultants to analyze the SBA's accounting errors.

Chair Snowe, along with Rep. Todd R. Platts, the Chairman of the House Subcommittee on Government Efficiency and Financial Management, Rep. Edolphus Towns, the Ranking Member of that Subcommittee, and Rep. Marsha Blackburn, the Vice-Chair of that Subcommittee, sent a letter to the GAO on May 21, 2003 concerning the SBA's loan sales program. The letter asked that the GAO, in light of its report on the loan sales, summarize the recommendations provided to the SBA by the outside consultants, assess whether the recommendations would be likely to result in reliable subsidy cost estimates for the SBA's accounts, determine whether the SBA was implementing the recommendations, and provide quarterly reports on the SBA's progress in fixing its accounting problems until such time as the SBA and the GAO "agree that all necessary corrective measures have been effectively implemented."

In late July 2003, the SBA requested that the GAO delay the beginning of its study until "late August/early September 2003" because pertinent SBA personnel were occupied with other tasks. Along with the other requestors of the study, Chair Snowe reluctantly granted this request because the duration of the delay was not substantial and the SBA insisted that its accounting personnel were too busy to work with the GAO at that time.

In October 2003 the SBA requested that the start of the GAO's study be delayed again until December 1, 2003. The SBA stated this further delay was necessary because SBA's accounting personnel were occupied working on preexisting tasks, including the Fiscal Year 2003 financial statements, Fiscal Year 2005 budget, the migration of the agency's financial accounting system to a new contractor, and three other GAO studies (of the SBA's loan monitoring system, 7(a) loan program econometric model, and workforce transformation).

The House Subcommittee members agreed to delay the GAO study until, at the latest, December 1, 2003, so long as the SBA committed to allow the GAO full access to SBA personnel and documents. On November 20, 2003, the SBA informed the GAO that it did not intend to provide the GAO access to SBA accounting documents and personnel until after the OMB had approved the new disaster loan accounting model, which would not be until January 2004.

As a result, Chair Snowe wrote Mr. Barreto on November 24, 2003 stating that the GAO study (first requested in May 2003) was essential to Congress's decision-making responsibilities, and requesting that the study be allowed to begin immediately.

The SBA did not immediately reply to the letter, but in early January 2004 the SBA insisted that delaying GAO's commencement of the study until January 2004 was necessary because the new disaster loan models would not be completed and approved by the OMB until then. The SBA denied that the earlier requests for delays, in July 2003 and October 2003, were because SBA personnel were "too busy" at that time; the SBA claimed that its earlier requests to Congress for delays were based upon the financial models not being ready yet. The GAO continues to work with the SBA to examine these accounting issues.

F. GOVERNMENT-WIDE AUDIT ISSUE, AND GAO AND CBO REPORTS

The GAO is required to do a government-wide audit of all agencies each year, and its audit of the SBA was delayed many times in 2003 and 2004 by the SBA's refusal to allow the GAO access. After discussions with the Committee, the SBA agreed to provide more access to the GAO, and the latter completed its audits for 2003 and 2004.

On July 22, 2003, Chair Snowe sent a letter to David M. Walker, the Comptroller General, requesting that the GAO conduct a study of the SBA's contract with Dun & Bradstreet regarding the monitoring of the SBA's loan portfolio. To improve its ability to monitor its 7(a) and 504 loan portfolios, the SBA awarded a contract to Dun and Bradstreet, in association with Fair Isaac Corporation, to provide information from a computer-based loan monitoring system. The SBA's monitoring of potential risks associated with its loan portfolios and its management of information technology are both critical in ensuring that the SBA's primary business loan programs are fulfilling their intended goals of providing credit to eligible small businesses, and in ensuring that SBA lending partners follow lending requirements.

In a December 2002 report (Small Business Administration: Progress Made but Improvements Needed in Lender Oversight, GAO–03–90, Dec. 9, 2002), the GAO reported that the SBA needed to improve its lender oversight process to adequately measure the financial risk lenders pose to the SBA. In discussions with Committee staff in April 2003 about the status of the SBA's response to the GAO's recommendations for improvements in information technology management, the GAO reported that the SBA had decided to revise its approach to loan-monitoring after dedicating several years of effort and approximately $12.7 million towards development of an in-house loan monitoring information system.

In her July 2003 letter, Chair Snowe requested that the GAO conduct a study of the SBA's contract with Dun and Bradstreet in order to determine (1) what data is necessary to adequately monitor the 7(a) and 504 loan portfolio, (2) how the SBA intends to achieve the goal of developing or obtaining information that will meet the agency's needs, (3) the extent to which the contract addresses the SBA's longstanding data integrity problems, (4) to what degree the contract will improve the SBA's loan monitoring capability, and (5) how closely the SBA's intended future loan monitoring capability will resemble best practices of private U.S. banks.

The GAO analyzed these issues and completed its report in June 2004 (Small Business Administration: New Service for Lender Oversight Reflects Some Best Practices, but Strategy for Use Lags Behind, GAO–04–610). The GAO determined that the new loan monitoring system would be comparable in quality to those used in the private sector, but that the SBA had not yet developed comprehensive plans for utilizing the system to improve and monitor SBA programs. The SBA responded that it was still in the process of developing those plans. The Committee is continuing to work with the Agency on this vital issue.

On October 30, 2003, Chair Snowe sent a letter to Dr. Douglas Holtz-Eakin, the Director of the Congressional Budget Office (CBO), requesting that the CBO conduct a study on the effect on small businesses of the call-up to active duty of military reservists who are employees of small businesses. This is an issue of significant importance to thousands of small businesses, who may have lost their owners, managers, or key employees because those persons were reservists who were called up to active duty. The CBO is still conducting the study, and the Committee will examine its findings when the study is completed.

In October 2004, Chair Snowe and Senator Enzi requested that the GAO begin a study of the effects on small businesses of the Sarbanes-Oxley Act. The GAO has not yet completed the study, which will examine whether there have been positive and/or negative developments for small business accounting practices, costs, and access to capital as a result of the Sarbanes-Oxley Act.

G. SBIC PROGRAM

Small Business Investment Companies (SBICs) provide equity investments, long-term loans, and management assistance to small businesses. SBICs are privately owned and managed, investing in small businesses with the prospect of sharing in the profits as they grow. SBICs may be financed either by the sale of equity securities (Participating Securities) or debt instruments (Debentures). To be licensed by the SBA, each SBIC must raise private capital. The SBA then matches the private capital with government-guaranteed capital, by guaranteeing the SBIC's sale to investors of equity securities (or bonds, in the case of debenture SBICs). The SBIC program is a zero-subsidy program; the fees charged to SBICs pay for the SBA guarantees.

The SBIC program began in 1958, and has been a major contributor to the venture capital industry in the United States. SBIC investing peaked in 2000 at $5.4 billion, but then declined to $4.5 billion in Fiscal Year 2001, $2.7 billion in Fiscal Year 2002, $3.5 billion in Fiscal Year 2003, and $2.6 billion in Fiscal Year 2004. The decrease in SBIC investments during this period is less drastic than the decrease in private venture capital investments over the same period, and thus the relative importance of SBIC investments in the venture capital field is greater now than during the late 1990s. The SBA has estimated that one job is created for every $36,000 invested in a small company under the SBIC program. There are currently approximately 443 SBICs nationwide.

Since its beginning in FY 1994, the Participating Securities SBIC program has had impressive results: More than $4.7 billion in private capital has been raised by the 221 privately managed Participating Securities funds, and more than $7.4 billion has been invested by Participating Securities funds in U.S. small businesses during the period.

In 2004 the SBA indicated that the Administration's projections for the future of the Participating Securities SBIC Program (but not the Debenture SBIC Program) predicted that the program would operate at a substantial loss for the Government. These projections were based upon the program's past performance and the economic events of the period 1994–2004; they may also have contained some predicted results for the performance of SBICs in the future. The SBA indicated that this projected loss could exceed $1 billion. In response to this expectation, the SBA submitted to Congress a legislative proposal to change the Participating Securities SBIC program by increasing the fees charged to SBICs, and increasing the government's share of an SBIC's profits. In a series of meetings, representatives of SBICs strongly opposed the Administration's proposal, arguing that it would effectively end the program by rendering it completely unpalatable for venture capitalists.

On June 25, 2004, Chair Snowe and Senator John Kerry sent a letter to SBA Administrator Hector Barreto that contained draft legislative text regarding the SBIC program. The legislative proposal, which was constructed by SBICs and suggested to the Committee, would have amended the Small Business Investment Company Act of 1958, under which the SBIC program is organized, and would have increased the SBA's profit participation in the SBIC program by promising the SBA a profit participation in each SBIC equal to the percentage of financing in that SBIC that the SBA had contributed. The Senators requested a section-by-section analysis of the draft legislation.

On July 8, 2004, Ronald E. Bew, the SBA's Associate Deputy Administrator for Capital Access, sent Chair Snowe and Senator Kerry a letter stating that, in the SBA's view, the draft legislation did not satisfy the requirements of the Credit Reform Act and, if the draft legislation were to satisfy that Act, it would have a positive subsidy rate of approximately 21%. Mr. Bew's letter also contained a statement, without explanation, indicating that the proposed draft legislation would "shift" a budgetary cost from the U.S. Treasury to the SBA.

On July 12, 2004, Chair Snowe and Senator Kerry sent another letter to Administrator Barreto requesting that Mr. Barreto explain in more detail the SBA's conclusion that the draft legislation sent on June 25, 2004, did not satisfy the Credit Reform Act of 1990, and how, in contrast, the current law governing the program does satisfy that Act. The senators also reiterated their request for a section-by-section analysis of the draft legislation. The letter also asked that the SBA identify what aspect of the proposed draft legislation would "shift" a budgetary cost from the U.S. Treasury to the SBA. Finally, the letter asked the SBA to explain in greater detail the manner in which the SBA calculated that the draft legislation, if scored under the credit reform standards as debt, would still have an estimated subsidy rate of 21%. The letter requested a reply by July 19, 2004.

On July 27, 2004, Chair Snowe, Senator Kit Bond, Senator Judd Gregg, Senator James Talent, and Senator Norm Coleman sent a letter to Joshua Bolten, Director of the Office of Management and Budget (OMB), regarding the SBIC program. The letter noted that the private investment community, the Administration, and Congress all agree that the program needs a legislative solution. The letter also mentioned that the private sector participants in the program had testified before Congress in opposition to the Administration's proposal, and had indicated that the flow of private capital into the program would stop if the Administration's recommended changes were enacted. The Senators stated that they are attempting to construct an alternative approach that would achieve the following objectives: (1) maintain incentives necessary to continue to attract private investment in SBICs; (2) eliminate taxpayers' exposure by maintaining a zero subsidy rate for the program; and (3) maintain strict licensing procedures to ensure only qualified venture capital managers are allowed to participate. The Senators requested that the OMB engage with congressional staff and industry representatives in the effort to design legislation to improve this program. Subsequently, OMB personnel have communicated with Congressional staffers regarding the program, and that process is still on-going.

H. OVERSIGHT OF THE 7(A) PROGRAM

On September 9, 2004, Chair Snowe sent a letter to Administrator Barreto requesting he provide her with (1) information regarding an email that was apparently sent in late August 2004 from the District Director of the SBA's San Diego District Office, as well as the Deputy District Director and the chief loan officer in that District Office, to many of the lenders participating in the 7(a) loan program in that region; and (2) information regarding any similar messages that might have been sent in other SBA Districts. The email sent to lenders encouraged lenders to submit as many 7(a) loan applications during Fiscal Year 2004 as possible, and mentioned that in order to find additional applications to submit lenders might wish to consider changing the credit thresholds the lenders used to determine loan applicants' eligibility for loans. The letter requested that Mr. Barreto examine the circumstances under which the SBA officials sent the email to lenders, and also asked

Mr. Barreto to determine whether other SBA district offices had made similar communications to lenders in other regions. Chair Snowe requested a reply by September 15, 2004.

On September 14, 2004, Donald R. Swain, the Director of the SBA's Executive Secretariat, sent Chair Snowe a letter informing her that the SBA expected to reply to her inquiry "fully within 14 days." Administrator Barreto sent Chair Snowe a letter on October 8, 2004, informing her that the messages in the August 2004 email to lenders were not in conformance with SBA policy, and that the SBA had informed the employees in question that they should refrain from such messages.

III. TAX ISSUES

A. SMALL BUSINESS EXPENSING

The Committee was extremely active throughout the 108th Congress in terms of improving the ability of small businesses to deduct more of their costs in acquiring capital used in their business in the year of purchase. On January 14, 2003, Chair Snowe introduced S. 158, The Small Business Expensing Act of 2003. In short, this bill would have extended the then $25,000 expensing limit to $75,000 and the then $200,000 phase-out to $325,000. The bill would have made the changes permanent.

Although never passed, this bill played a large role in the small business expensing modifications that were included in the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA), which Congress passed and the President signed on May 30, 2004. JGTRAA provided that the $25,000 expensing limit would be increased to $100,000 and the $200,000 phase-out would be increased to $400,000.

These increases, however, became effective only until the end of tax year 2005. As such, absent further legislation, the levels would revert back to their respective $25,000 and $200,000 amounts beginning in 2006.

On October 22, 2004, the President signed H.R. 4520. One of the measures included in that bill is a provision to extend the expensing limits enacted by JGTRRA for an additional two years. Accordingly, the current $100,000 expensing limit and $400,000 phase-out will remain in effect through the end of tax year 2007.

Chair Snowe also offered an amendment to the Senate version of H.R. 4520 (S. 1637) during the Finance Committee mark-up that would have modified the small business expensing rules. This amendment would have changed the rate upon which the taxpayer's expensing amount would phase-out to allow more companies to qualify. Currently, the taxpayer's expensing benefit phases-out dollar-for-dollar, but Chair Snowe's amendment would have altered that rate so that the amount that would otherwise qualify for expensing would be phased-out by only one half of the amount by which the cost exceeds the phase-out limit. Although this amendment was included in the Senate's bill, it was not included in the Conference Report.

B. MODIFICATION OF THE UNRELATED BUSINESS TAXABLE INCOME RULE

On April 10, 2003, the Committee introduced S. 885—The Small Business Investment Company Act of 2003. This bill would have amended the unrelated business taxable income rules to provide that tax-exempt entities would not be subject to paying unrelated business taxable income from investments made in debenture small business investment companies.

Although Congress never passed S. 885, Chair Snowe was successful in including the provisions in the Senate passed version of H.R. 4520. The Conference Report to H.R. 4520 (P.L. 108–357) contained a modified provision to address the problem. In general, the measure contained in H.R. 4520 modifies the debt-finance property provisions in the unrelated business taxable income rules in the code by excluding from the definition of acquisition indebtedness any indebtedness that a small business investment company licensed under the Small Business Investment Act of 1958 that is evidenced by a debenture issued by such company under section 303(a) of such act and held or guaranteed by the Small Business Administration. The exclusion will not apply, however, if any exempt organization owns more than 25 percent of the capital or profits interest in the small business investment company, or exempt organizations own, in the aggregate, 50 percent or more of the capital or profits interest of the small business investment company. This exclusion applies to small business investment companies licensed after October 22, 2004.

C. MANUFACTURING TAX DEDUCTION

H.R. 4520 provides an income tax deduction that domestic manufacturers are able to claim in order to increase their competitiveness abroad. The deduction is from taxable income (or, in the case of an individual from adjusted gross income) that is equal to a portion of the taxpayer's qualified production activities income. For taxable years beginning after 2009, the deduction is equal to nine percent of the lesser of (1) the qualified production activities income of the taxpayer for the taxable year, or (2) taxable income (determined without regard to this provision) for the taxable year. For taxable years beginning in 2005 and 2006, the deduction is three percent of income, and the deduction is six percent of income for taxable years beginning in 2007, 2008, and 2009. The deduction is limited, however, to 50 percent of the wages that the taxpayer pays during the calendar year that ends in such taxable year.

Chair Snowe worked diligently both during the Senate Finance Committee mark-up as well as during the Conference negotiations to ensure the deduction would not be limited to only certain types of entities. The deduction enacted under H.R. 4520 is not entity-specific and applies to those manufacturers that pay wages. Consequently, not only are corporations eligible to claim the deduction, but so too are shareholders in a sub-chapter S corporation eligible for the deduction as well as partners in a partnership.

D. MODIFICATIONS TO THE NEW MARKETS TAX CREDIT

The Committee was extremely influential in modifying the application of the new markets tax credit program in terms of making it accessible than more taxpayers than under current law.

Specifically, Chair Snowe worked as a conferee to H.R. 4520 to modify the low-income test for high migration rural counties. As provided under the bill, in the case of a population census tract located within a high migration rural county, low income is defined by reference to 85 percent (rather than 80 percent) of statewide median family income. For this purpose, a high migration rural county is any county that, during the 20-year period ending with the year in which the most recent census was conducted, has a net out-migration of inhabitants from the country of at least 10 percent of the population of the county at the beginning of such period.

E. CASH METHOD OF ACCOUNTING (S. 2675)

On July 15, 2004, Chair Snowe introduced S. 2675 to expand the availability of the cash method of accounting for small businesses. Currently, the general rule under the tax code is that only those small businesses that generally earn less than $5,000,000 in annual gross receipts are able to use the cash method of accounting in determining their federal income tax liability. Chair Snowe's bill would increase this threshold to $10,000,000.

Chair Snowe's bill also permits those taxpayers that have inventory to potentially qualify for the cash method of accounting. Currently, if a taxpayer otherwise satisfies the requirements for using the cash method of accounting but also has inventory in its business, it cannot use the cash method. Chair Snowe's bill provides an exception for those taxpayers that have inventory by permitting them to account for those costs as if they are an incidental material supply, which is a standard that exists under current law.

F. INVESTIGATION OF THE TAX CODE

Chair Snowe, in her role as Committee Chair requested several GAO reports related to the tax code. One report reviewed the Internal Revenue Service's management of its Schedule K–1 Document Matching program, which the IRS began in 2002 to compare the information that certain tax flow-through entities, such as partnerships and S-corporations, provide on their IRS form K–1 to what their respective owners report on their individual income tax returns. Regrettably, during the first year of this program, a significant number of taxpayers received notices from the IRS questioning the accuracy of their reported income and requiring them to prove that they had, indeed, filed their returns correctly.

In light of these problems, Chair Snowe and Senator Bond requested that the GAO determine the extent to which this program burdened compliant taxpayers and the steps that the IRS should take to improve the program. The GAO report, entitled "Changes to IRS's Schedule K–1 Document Matching Program Burdened Compliant Taxpayers" (GAO–03–667), explains that although the IRS intended originally to focus on only two categories of income that are easily identified on tax returns, namely interest and dividends, the IRS determined during the testing of the program that this approach was not optimal because it could not separate under-reported K–1 interest and dividend income from the other underrreported income such as the income that banks pay. Because the IRS expanded the matching program to cover additional categories of income and in the process thereof sent thousands of under-reporting notices to thousands of taxpayers who were eventually found to have met their tax obligations, the report concluded that the expansion of the matching program created an unnecessary burden for those compliant taxpayers and that this expansion also reduced the IRS' already limited enforcement resources.

Although encouraged that the IRS recognized the shortcomings in implementing the matching program for 2002 and took steps towards improving the program's efficiency and accuracy for 2003, Chair Snowe and Senator Bond wanted to ensure that the IRS continued to implement the suggestions and conclusions made in the Report. Accordingly, Chair Snowe and Senator Bond sent a letter to IRS Commissioner Everson on July 9, 2003 to applaud the IRS for its work in this area and stress the importance of acting on the GAO's conclusions.

Chair Snowe and Senator Bond also requested a GAO report that reviewed the Workforce Planning initiative within the Taxpayer Education and Communication Unit (TEC) of the IRS. The purpose of this Report (GAO–03–711) was to determine whether the IRS has begun to develop a strategic workforce plan for TEC that incorporates the critical elements that should be in a typical workforce plan and to determine how the IRS should proceed with the plan's development.

The Report concluded that while both the IRS and the Small Business/Self-Employed (SB/SE) division have begun to develop this strategic workforce plan, TEC, since its inception in October 2000, has operated with a short-term staffing plan that does not meet the critical elements for what a strategic workforce plan should include.

Concerned with this conclusion, Senators Snowe and Bond sent a letter to IRS Commissioner Everson and IRS SB/SE Commissioner Hart on July 18, 2003. While the letter commended the IRS for recognizing the need to develop and institute a strategic workforce plan for TEC, it stressed the importance of implementing the GAO's recommendations concerning the plan's element for a proper strategic workforce.

An additional GAO Report that Chair Snowe requested focused on the compliance burden that the Federal tax system imposes on small businesses and the self-employed. Chair Snowe made this request because of her interest in alleviating any unnecessary burden that federal tax requirements impose on small businesses.

The GAO's report (GAO–04–304) concluded that the expenses that small businesses reported on schedules C and F of their tax returns varied widely across and within expense categories for tax year 2001. Specifically, the Report concluded that there was a wide variation in both median dollar amounts and ranges of the expenses, and the expenses varied greatly within the categories of expenses, such as the expenses for wages that taxpayers reported on Schedule C.

The final GAO report that Chair Snowe requested focused on the substantiation of business expenses by small business taxpayers and whether changing the rules that taxpayers must follow in meeting their tax obligation would actually improve taxpayer compliance.

G. NOTIFICATION TO SMALL BUSINESSES OF ERRONEOUS ALTERNATIVE MINIMUM TAX (AMT) PAYMENTS

On May 29, 2003, Chair Snowe sent a letter to Commissioner Everson regarding the number of small corporate taxpayers that erroneously paid the Alternative Minimum Tax (AMT). The letter stemmed from a report that the Treasury Inspector General for Tax Administration (TIGTA) issued titled "Significant Actions Were Taken to Address Small Corporations Erroneously Paying the Alternative Minimum Tax, but Additional Actions are Still Needed" (Reference Number 2003–30–114). In general, the Report concludes that the IRS failed to contact all of the small corporations that erroneously paid the corporate AMT in 2001 and failed to identify those taxpayers that might have erroneously paid the corporate AMT for tax periods after November, 2000.

Chair Snowe's letter stressed the necessity of improving this oversight. For example, many of these small corporations likely have a limited cash flow—meaning they could have reinvested this tax liability that they were not required to pay into their business rather than with the Federal Government. Moreover, subjecting these taxpayers to the AMT imposes additional administrative costs and burdens that otherwise would not have been required. Consequently, Chair Snowe urged Commissioner Everson to implement the recommendations of TIGTA's report to ensure that small corporations that erroneously paid the AMT are notified of their mistake and issued a prompt refund.

IV. WOMEN'S BUSINESS CENTER

According to the Center for Women's Business Research, in 2004 there were 10.6 million women-owned businesses, generating almost $2.5 trillion in revenues and employing more than 19 million Americans. With women entrepreneurs making significant contributions to the economy and growing at twice the rate of all other firms, Chair Snowe wanted to ensure that programs such as the SBA's Women's Business Center program continued to help these women succeed. During the 108th Congress, she introduced three bills related to improving programs and services for women in small business.

In addition, Chair Snowe sent several letters to Administrator Barretto in an effort to resolve the funding shortfall with the Women's Business Center Program.

A. WOMEN'S SMALL BUSINESS PROGRAMS IMPROVEMENT ACT OF 2003

On May 23, 2003, Senator Snowe, along with Senators Bond and Burns introduced S. 1154, the Women's Small Business Program Improvement Act of 2003. This bill was designed to improve the programs and services that the SBA delivers across the nation for women business owners through the Office of Women's Business Ownership, the Women's Business Centers Program, the National Women's Business Council, and the Interagency Committee on Women's Business Enterprise. The bill provided consolidation, direction and integration of existing programs that have previously been created to offer opportunities for women through their entrepreneurial endeavors. Additionally, the bill made the Women's Business Center Program a permanent program for existing eligible Centers so that women can depend on the experienced services of long-term counseling and small business education and training. These Centers have proven to be a great value to the communities they serve and this bill ensures that these programs and services continue to be available.

B. WOMEN'S BUSINESS CENTER PRESERVATION ACT OF 2003 (S. 1247)

On June 12, 2003, Chair Snowe introduced S. 1247, the Women's Business Center Preservation Act of 2003. This bill modified the percentage of funds for the Women's Business Centers (WBC) Program that the SBA can use for sustainability grants in Fiscal Year 2003. Under section 29(k) of the Small Business Act, funding for the WBC Program is split between initial grants for new Women's Business Centers and sustainability grants for Centers that have completed their original grant. As a result of this allocation, only 30.2 percent of the program's $12 million in appropriated funds could be used for sustainability grants. The bill modified this allocation by increasing the percentage for sustainability grants to 36 percent in order to address the funding shortfall that put a number of WBCs in jeopardy in Fiscal Year 2003. S. 1247 was limited only to Fiscal Year 2003 and pertained only to funds already appropriated to the SBA for the WBC program.

C. THE WOMEN'S SUSTAINABILITY RECOVERY ACT OF 2004 (S. 2267)

On April 30, 2004, the Senate unanimously passed S. 2267, the Women's Sustainability Recovery Act of 2004, a bill introduced by Chair Snowe and included a bipartisan co-sponsorship of 14 Senators. This legislation, similar to S. 1247, the Women's Business Center Preservation Act of 2003, assured that each of the existing eligible women's sustainability centers had the opportunity to compete for a sufficient pool of funds. For Fiscal Year 2004, the SBA was appropriated $12.5 million for the Women's Program. Under outdated legislation, only 30.2 percent of the appropriated funds was available for sustainability. Because the SBA increased the number of awards to women's business centers over the past 3 years, the reserve which was legislatively mandated for the sustainability centers was inadequate for the growing number of centers. The bill increased the percentage reserved for sustainability centers to 48 percent of the programs appropriated funds for Fiscal Year 2004 sustainability grants.

D. SBA'S WOMEN'S BUSINESS CENTER PROGRAM GRANTS FOR FISCAL YEAR 2004

On April 14, 2004, Chair Snowe and Ranking Member Kerry sent a letter to SBA Administrator Barreto requesting the agency's plans for funding new, regular and sustainability women's business centers. The SBA opened the application period for Fiscal Year 2004 Women's Business Center (WBC) grants on April 1, 2004. The SBA's intentions at the time were to renew 35 regularly funded women's business center grants, renew 32 of the sustainability center grants, and award 21 new, regularly funded women's business center grants. However, Chair Snowe and Senator Kerry's concern was that the agency's most experienced women's business centers will be insufficiently funded. Under the current formula, 53 sustainability centers in 39 states would be competing for a pool of funds that only provides for 32 full sustainability grants. As a result, many of the most effective and experienced centers that have been the source of business development in their communities and States were in jeopardy of closing.

On June 30, 2004, Chair Snowe was joined by 12 other Senators in sending a letter to Administrator Barreto requesting that the SBA assist in advocating for compromise language that increased the percentage reserved for sustainability grants from 30.2 percent to 48 percent. With the SBA's assistance, a new compromise bill was drafted that addressed the immediate women's business center funding issue for Fiscal Year 2004. However, the SBA still made plans to make women business center grant awards without the implementation of the compromise language. Under the funding formula, 53 sustainability centers in 39 states would be competing for a pool of funds that only provides for 32 full sustainability grants. Therefore, the agency's most experienced women's business centers would be insufficiently funded and in jeopardy of closing.

V. SBA TRANSFORMATION

A. IMPLEMENTATION OF SBA'S TRANSFORMATION INITIATIVE

Recognizing the need to transform the agency and its workforce to meet the modern demands of small businesses, the SBA announced a 5-year workforce transformation initiative in July 2002. On July 23, 2003, the SBA delivered an incomplete and basic outline of their upcoming plans to move into the second phase of the agency's transformation initiative. The plan included: strategic human capital planning and organizational alignment through the centralizing of liquidation functions thereby, removing this function from the district office; and improving services to small business customers by focusing the staff on partner management and outreach. On August 1, 2003, Chair Snowe, sent a letter to SBA Administrator Hector V. Barreto requesting detailed information on the SBA's plans to centralized the loan liquidation and purchase guarantee functions.

The first phase of the plan began in March 2003, as a pilot program in three district offices in North Carolina, South Florida, and Arizona. The pilot included an initial training period followed by the centralization of 7(a) liquidation and purchase activity in Santa Ana, California, and of the equivalent 504 program activity in Sacramento, California. Although it was clear that the SBA needed to address and solve its management and programmatic inefficiencies, Chair Snowe wanted to ensure that the SBA had designed a complete plan before moving forward with the next phase. On August 8, 2004, the SBA responded to Chair Snowe's request for additional details on the agency's transformation plans.

B. SBA'S BUYOUT ANNOUNCEMENT REGARDING AGENCY TRANSFORMATION PLANS

On September 9, 2003, the SBA and the AFGE Council 228 signed a memorandum of understanding (MOU) that established and staffed a liquidation center in Herndon, Virginia. This MOU included an agreement that the SBA district office staff who reported performing liquidation functions during 25% or more of their time in the agency's cost allocation survey would be directly reassigned to the liquidation center or to the 6 most severely understaffed district offices: New York, Newark, Atlanta, Chicago, San Francisco, and Los Angeles. Otherwise, the SBA employees identified would have to choose the option of early retirement or a buy-out.

On September 10, 2003, 180 SBA district office employees received letters identifying them as being responsible for liquidation work. Those employees were given 7 calendar days to accept a buyout option, or choose to stay and be directly reassigned without knowledge of where that assignment would be located. Those employees choosing to accept a buy-out were required to separate from Federal service no later than September 30, 2003. Although the Committee was aware of the SBA's intentions to eventually reposition staff, there was no notification to the Committee of these plans prior to implementation.

As a result of the SBA's decision to offer buyouts and direct reassignments to SBA personnel, on September 15, 2003, Chair Snowe, again sent a letter to Administrator Barreto requesting additional information on the agency's transformation plans. The SBA had determined that a significant portion of its workforce was not well positioned geographically to meet the goals that the current Administration wants to achieve—reaching more small businesses directly. As a result, part of the transformation plan was designed to move personnel to locations in need of staffing. In addition, the agency expected to down-size its workforce and to free up limited salary and expense resources. As indicated in the letter, Chair Snowe's concern regarding the buyouts was that if necessary personnel were removed, many States would face tremendous challenges in providing SBA programs and services where current staffing was already minimal.

C. SBA'S PLANS TO IMPROVE AND TRANSFORM THE 504 AND 7(A) LOAN LIQUIDATION AND PURCHASING ACTIVITIES

On October 30, 2003, Chair Snowe sent a letter to Administrator Barreto supporting the agency's new plan to streamline and modernize the loan liquidation program. According to the SBA's plans, by streamlining the workforce the agency would be able to improve loan processing functions, reduce personnel costs, and improve marketing and outreach. Additionally, the SBA expected to receive an even smaller operating budget for Fiscal Year 2005. Understanding the realities of the appropriation, and realizing that the agency must find ways to do more with less funding, this new transformation initiative was a step towards accomplishing the SBA's mission to serve more small businesses with limited funding.

The agency's new transformation plan contained three key components to effectively deliver services and assistance to small businesses through better management of the SBA's workforce including: increasing the number of employees in the field offices that directly assist small businesses; reducing the cost of operations not directly related to assisting small business, thereby providing more resources for assisting small businesses; and ensuring that key positions in all the field offices are filled with the most capable and qualified staff.

The final results of the pilot centralization involving three District Offices—Phoenix, Arizona, Charlotte, North Carolina, and Miami, Florida, showed some success.

The centralization of the 504 loan application processing decreased the processing time for these loan applications from more than two weeks to an average of two days. Through this pilot, 631 applications were submitted and nearly 500 were approved. By reducing the processing time for these loan applications, small business owners could move forward with construction of a new facility or purchase necessary machinery quicker. The results of reducing the processing for these loans allows new capital flows into the economy sooner and small businesses are able to create and retain more jobs sooner helping to spur job growth.

Additionally, the centralization of the SBA's 7(a) loan liquidation and guarantee purchase activities showed similar results. The processing time for these activities was reduced to an average of 60 days from a national average of over 500 days. The SBA modeled its approach after commercial banks and lenders and the SBA's lending partners eventually would absorb all of SBA's liquidations functions as the agency continued to streamline these processes.

Based on these results and understanding the SBA's plan as it was presented, Chair Snowe provided her support for the initiative.

VI. SBA'S INTERNATIONAL TRADE PROGRAM: FUNDING CONSTRAINTS FOR U.S. EXPORT ASSISTANCE CENTERS (USEACS)

On September 23, 2003, Chair Snowe sent a letter to SBA Administrator Barreto of the SBA expressing her concern that the agency was in jeopardy of being withdrawn from the U.S. Export Assistance Centers (USEACs). USEAC's are one-stop shops located in major metropolitan areas throughout the United States that promote trade and provide small or medium sized businesses with local export finance assistance. USEACs work, in partnership with the U.S. Department of Commerce and the U.S. Export-Import Bank, is the only partner that offers loans that are geared toward small businesses developing or expanding in the export market.

As a result of the SBA not paying its portion of overhead costs for the USEACs, the SBA faced the possibility of being withdrawn from these centers based on a Memorandum of Understanding (MOU) with the Department of Commerce and the Export-Import Bank. To meet the interagency agreement in Fiscal Year 2002, the SBA absorbed the salaries and the agency's share of operating and facility costs. However, for Fiscal Year 2003 the agency only allocated enough money for salaries with no funds obligated for operating and facility costs. As a result of Chair Snowe bringing the matter to the attention of the Administrator, the SBA responded immediately and fulfilled their obligation under the MOU agreement.

VII. THE SBA BUDGET AND APPROPRIATIONS FOR FISCAL YEAR 2005

A. FISCAL YEAR 2005 VIEW AND ESTIMATES LETTER TO SENATORS NICKLES AND CONRAD

On February 20, 2004, Chair Snowe sent a letter to Budget Committee Chairman Don Nickles and Ranking Minority Member Senator Kent Conrad regarding her views on the President's Fiscal Year 2005 budget request for the SBA. Chair Snowe's letter listed concerns regarding the request for zero appropriations and recommended funding levels for the 7(a) loan guaranty program, microloan program, microloan technical assistance, Federal and State Technology Partnership program, and U.S. Export Assistance Centers. In addition, Chair Snowe requested an increase in appropriations for the Small Business Development Center, SCORE and the office of the National Ombudsman. Overall, Chair Snowe's total request was $121 million over the FY2004 appropriations to provide adequate funding levels for the SBA's key lending and technical assistance programs.

B. AMENDMENT TO S. CON. RES. 95

On March 11, 2004, the Senate agreed to amendment SA 2839 offered by Chair Snowe to increase the budget authority for the SBA in the Senate Budget Resolution for Fiscal Year 2005. By increasing the SBA's budget authority the agency would effectively be able to provide its lending and technical assistance resources to our nation's small businesses. The President's proposed budget for the SBA was 15 percent lower than budget proposed last year and included zero funding for many of the agency's programs including the SBA's 7(a) program, HUBZone program, and U.S. Export Assistance Centers. With the SBA helping to create or retain more than 6.2 million jobs during the last five years, this amendment provided necessary funds that would aid the agency in its efforts to revitalize our nation's economy. The amendment increased the SBA's budget $121 million over Fiscal Year 2004 appropriations and provided the Appropriations Committee with the ability to provide funding for programs such as the 7(a) loan guaranty program, the Microloan program and Small Business Development Centers.

C. FISCAL YEAR 2005 APPROPRIATIONS LETTER TO SENATORS GREGG AND HOLLING

On May 10, 2004, Chair Snowe sent a letter to Chairman Judd Gregg and Ranking Member, Senator Ernest Hollings of the Subcommittee of Commerce Justice State and the Judiciary requesting that they utilize the additional funding available in the Fiscal Year 2005 Senate passed budget resolution. The request included funding for the Microloan program, U.S. Export Assistance Centers, Federal and State Technology Partnership Program and the Rural Outreach Program. Additionally, Chair Snowe requested increasing funds for Small Business Development Centers, SCORE and the Office of the National Ombudsman. The letter also requested to continue appropriated funds for the 7(a) program. The SBA requested zero appropriated funds in Fiscal Year 2005 for the program with plans to raise fees on lenders and borrowers and reduce the guarantee rates to substitute for appropriations. With this proposal raising several concerns, Chair Snowe requested that necessary appropriations continue until a solution that would most effectively reduce the programs subsidy rate was constructed so that small business growth would not be hindered.

VIII. SBA Reauthorization—Expiration of SBA Programs

On July 26, 2004, Chair Snowe sent a letter to SBA Administrator Barreto requesting information on SBA's programs that have suffered a full lapse in authority and may be partially restricted or altered because of the continued expiration of SBA programs. In particular the letter addressed the Women's Business Center Program, the 7(a) loan guaranty program, the Preferred Surety Bond Program and the Small Disadvantaged Business Program. The Senate had unanimously passed S. 2700, a bill introduced by Chair Snowe to temporarily extend through September 17, 2004, certain programs under the Small Business Act and the Small Business Investment Act of 1958. However, this bill did not pass the House of Representatives before the Congress recessed and, as a result, small businesses would not receive the valuable assistance provided by many of the SBA's programs until Congress returned in September to reconsider the bill.

IX. Procurement Issues

A. Small Business Procurement Opportunities, Title IV of S. 1375, the Small Business Administration 50th Anniversary Reauthorization Act of 2003

For over half a century, the Small Business Act has been directing the Federal Government to provide a fair portion of prime contracts and subcontracts to small businesses. Therefore, procurement matters have figured prominently in Chair Snowe's efforts to reauthorize the Small Business Administration. Numerous contracting-related provisions were favorably reported by the Committee and unanimously approved by the Senate on September 26, 2003 as part of the earliest SBA reauthorization bill, S. 1375. S. 1375 was never voted on by the House. The descriptions of these provisions contained in Senate Report 108–124 are reprinted below.

S. 1375 Procurement Provisions

Sec. 401: Contract consolidation—Section 401(a) replaces the definition of 'bundled' contracts with 'consolidation of contract requirements' to mean the use of a solicitation to obtain offers for a single contract or a multiple award contract to satisfy two or more requirements previously provided or performed, or of a type that is capable of being provided or performed by small business for that department or agency under two or more separate contracts smaller in cost than the total cost of the contract for which the offers are solicited.

Section 401(b) amends Section 15(e) of the Small Business Act and complements the intent of the original contract bundling legislation. It sets forth the procedures to be followed by Federal agencies and the SBA with regard to consolidation-of-contract requirements.

This section also limits the authority of Federal agencies to execute an acquisition strategy that includes a consolidation-of-contract requirement with a total value in excess of $2 million ($5 million for the Department of Defense) unless the agency demonstrates that the consolidation is necessary and justified based on market research. In addition, agencies must identify alternative contracting approaches that would involve a lesser degree of consolidation of contract requirements.

When an agency contemplates a consolidated procurement above $5 million ($7 million for the Department of Defense), this section requires the agency to conduct a more extensive review that includes the estimated benefits of the proposed consolidated contract requirements and how such benefits were calculated. Additionally, this section requires an agency to: (1) assess the specific impediments to participation by small business concerns as prime contractors that will result from the consolidation; (2) specify actions designed to maximize small business participation as prime contractors, including provisions that encourage small business teaming; (3) specify actions designed to maximize small business participation as subcontractors (including suppliers) at any tier under the contract or contracts that may be awarded to meet the requirements; and, (4) identify alternative strategies that would reduce or minimize the scope of consolidation and justify the rationale for not choosing the alternatives.

Section 401(c) modifies Section 15(p)(4)(B) of the Small Business Act to require the SBA to collect procurement strategies that have been successful in maximizing small business prime and subcontracting opportunities. It requires the SBA to include in its annual contract bundling report to the Congress a section that identifies and describes these best practices.

Section 401(d) amends Section 15(l) of the Small Business Act to provide for at least one Procurement Center Representative (PCR) in each state. In addition, this section directs the Administration to ensure there is not less than one PCR assigned at each major procurement center. This subsection also clarifies that these individuals shall be independent of, and have responsibilities independent from those of, SBA Breakout Procurement Center Representatives and Commercial Market Representatives.

Section 401(e) makes technical corrections to Section 15(k) of the Small Business Act, and Section 401(f) makes conforming amendments to Section 15(p) of the Small Business Act.

Section 401(g) requires the GAO to conduct a study by June 30, 2004, of the feasibility of establishing contract consolidation thresholds based on industry categories.

Sec. 402: Agency accountability—Section 402 makes numerous changes that hold agencies accountable for small business utilization goals. Subsection (a) amends Section 15(g)(2) of the Small Business Act to require agency heads to identify, in their strategic plan and their annual budget submission to Congress, a specific portion of their budget requests that will be awarded to small businesses; and, to report on these amounts as part of the Government Performance and Results Act (GPRA) in their Annual Performance and Accountability reports.

Additionally, the head of an agency may also be required to provide a complete report to the agency's congressional appropriators on the agency's small business utilization at the next appropriations cycle.

This section also directs agency senior procurement executives to communicate to subordinate employees the importance of achieving small business goals. In addition, it directs agencies to include in the annual performance evaluation for senior procurement and program office employees, a factor that measures the success of that senior executive in small business utilization.

For agencies that fail to achieve their small business achievement goals, this section would permit, where appropriate, a percentage of the performance bonus for that agency's senior procurement and program office employees to be withheld.

Section 402(b) amends Section 15(k)(3) of the Small Business Act to ensure that all Directors for the Office of Small and Disadvantaged Business Utilization report to the head of the agency.

Section 402(c) amends Section 10(d) of the Small Business Act to require, in addition to the Department of Defense, all Federal agencies represented on the President's Management Council to submit annual small business achievement reports to the Committees and the Committee on Small Business of the House of Representatives showing the amount of funds appropriated that have been expended, obligated, or contracted to be spent with small business.

Sec. 403: Small business participation in prime contracting—Section 403(a) amends Section 15(g) of the Small Business Act to establish a government-wide goal for participation by small businesses of the dollar value of awards placed against multiple award schedule contracts at not less than 23 percent.

Subsection (b) amends Section 15(j) of the Small Business Act to ensure that the small business reserve threshold is adjusted for any increase to the simplified acquisition threshold. This subsection further amends Section 15(j) to include Federal Supply Schedule orders within the small business reserve.

Sec. 404: Small business participation in subcontracting—Section 404(a) makes several changes that hold prime contractors responsible for the validity of subcontracting data. It amends Section 8(d)(6) of the Small Business Act to require the chief executive officer of large prime contractors to certify the accuracy of the firm's subcontracting report under penalty of law. It also requires large prime contractors to certify that they will use small business subcontractors in the amount and quality used in preparing their winning bid or proposal unless such firms no longer are in business or can no longer meet the quality, quantity or delivery date.

Subsection (b) amends Section 16(f) of the Small Business Act to impose penalties for false certifications of past compliance with small business subcontracting.

Sec. 405: Evaluating subcontract participation in awarding contracts—Section 405 amends Section 8(d) of the Small Business Act to provide for the consideration of proposed small business participation as subcontractor and suppliers as part of the process of selecting among competing offerers for any contract award that includes significant opportunity for subcontracting. It also provides for recognition of a prime contractor's past performance in supporting small business subcontracting participation in other Federal contracts.

This section requires the SBA to share subcontracting compliance review data with Federal contracting officers and to update a national centralized government-wide database with prime contractor past performance specifically related to subcontracting plan compliance.

It also requires contracting officers to withhold prime contractor payment until the prime contractor provides the agency with complete and accurate subcontracting reports.

If a subcontracting violation is found to constitute a material breach of contract, this section requires such material breaches to be referred to the Inspector General of the affected agency for investigation.

Sec. 406: Direct payments to subcontractors—Section 406 amends Section 8(d) of the Small Business Act to establish a pilot program in certain agencies to test direct payment to small business subcontractors. This program shall remain in effect until September 30, 2006.

Sec. 407: Women-owned small business industry study—Section 407 amends Section 8(m)(4) to direct the GAO to conduct a study by December 31, 2003, to identify industries in which small businesses owned and controlled by women are underrepresented with respect to Federal procurement.

Sec. 408: HUBZone authorization—Section 408 amends Section 31(d) of the Small Business Act to extend authorization of funding levels for the HUBZone program through Fiscal Year 2006.

Sec. 409: Definition of HUBZone; treatment of certain former military installation lands as HUBZones—The section amends Section 3(p) of the Small Business Act to designate military installations undergoing closure as HUBZones.

Sec. 410: Definition of HUBZone small business concern—Section 410 amends Section 3(p) of the Small Business Act to modify the ownership requirements for HUBZone small businesses to include any small business investment company, specialized small business investment company, New Markets Venture Capital company, or other similar investment company, provided such ownership does not exceed 15 percent of the small business concern.

Sec. 411: Acquisition regulations—Section 411 establishes a deadline for procurement regulations to be issued no later than 180 days after the date of the enactment of this bill.

B. AMENDMENTS TO THE RONALD W. REAGAN NATIONAL DEFENSE AUTHORIZATION ACT FOR FY 2005

The annual DoD Authorization Act traditionally contains a number of provisions affecting access of small business to government contracts as well as integrity of procurement programs. During consideration of H.R. 4200 and its Senate companion, S. 2400, Chair Snowe took a stand for small business by filing a series of amendments to the bill. The Senate unanimously adopted four Snowe amendments:

1. *Amendment No. 3399 (Feingold-Snowe)*—Amendment No. 3399 required that, as part of pre-separation counseling, veterans receive counseling on procurement opportunities available to veterans and service-disabled veterans. It also permitted the Department of Veterans Affairs (VA) and the Department of Defense (DOD) to allow such counseling on their facilities through the SBA, VA Outreach Centers, Small Business Development Centers, and other government agencies. It also required the General Accounting Office to conduct a new study to determine what improvements in veteran

pre-separation counseling, including procurement counseling, will be needed to better serve the nation's veterans.

Although the House-Senate conferees chose not retain the counseling provisions except the GAO study provision, on October 21, 2004 President Bush quickly moved to issue the Service Disabled Veterans Executive Order No. 13360, which implemented the substantive changes to service-disabled veterans procurement counseling sought by Chair Snowe. The Committee will exercise oversight over implementation of this Executive Order by working with Executive Branch agencies and with the GAO.

2. *Amendment No. 3273 (Snowe-Coleman-Kerry)*—Amendment No. 3273 was meant to better protect the interests of small businesses on the Office of Federal Procurement Policy's (OFPP's) Advisory Panel on Review of Acquisition Law and Policy by requiring the panel to make recommendations on assuring competition and small business participation, and providing for review of its report by both the Senate and the House Small Business Committees. The amendment was meant to apply President Bush's Executive Order 13272 on consideration of small business interests to the formulation of federal procurement policy. In her June 17, 2003 letter to the White House, Chair Snowe asked the OFPP to implement the substantive policies of the Amendment.

On July 12, 2003, Acting OFPP Administrator Robert Burton wrote to the Committee to announce the Administration's intent to implement the policies of the Amendment by placing a senior-level SBA official on the panel and requiring the panel to consider small business prime and subcontracting issues. Despite such support from the Bush Administration, the House-Senate conferees chose not to include this Amendment into the final bill. Nevertheless, the Committee is pleased with the commitment of the Bush Administration concerning the panel.

3. *Amendment No. 3246 (Snowe)*—Amendment No. 3246 expanded the DOD's Mentor-Protege Program to include service-disabled and HUBZone small business concerns in order to boost contract participation by these groups as DOD suppliers and subcontractors. The National Defense Authorization Act for FY 1991 established the pilot Mentor-Protege Program to provide reimbursements and other incentives for major DOD contractors to furnish disadvantaged small businesses assistance to enhance their capabilities and increase their participation as subcontractors and suppliers on DOD contracts. Four years ago, Chair Snowe worked closely with Chairman Warner to extend the benefits of this successful program to women-owned small businesses. This Amendment was retained in the final version of the Act and signed into law.

4. *Amendment No. 3434 (McConell-Snowe)*—Amendment No. 3434 set forth the sense of the Senate to protect, in any future adjustments for inflation, the dollar value of contract awards required to be reserved for small businesses to include those valued from $2,500 to $100,000. Existing law allows procurement officials to forego full and open competition on many contracts worth less than the simplified acquisition threshold of $100,000. This amendment, which was introduced by Senator Mitch McConnell (R–KY) at the behest of Chair Snowe, also directs the Administrator of Federal Procurement Policy to ensure that appropriate government-wide

policies and procedures are in place to monitor data on purchases made by federal agencies using government purchase cards and to encourage the maximum practicable number of those purchases be made from small businesses. Small Business Act provisions set a government-wide statutory goal of 23 percent of all prime contract awards to be awarded to small businesses. The government purchase card program has been around since 1989, when it was created as a way for agencies to streamline purchases of low-cost goods and services. Initially about 10,000 employees were issued cards. In the first year, they made only 2,000 transactions. In Fiscal Year 2002, they accounted for more than $15.2 billion in government expenditures and 25 million transactions.[1] The sense of the Senate provision was not retained in the final version of H.R. 4200.

The GAO recently reported (at the Committee's request) difficulties, with the collection of demographic data and has recommended specific action to improve data collection. GSA states they are making advances in collecting data on purchase card expenditures with small businesses, including minority and women-owned firms, but additional improvements are needed. The parity provision was retained in the final version of the bill and signed into law.

5. *Amendment No. 3344 (Byrd-Snowe-Allen-Coleman-Kerry)*—Amendment No. 3344 intended to expand the Commission on the Future of National Technology and Industrial Base by adding small business concerns for participation in and consideration by the Commission and to require that it study shortages of critical technologies and raw materials. The Senate unanimously approved this provision, although the Conference Committee chose not to create the Commission.

C. PROCUREMENT PROVISIONS IN S. 2821, THE SMALL BUSINESS REAUTHORIZATION AND MANUFACTURING ASSISTANCE ACT OF 2004

Chair Snowe continued her efforts to address important procurement matters as part of the second SBA reauthorization bill, S. 2821. That legislation contained 2 contracting provisions: Section 502, Procurement Center Representatives, which duplicated Section 401(d) of S. 1375, and Section 501, Women-owned Small Business Concerns. Section 501 directs the Administrator to conduct a study, within 90 days of enactment of this legislation, to identify industries in which small businesses owned and controlled by women are underrepresented with respect to Federal procurement; and conveys special authorities to the Administrator in carrying out the Small Business Act. This provision was originally in H.R. 2802 and was reported out of the House Small Business Committee, but left pending in the House.

Chair Snowe, along with Senator Bond and Senator Allen, also sponsored an amendment concerning the HUBZone and the Section 8(a) programs. The amendment was later incorporated into the third and final SBA reauthorization bill which passed as a part of the Consolidated Appropriations Act for FY2005.

[1] Fiscal Year 2002 Federal Procurement Report, Federal Procurement System, General Services Administration, p. 13.

D. HUBZONE AND SECTION 8(A) IMPROVEMENTS IN THE SMALL BUSINESS REAUTHORIZATION AND MANUFACTURING ASSISTANCE ACT OF 2004

The HUBZone Program continues to provide a valuable opportunity to reach out to small business owners who have not participated in government contracting in the past. The success of the program, however, will depend on addressing several unforseen issues that have arisen in the past year, as well as taking steps to strengthen the program's focus.

New questions about eligibility and program implementation have arisen. In response, Chair Snowe, Senator Allen, Senator Bond, Senator Murkowski, Senator Gregg, and Senator Talent crafted legislation to reform the HUBZone program that was included into the Small Business Reauthorization and Manufacturing Act, Public Law No. 108–447. An excerpt from the Explanatory Statement filed By Chair Snowe in the Congressional Record on November 19, 2004 concerning these, is reprinted below.

Streamlining And Revision Of Hubzone Eligibility Requirements—The Historically Underutilized Business Zone (HUBZone) program was designed to direct portions of federal contracting dollars into areas of the country that in the past have been out of the economic mainstream. HUBZone areas, which include qualified census tracts, poor rural counties, and Indian reservations, often are out-of-the-way places that the stream of commerce passes by, and thus tend to be in low or moderate income areas also characterized by comparatively high unemployment. These areas can also include certain rural communities and tend generally to be low-traffic areas that do not have a reliable customer base to support business development. As a result, businesses have been reluctant to move into these areas and expend the necessary funds to develop the infrastructure for creation of jobs.

The HUBZone program seeks to overcome these problems by providing the means for Federal procurement activities to become customers for small businesses that locate in HUBZones. In past years, the HUBZone program has encountered issues relating to the statutory requirement that a HUBZone firm be entirely owned and controlled by individual U.S. citizens. This requirement means that all HUBZone applicants need to be owned by human beings directly and not human beings organized as business entities. However, many small business owners and small business investors prefer to take advantage of various corporate forms in order to limit the personal liability for themselves and their families. Exceptions for Alaska Native Corporations, Indian tribal governments, and community development corporations were added by the Small Business Act reauthorization legislation in 2000. Even with those changes, the presence of a corporate entity or a limited liability company with an ownership stake in a small business would have automatically disqualified an otherwise eligible firm from participation in the HUBZone program. Small agricultural cooperatives, which already maintain presence in rural HUBZones, would have faced similar restrictions. These rules unnecessarily impede the flow of capital to the very areas that need it the most and create compliance conflicts with other small business procurement programs.

Section 151 addresses this problem through streamlining and revision of the eligibility requirements for HUBZone small businesses to include small businesses that are 51 percent owned by United States citizens, as well as to include small businesses which are small agricultural cooperatives or are owned and controlled by small agricultural cooperatives.

In addition, HUBZone firms owned by the Indian tribes have been facing peculiar challenges due to statutory requirements that they must hire a certain percentage of its workforce performing a federal contract or subcontract from Indian reservations or adjacent areas. These requirements, while motivated by the desire to spur economic development of the tribes, over time had the unintended consequence of putting tribally-owned firms at a disadvantage in comparison with all other HUBZone concerns by imposing a geographic restriction on the kinds of contracts that tribally-owned HUBZone firms could perform. Geographic restrictions also impeded business synergies between tribally-owned HUBZone firms and Alaskan Native Corporations. To remedy this disparity, the Act is providing tribally-owned HUBZone concerns the option of qualifying for the program based on locating in, and hiring workers from, either Indian reservations or any other HUBZones on the same terms as available to other HUBZone firms. Congress notes that the Indian tribes, as owners of the HUBZone firms, will be receiving expanded economic benefits from new contracting opportunities.

Expansion Of Qualified Areas—Congress observes that the HUBZone area qualifications are also in need of improvement. Paradoxically, economically distressed rural communities in states with high unemployment—among the neediest of needy areas—currently do not qualify for the HUBZone program because rural areas currently must qualify in relation to the statewide unemployment average. As an example, in calendar year 2003, Alaska had a statewide unemployment rate of 8.0 percent. To qualify as a HUBZone area, it was necessary for an Alaskan rural community to have an 11.2 percent unemployment rate. But, in 25 of the 50 states, a rural community could have qualified as a HUBZone with an unemployment range of 7.8 percent or less.

Section 152 addresses this problem by modifying the definition of a "qualified non-metropolitan county" to provide the option of comparing the unemployment statistic for that area to the statewide average or to the national average. The new statutory HUBZone definition should give the Small Business Administration flexibility to address both national and state-wide unemployment disparities without hurting the states that have comparatively low unemployment overall, but with pockets of serious unemployment.

Congress recognizes the drastic economic ramifications of military base closures and that the HUBZone program can uniquely harness the strength and the creativity of the private sector by providing incentive for small businesses to relocate to areas suffering such ramifications. According to congressional research, more than 300 military bases closed or realigned between 1988 and 2003 and more than 50 percent of these bases were located outside of a designated HUBZone. Therefore, Congress intends that, upon the later of the enactment of this act or the date of final closure, existing as well as future military base closure areas be designated as

HUBZones for a period of five years in order to reinvigorate the productive capacity of such areas and leverage existing local customers and a skilled workforce. Congress believes that new businesses and new jobs created through the HUBZone small firms mean new life for areas affected by base closure.

Additionally, Congress notes the existence of numerous complaints that the current definition of HUBZone qualified areas based on census income data, in conjunction with the definition of HUBZone qualified redesignated areas, fail to provide adequate time to recoup a return on investment. These concerns appear justified. Congress observes that the HUBZone program is relatively young, and the federal government is not even close to meeting its statutory prime contracting goal of 3 percent. Because the HUBZone program was enacted into law in 1997, the initial HUBZone areas were designated on the basis of the 1990 Census. However, the federal government conducted another census in 2000. As a result, many areas were redesignated after only 3 years of the program's existence. The statute currently grandfathers the redesignated areas into the program for 3 years.

Congress notes that, at the time of the last redesignation, the small business community received comparatively few benefits from the HUBZone program despite the substantial workforce recruitment, compliance, and business development efforts that must be expended by each of the HUBZone firms. These small businesses, which made business decisions to pursue the HUBZone strategy by locating in a HUBZone, adjusting their ownership structure, and recruiting HUBZone residents are in danger of being penalized for the federal government's slow initial implementation of the HUBZone program. Further, anecdotal evidence indicates that it may take a long time for a new firm to secure a federal contract, and that multiple-order contracts commonly envision task orders over a number of years. In these circumstances, a 3-year grandfather clause would appear not to provide sufficient time for a small business to generate a return on the HUBZone investment. By comparison, companies under the 8(a) program can maintain such a designation for 9 years, and a general small business designation can be maintained indefinitely. Therefore, Congress imposes a moratorium on HUBZone area redesignations by providing for an extension of the redesignation period until the conclusion of the 2010 Census. No certified HUBZone firm shall be decertified as a result of either the redesignation process based on the 2000 Census data or any revised unemployment data subsequent to December 21, 2000, the date of passage of enactment of the HUBZone in the Native America Act. It is the intent of Congress to have the Small Business Administration reinstate any HUBZone firm previously decertified based on these two criteria.

Congress also finds that, concurrently with the moratorium, a study on the effectiveness of the HUBZone area definitions, including the redesignation period, must be conducted by the Office of Advocacy of the United States Small Business Administration. The Office of Advocacy is chosen to conduct this study for its particular expertise in small business procurement, rural small business development, and general small business matters. Congress directs the Office of Advocacy to examine the impact and effectiveness of the HUBZone definitions on small business development and jobs creation, and expects that the Office of Advocacy will periodically consult with congressional small business committees on matters concerning this study. Findings and recommendations of the study must be reported to congressional small business committees by May 1, 2008.

Price Evaluation Preference—With regards to the application of existing HUBZone price preferences to international food aid procurements conducted by the United States Department of Agriculture (USDA), Congress concludes that the preferences as they currently stand are hindering the goals of U.S. foreign humanitarian food assistance programs. This view is supported by extensive consideration of market data from the Kansas City auction office of the USDA Farm Service Agency, the structure of auction tenders and other auction processes, as well as data supplied by the industry. It appears that there is a risk of various unintended and undesirable consequences to applying the current HUBZone mandate to international food aid acquisitions. In particular, it appears that, in the context of food aid tender auctions, the claimed job gains fostered by the current price preference are offset by job losses in other communities, the non-HUBZone small businesses attempting to compete may experience undue harm, and the competitive supplier base may atrophy. In turn, this may undermine USDA's capacity to secure adequate foodstuffs for malnourished persons and increase the costs to the food aid programs without realizing adequate jobs creation and business development benefits.

The HUBZone price preference alternative adopted in this act (a 5 percent price evaluation preference on 20 percent of the contract) would alleviate these potentially damaging effects on the U.S. food aid system. Congress believes that this approach would preserve the HUBZone program's goal of providing HUBZone-eligible companies with a meaningful opportunity to compete while ensuring that the USDA has an adequate capacity of supply from which to draw to deliver emergency food aid in catastrophic situations. This approach would also eliminate the current HUBZone program's application problem which directly penalizes non-HUBZone small businesses due to the nature of the food aid auctions. The potential for job losses in other communities would be limited. Importantly, this approach also reflects the cornerstone of America's efforts to provide food assistance to the world's neediest people through competitive markets.

According to President Dwight D. Eisenhower and Congressional architects of the Small Business Act, an overarching purpose of small business procurement programs is to assure a vibrant, competitive supplier base for the Federal Government. Price preferences are employed to further this purpose, and should be structured accordingly. Congress notes that, in general, price preferences have been a valuable tool for encouraging a more robust supplier base. Nevertheless, Congress believes that, in these very special circumstances, it is important to encourage competition by keeping multiple vendors actively bidding in our food assistance programs to secure the lowest cost procurement and emergency supply chains in the case of humanitarian crisis. This approach builds on the current small business 10 percent set-aside by an additional 20 percent allocation of every tender to small businesses and HUBZone applicants. It guarantees full and open competition, including competition pursuant to the Small Business Act, in food aid procurement tenders to assure that U.S. food aid programs do not suffer consequences inconsistent with the intent of the price preference program. The approach in this legislation safeguards the dual interests of a vibrant small business presence in federal procurements and robust food aid programs.

HUBZone Authorizations—Congress notes that the Federal Government has failed to meet its statutory HUBZone contracting goals every single year these goals have been in effect. Continuous, dedicated authorization of the HUBZone program is essential to continue the effort to bring economic opportunities to the HUBZone areas. Therefore, Congress extends the current authorization of appropriations of $10,000,000 for the SBA's HUBZone program through Fiscal Year 2006.

Participation In Federally Funded Projects—Section 155 removes the burdensome paperwork requirements for additional certification by firms seeking to perform any State, or political subdivision projects that utilize federal dollars if they are currently certified, or otherwise meet the applicable qualification requirements, for participation in any program under 8(a) of the Small Business Act.

This change will: (1) provide federally certified 8(a) small businesses with access to all State and local projects funded in whole or in part by the Federal Government; (2) eliminate the burden of requiring 8(a) small businesses to get certifications from the State or local government or both in addition to their federal certification under 8(a); and, (3) decrease certification costs and eliminate time delays associated with the burden of receiving additional State or local government certifications for businesses authorized to participate in program established by § 8(a) of the Small Business Act.

E. SBIR LEGISLATION TO FACILITATE THE INTENT OF CONGRESS FOR THE SMALL BUSINESS INNOVATION RESEARCH PROGRAM

In establishing the Small Business Innovation Research Program, Congress sought to encourage government agencies to use their research and development money to provide development funding for innovative research by small businesses where there is a strong potential for commercializing the research results and creating appropriate production capacity. A key indicator of commercial potential is availability of non-governmental funding.

Recently, administrative law judges at the SBA Office of Hearings and Appeals issued a series of decisions which, for the first time in over 20 years, excluded majority venture-backed firms which were otherwise small from participation in the SBIR Program. It appears that the OHA opinions do not represent the final decision of the SBA, as they may be overruled by the Administrator. Nontheless, these decisions had serious adverse implications for many companies, especially those in the biotechnological field, and for agency programs that encourage commercialization, like the DOD's Phase II Plus. At stake is the continuous inflow of investment capital for small companies that develop life-saving drugs and products critical to national defense and to the advancement of innovation.

Chair Snowe and two other members of this Committee, Senator Bond and Senator Bennett, along with Senator Kennedy, introduced a bill, S. 2834, designed to restore the status quo prior to the OHA decision. Following in-depth discussions with industry and among member staffs, the Committee is considering a substitute bill as well as activities to study this issue further. Committee staff has been in discussions with the National Academy of Sciences, which has been directed by law to study the SBIR Program, concerning possible workshops or other study activities on this issue.

F. INVESTIGATION OF THE SBA'S CONTRACTING PRACTICES

As part of the Committee's oversight role, Chair Snowe has been working with the Inspector General of the SBA to review the integrity of the SBA's own procurement processes and reduce their vulnerability to waste, fraud, and abuse. The Committee will continue this work in the 109th Congress in order to ensure that the SBA leads other acquisition agencies by example.

G. CONTRACT BUNDLING

Last March, a hearing of the Small Business Committee was called to learn more about the President's plan to unbundle contracts for small business. During the hearing Administration officials assured the Chair that appropriate metrics would be put in place to track progress in implementing the plan. Since that time, however, the Committee learned that several agencies were not complying with certain requirements of the plan.

Chair Snowe sent letters to the OMB's Office of Federal Procurement Policy to request information on the metrics they have put in place to monitor agency progress. In addition, letters were sent to each of the agency's on the President's Management Council to request their progress in addressing contract bundling concerns.

1. *Oversight of Contract Bundling Practices in Acquisition of Translation and Interpretation Services for the War on Terrorism*— As Chairs of the Senate Committee on Small Business and the Senate Committee on Governmental Affairs, Senator Snowe and Senator Collins have taken a keen interest in the acquisition planning of the Army Intelligence and Security Command (INSCOM) for reprocurement of translation services. Existing contract, originally awarded to BTG, Inc. for 75 translators, was novated to Titan Corporation as a result of a merger and acquisition of the awardee and ballooned to over 4,000 contractor personnel. Traditionally, small boutique firms full of experts in particular languages, translation techniques, and substantive subject matter vocabularies have been the backbone of the translation services industry. Titan did not specialize in translation services at the time of its merger with BTG. Media reports suggested that Titan was forced to rely on hiring taxicab drivers and random local individuals off the street in order to accommodate the growing demands of the military in the war on terror. The Committees received information suggesting that the apparent result of such practices has been loss in professionalism, and Titan translation staff recently made the news due to alleged involvement into the Abu Ghraib prison abuse scandal.

The Central Contractor Registry lists over 1,000 small and HUBZone small businesses which offer translation services to the government, including companies such as World Wide Language Resources of Maine. INSCOM's original strategy would have excluded these companies from prime contracts by creating a mega-contract for worldwide translation services in all languages and translation assignment management for the military and civilian agencies.

Chair Snowe and Senator Collins have written Michael Wynne, the Acting Under Secretary of Defense for Acquisiton, Technology, and Logistics and asked him to take all necessary actions to unbundle this procurement and to prevent wholesale delegation of inherently governmental functions to Titan. The SBA also opined that INSCOM's approach implicated bundling concerns. In the name of administrative convenience, the Army's choice to exclude small businesses from translation prime contracts would have discarded a large, qualified supplier base precisely at the time when our military forces are in need of quality, responsible translation providers. Chair Snowe was pleased that the Army withdrew its solicitation.

Acting Under Secretary Wynne, who is also the nominee for that post, has written Chair Snowe with assurances of INSCOM's plans to comply with bundling regulations. As part of the Senate's advice and consent responsibilities, Committee staff will continue to provide oversight on this important issue by seeking further clarifications and commitments for implementation of Congressional and Presidential contract bundling initiatives from the Acting Under Secretary.

2. *Oversight of Contract Bundling in Commercial Satellite Telecommunications Services for the Military*—In the Ronald W. Reagan National Defense Authorization Act, Congress directed the Secretary of Defense to conduct a study of commercial satellite telecommunications acquisitions by the DOD. These services were originally procured through a large-business contract known as MTC. However, subsequently the DOD implemented a small business IDIQ contract structure known as DSTS–G. Under DSTS–G, small businesses act as value-added resellers, making large providers to compete for each task order. It was the largest DOD small business procurement in history at the time of the award, and provided a strong demonstration of the ability of small businesses to be a strong presence in the high-technology fields.

Chair Snowe has written a letter reminding the DOD that analysis of contract bundling and consolidation must be conducted prior to any changes in the existing DSTS–G procurement strategy. Chair Snowe also requested the Administrator of the SBA to appeal any decision to bundle this contract. In response, Lt. General Harry Raduege, DISA Director, assured the Committee that DISA will comply with all applicable contract bundling and contract consolidation regulations in any further actions taken with regard to the DSTS–G contract. The Offices of Small and Disadvantaged Business Utilization for the DISA and the DOD also provided valuable assistance in addressing this matter.

3. *Oversight of Contract Bundling in Information Technology Procurements by the U.S. Air Force Information Technology Commodity Council*—Congressional and Presidential initiatives to combat contract bundling have been facing a number of implementation hurdles due to some agencies' undue emphasis on the so-called "enterprise buying" acquisition strategies. Enterprise buying may provide the benefit of volume discounts to the government, but, just

as likely, may saddle the government with limited technical options and higher costs by artificially excluding innovative small business suppliers and subsidizing higher overhead of large contractors.

On June 9, 2004, Chair Snowe and Senator Allen wrote to Marvin Sambur, Assistant Secretary of the Air Force for Acquisition, with concerns over the plans of the Air Force Commodities Council (ITCC), Headquarters Standard Systems Group, to exclude small businesses, especially small manufacturers, from participating in the competition for service-wide desktop/laptop/server blanket purchase agreements (BPAs). In response, Assistant Secretary Sambur advised the Committee that the Air Force set aside three out of seven BPAs to small businesses, one for an Original Equipment Manufacturer (OEM) and two for Value-Added Resellers (VAR). The small business VAR BPAs represent the entire reseller market under this acquisition. The Air Force recently made awarded the OEM BPA to NCS Technologies, Inc. of Virginia.

H. OVERSIGHT OF CONTRACTING PRACTICES PURSUANT TO THE SBIR PROGRAM

Small businesses participating in the SBIR Program's rigorous Phase I and Phase II grant competitions often do so in reliance on the possibility of receiving a sole-source Phase III contract award as well as on the statutory and regulatory protections for their data rights. The SBA's Office of Technology has appellate authority in instances where agencies award contracts for technologies subject to the SBIR Program to non-SBIR companies. The Office of Technology is also responsible for government-wide data rights protection policy. Committee staff has been working with the SBA to strengthen the exercise of its appellate authority and to strengthen the agencies' compliance with the SBIR Program requirements.

I. GOVERNMENT-WIDE MENTOR-PROTÉGÉ PROGRAM REVIEW

Many federal agencies operate mentor-protégé programs based on section 637 of the Small Business Act, which authorizes agencies to provide subcontracting incentives for small business. The Department of Defense currently operates a statutory pilot program to encourage mentoring arrangements between mentor firms, typically large firms with demonstrated capability, to provide technical assistance to small business protégé. The DOD program authorizes reimbursements and other incentives.

While mentor-protégé is not directly related to bundling, it can help protégé firms overcome its effects. Getting technical assistance and developing business infrastructure can help a small firm manage larger contracts than it would otherwise be able to handle. Thus, it prepares smaller firms to stay in the Federal procurement market that is increasingly skewed toward larger contracts.

Chair Snowe sent a series of letters to government agencies concerning their mentor-protege programs in order to assess best practices before introducing government-wide mentor-protege legislation. Committee staff is in the process of analyzing the agencies' responses.

J. SBA'S PROPOSED REVISION OF SIZE STANDARDS

The SBA's proposed change of size standards is the single most controversial procurement policy matter for small business today. On March 19, 2004, the SBA published the Proposed Rule to change the current system of small business size standards used, among others, for small business government contract programs. The current system employs both revenue- and employee-based standards, and provides over a thousand standards tailored to various industries. The new system attempted to create a few across-the-board employee-based standards, with some exceptions. The ostensible goal of the change was to simplify size determinations and contracting processes.

Comments voiced by the industry at various roundtables organized by the SBA have been almost uniformly negative. It was pointed out that the proposed rule would have the effect of *depressing the creation of jobs* by creating artificial payroll ceilings for companies, that the data used to convert revenues standards into employee-based standards is almost 7 years old, and that small businesses would face greater bias in contractor responsibility standards set forth by the Contracting Officers. In addition, the Committee received information that the change in standards would render over 34,000 businesses no longer small, denying them overnight the ability to participate in government contracts pursuant to the Small Business Act or to qualify for SBA loans and small business regulatory assistance.

Chair Snowe opposed this change and, in a statement on July 1, welcomed the SBA's decision to withdraw its proposed rule and called for agency consultations with Congress on this issue. The Committee plans to work closely with the SBA during the public hearings the agency is planning to conduct on size standards, and intends to conduct close oversight of the revision process.

K. SMALL BUSINESS PRIME CONTRACTING AND SUBCONTRACTING AT THE U.S. DEPARTMENT OF ENERGY

1. *Joint Inquiry with the Senate Committee on Energy and Natural Resources and the Comprehensive GAO Studies*—With over 90 percent of its budget spent on contracts, the U.S. Department of Energy (DOE) is a leader among federal agencies in terms of overall contracting activity. In fact, DOE prime contract awards amounted to over $19 billion in Fiscal Year 2003. However, data collected by the Federal Procurement Data System (FPDS) show that for FY '03 DOE, nonetheless, ranked dead last among the 15 Executive departments required to comply with the government-wide statutory small business contracting goal of 23 percent, awarding only about 4 percent of its prime contracts to small businesses. By contrast, the top ranking agency, the department of Housing and Urban Development, awarded 54 percent of its prime contracts to small businesses during the same year. The DOE's low goaling achievements came into focus after 199, when the OFPP, upon advice of this Committee's then-Chairman Kit Bond and Ranking Member John Kerry, directed the DOE to abandon the accounting fiction of including first-tier small business subcontracts together with its actual small business prime contracts.

On May 18, 2004, the Senate Committee on Energy and Natural Resources held hearings concerning the small business prime contracting and subcontracting practices at the DOE. At that hearing, a GAO representative testified that, despite a contracting plan prepared by DOE's Office of Small and Disadvantaged Business Utilization, it was unclear whether the DOE made an actual Department-wide commitment to the Congressionally-mandated small business goal, and whether it has established a consistent long-term strategy for achieving that goal. The Energy Committee also received information that the DOE was considering to simply novate existing small business subcontracts by making them prime contracts on paper, but continuing to make large contractors responsible for management and oversight responsibility for these small business prime contracts. Concerns have also been raised that the uncertainties in the DOE's approach to small business contracting may have adverse impacts on other legitimate agency objectives.

In written testimony before the Energy Committee, Chair Snowe reaffirmed this Committee's view that prime contract goals are a vital indicator of whether small businesses have fair and meaningful access to business opportunities at the DOE, and that accurate accounting for prime contracting goals must be reflective of the actual awards made to small businesses by the DOE. Chair Snowe also emphatically stated that small businesses not only do not hinder good management, but provide significant value to the government. Chair Snowe called for a reform of the DOE's internal acquisition processes and strengthening of the DOE's acquisition workforce, its Office of Small and Disadvantaged Business Utilization, and its Office of Inspector General.

On November 19, 2004, this Committee and the Committee on Energy and Natural Resources announced a joint inquiry into small business prime contracting and subcontracting practices at the Department of Energy. The Chairs and Ranking Members of the two Committees wrote to Comptroller General David Walker requesting that the GAO conduct comprehensive studies of DOE procurement policies and practices. "Given the challenge facing DOE to dramatically increase its small business prime contracting, we want to assure that DOE utilizes appropriate practices and has the necessary tools to aggressively expand prime contracting to small businesses while also ensuring the success of their other mission requirements," Chair Snowe and her colleagues wrote in their request to GAO.

The Committee's letter of request included the following questions:

a. What steps is DOE taking, or planning to take, to increase its level of prime contracting with small businesses? What criteria does the department use to identify work performed by its facility management contractors that could be set aside for a prime contract with small business while adequately assuring mission accomplishment, safety, and security?

b. What are the federal government's "best practices" in increasing small business prime contracting which adequately assure mission accomplishment, safety, and security considerations for other agencies? Is DOE following the "best practices" used by other federal agencies that share similar national security or safety challenges as those faced by DOE, or any applicable guidance of the SBA or the OFPP, for increasing their small business prime contracting?

c. What challenges or barriers exist to DOE increasing its level of small business prime contracting, and what is the department doing to address these challenges? For example, does the DOE have sufficient resources, acquisition workforce, and internal processes to fully implement a small business prime contracting program that complies with small business contracting goals and federal contracting competition requirements, as well as the capabilities to administer its large and small prime contracts with sufficient oversight to assure mission accomplishment, safety, and security considerations?

d. What are the typical small business subcontracting requirements imposed by the DOE on its facility management contractors?

e. What are the frequently occurring concerns and challenges experienced by DOE small business subcontractors, and what are potential approaches to assure that the facility management contractors address or mitigate these concerns and challenges?

The staff of both Committees has been working with the GAO to develop, adjust, and monitor audit objectives as well as the methodology for the studies. Two studies, one on prime contracting and the other on subcontracting, are expected.

2. *Small Business Prime Contracting Requirements in Division C (Energy and Water Appropriations) of the Consolidated Appropriations Act for FY 2005*—In response to the testimony of the GAO and other reports on DOE's small business procurement practices, this Committee began to work together with the Senate Committee on Energy and Natural Resources as well as with the Subcommittee on Energy and Water Development of the Senate Committee on Appropriations to correct some of the improprieties in the procurement process and to strengthen the small business acquisition planning process. Just like the joint inquiry, the Committees' legislative work was motivated by the desire to attack the problems in DOE's practices rather than the symptom of the problems, i.e. the DOE's low goaling achievements for small business prime contracts.

Sections 312 and 313—The Energy and Water Appropriations Act contained provisions to mandate that the Energy Department's break-out efforts proceed through the existing consultative process with the Small Business Administration's breakout procurement center representative (PCR) or designee for considering breakout strategies in light of the Department's mission objectives. Ordinarily, the PCR consultative process is discretionary under the Federal Acquisition Regulation (FAR). Section 312 merely removes this discretion from the DOE and the SBA, and Section 313 reiterates the existing prohibition on performance of inherently governmental functions by private contractors as set forth in the FAR.

3. *Requirements for Production of Small Business Contracting Plans of the Department of Energy and of Related Views of the Small Business Administration in Section 312, Division C (Energy and Water Appropriations) of the Consolidated Appropriations Act for FY 2005*—In the course of facilitating the joint inquiry with the Senate Committee on Energy and Natural Resources, Chair Snowe requested Ms. Allegra McCullough, SBA Associate Deputy Admin-

istrator for Government Contracting and Business Development, to produce to this Committee the DOE's FY2005 official goaling plan and related SBA documents. In response, Ms. McCullough sent a letter to Chair Snowe contending that the responsive documents were privileged from production as pre-decisional and deliberative. The SBA Office of General Counsel also attempted to claim these privilege assertions on behalf of the Department of Energy.

The SBA's refusal to cooperate in the process of improving small business contracting opportunities at the DOE has been unfortunate. The Committee does not believe that Ms. McCullough and the SBA Office of General Counsel asserted a valid privilege from production by characterizing requested documents as pre-decisional and deliberative materials. To begin with, the DOE's official small business plan is not pre-decisional, since the DOE already reached its decision prior to sending this plan to the SBA. The precedents that addressed the deliberative process privilege recognized that it is neither Constitutional (unlike the Congressional oversight power) nor absolute. Rather, this privilege is commonly asserted in cases brought by private litigants and gives way to a countervailing public interest. This is because the deliberative process doctrine is rooted in the common law evidentiary principles and in the Freedom of Information Act, which do not bar Congressional inquiries. Moreover, the United States Court of Appeals for the District of Columbia Circuit, the location of the SBA headquarters, held on more than one occasion that Congress created for itself special access to materials otherwise protected by the deliberative process privilege against disclosures to private parties. The Committee is aware of no reported precedent—and the SBA cited none—upholding a deliberative process privilege against disclosures to Congress. Since the small business goaling process, and especially the agency plan, is a creature of the Small Business Act, there is a strong public interest in adequate Congressional oversight of the agencies that implement Congressional small business policies. Furthermore, any deliberative process privilege has been overridden since the 1950s by Section 10(e) of the Small Business Act, 15 U.S.C. 639(e), which states that the SBA "shall retain all correspondence, records of inquiries, memoranda, reports, books, and records . . . and shall at all times keep the same available for inspection and examination" by "duly authorized representatives" of the Senate Committee on Small Business and Entrepreneurship.

Accordingly, Chair Snowe and Chairman Domenici included into the Act specific documents production requirements directing the Department of Energy to submit a report to Congress including its small business contract goaling plans required by Section 15(h) of the Small Business Act together. The goaling plans are normally established by the DOE Office of Small and Disadvantaged Business Utilization within the Office of the Secretary of Energy, and are either approved or rejected by the SBA (or, in case of an appeal, by the OFPP). The Act does not change this practice, but places the overall responsibility for the report on the Secretary of Energy. In addition, the Act makes clear that the Secretary of Energy must request and address in the report the views of both the DOE Office of Small and Disadvantaged Business Utilization and of the Small Business Administration. Therefore, the Act gives the SBA a date certain by which it must provide its position on the

DOE's small business goals as part of the report of the Secretary of Energy to Congress.

As the President has signed the Consolidated Appropriations Act for Fiscal Year 2005 into law, Therefore, the Committee expects that the Small Business Administration and the Department of Energy will follow the law and produce to Congress the documents to which it is rightfully entitled. The Committee expects that, in the future, the Small Business Administration and other agencies will be working together with Congress to facilitate the policies of the Small Business Act and will fully cooperate with Congressional inquiries. The Committee will not hesitate to use appropriate tools at its disposal to vindicate the authorities and the Constitutional oversight prerogatives of the Legislative Branch.

X. Manufacturing and Small Business

Manufacturing employment in the United States has declined since its historic peak in 1979 and the loss has accelerated in recent years. The problem is particularly troubling because manufacturing jobs tend to pay a higher average hourly total compensation than jobs in other sectors of our economy.

Small business manufacturers constitute over ninety-eight percent of our nation's manufacturing enterprises. It is impossible to overstate small manufacturers' role within the overall manufacturing industry and our nation's economy.

Chair Snowe has placed a high priority on trying to resuscitate our nation's small business industrial base because she understands the importance it plays in preserving our economic and national security.

A. Small Manufacturers Assistance, Recovery, and Trade ("SMART") Act

On November 25, 2003, in response to what she learned from manufacturers throughout the country, including from those who testified at the "Small Business Manufacturing in a Global Market" field hearing, Chair Snowe and original co-sponsor Senator George Voinovich introduced S. 1977, the Small Manufacturers Assistance, Recovery, and Trade ("SMART") Act.

The SMART Act contains numerous provisions to benefit small manufacturers. Among those provisions are ones that would: (a) increase the amount of capital available to small manufacturers through the Small Business Administration's loan programs; (b) establish an Assistant Secretary for Manufacturing within the Department of Commerce, who will be responsible for identifying and addressing manufacturers' concerns; (c) create an Interagency Manufacturing Task Force—to coordinate the efforts and resources of numerous Federal agencies, spur interagency cooperation, and provide recommendations to assist manufacturers; (d) create a Small Business Manufacturing Task Force within the Small Business Administration to ensure that the Agency focuses a proper level of attention to manufacturers' concerns and that it promotes its manufacturing related services and programs; and (e) increase the number of SBA representatives at U.S. Export Assistance Centers.

Several key SMART Act provisions have either been enacted through legislation, or implemented directly by the Administration.

For instance, Albert Frink has been appointed as the Administration's first Assistant Secretary of Commerce for Manufacturing and Services; the Commerce Department has agreed to form an Interagency Working Group on Manufacturing, and the Consolidated Appropriations Act of 2004 included SMART Act language, increasing manufacturers' access to capital and creating a Manufacturing Task Force within the SBA.

B. SMALL BUSINESS MANUFACTURING FORUM IN BREWER, MAINE

On February 17, 2004, Chair Snowe held a "Small Business Manufacturing Forum" (the Forum) in Brewer, Maine. The Forum brought small manufacturers together with various organizations and agency representatives (hereafter "resource providers") who specialize in offering small business assistance. The manufacturers were provided the opportunity to express the problems and barriers they face and to provide concrete examples of steps they have undertaken to remain successful. The resource providers explained the various programs and services available to small manufacturers, and a breakout period during the Forum allowed the manufacturers time to meet with the resource providers to obtain their assistance.

C. MANUFACTURING EXTENSION PARTNERSHIP (MEP)

The MEP is a nationwide network of not-for-profit centers, whose sole purpose is to provide small and medium-sized manufacturers with help in implementing the most advanced manufacturing technologies and processes to succeed. The MEP was originally intended to be comprised of 12 federally supported centers, with federal funding ending after six years. In its 15 years of operation, the program has expanded away from this original design to include 400 locations, and Congress has removed the sunset provisions.

In a recent National Institute of Standards and Technology survey of MEP clients served during FY 2003, over 5,000 companies across the country reported that, as a result of MEP services, they: created or retained 35,028 jobs; increased $953 million in sales; retained sales of $1.84 billion; realized $681 million in cost savings; and invested $940 million in modernization, including plant and equipment.

The FY 2004 Omnibus Appropriations Conference Report drastically cut MEP funding from a previous level of $106 million to $39.6 million. The FY 2004 funding cut, coupled with potential shortfalls in FY 2005 funding, threatened to severely curtail the MEP's ability to assist the nation's manufacturers at a time when they most need assistance.

1. *Letter to Commerce Department to Transfer $8.5 million in funds to the MEP*—On May 13, 2004, Chair Snowe, along with five colleagues, sent a letter to Secretary of Commerce Donald Evans requesting that he reprogram and transfer Commerce FY 2004 funds to support the MEP program. The letter signed by 55 Senators expressed the belief that the MEP's appropriation level was insufficient to maintain the existing network of MEP centers. The failure to increase funding would lead to these centers having to close, or drastically reduce services, resulting in small manufacturers being unable to receive the assistance that helps them stay competitive in the global marketplace.

Thankfully, the Commerce Department responded by transferring $8.5 million from its Advanced Technology Program to the MEP.

2. *Recompetition of the MEP*—On July 30, 2004, Chair Snowe and Senator Kohl, Senator Lieberman, Senator Reed, Senator DeWine, Senator Schumer, Senator Levin, and Senator Bayh sent a letter to Phillip Bond, Under Secretary of Commerce for Technology, Department of Commerce, urging that he reconsider a system-wide recompetition for U.S. MEP centers.

The recompetition would have required that individual MEP centers justify their funding. This process, at a time when the MEP was operating under a severely reduced budget, threatened to divert the MEP's time and resources away from its mission of assisting our nation's small manufacturers. Such a hasty recompetition may have also dismantled the network of effective state and local partnerships that took over fifteen years for the MEP to build.

Fortunately, the Commerce Department responded appropriately by deciding to forego a system-wide recompetition during the MEP's time of crises.

3. *Chair Snowe and Senator Lieberman Lead Group of Senators in a Letter Requesting Restored MEP Funding in FY 2005*—On March 31, 2004, Chair Snowe and Senator Lieberman, Co-Chairs of the Senate Task Force on Manufacturing, led a group of 56 Senators in a bipartisan letter to the Commerce-Justice-State (CJS) Appropriations Subcommittee requesting that the MEP's funding be restored in FY 2005. On September 15, 2004, Senate Appropriators approved their CJS Appropriations bill (S. 2809) by a vote of 27–0. The bill included $112 million for the MEP for FY 05. The Consolidated Appropriations Act of 2004 provides $109 million for FY 05 for the MEP program.

XI. VETERAN ISSUES

A. SMALL BUSINESSES AFFECTED BY MILITARY DEPLOYMENTS

1. *Congressional Budget Office Study on the Affects of Military Deployments on Small Businesses*—Our country is profoundly indebted to our nation's Guard and Reserve members for their contribution to our national defense. There are more than 170,000 Guard members and Reservists deployed around the globe serving our nation's interests. These individuals leave their families, friends, and civilian careers, behind to answer the call of duty.

The current trend toward longer and more frequent Guard and Reserve deployments, imposes an especially profound burden on small businesses that employ Guard members and Reservists. This problem is further magnified when the business owner themself is deployed. It is often extremely difficult for small businesses to continue operations during deployments, or restart a venture after a deployment.

In response to these concerns, on October 30, 2003, Chair Snowe formally requested that the Congressional Budget Office (CBO) analyze the impact of reserve component call-ups on small businesses and examine the potential costs and effectiveness of options to alleviate hardships without weakening our national defense.

Since requesting the CBO study, Chair Snowe has collaborated with the CBO to ensure that its report will be comprehensive and helpful to lawmakers interested in assisting small businesses negatively affected by Guard and Reserve deployments.

2. *Letter to Administrator Hector Barreto Concerning the SBA's Role in Assisting Small Businesses Affected by Guard and Reserve Deployments*—On May 11, 2004, Chair Snowe sent a letter to SBA Administrator Barreto recognizing the SBA's efforts to assist small businesses negatively impacted by Guard and Reserve deployments. In that letter, Chair Snowe encouraged the SBA to be vigilant in efforts to respond to small businesses impacted by the deployment of Guard members and Reservists, and to reach out to veterans to provide them with the benefits and services they have earned.

B. VETERAN AND SERVICE-DISABLED VETERAN SMALL BUSINESSES

In 1992, the Census Bureau's Economic Census, Characteristics of Business Owners (CBO92–1), estimated that approximately 4.2 million American small businesses were owned by veterans, including approximately 313,000 small businesses owned by disabled veterans. More current data will be available with the Bureau's release of its 2002 Survey of Business Owners and Self- Employed Persons.

Despite the lack of accurate data on the number of veteran and service-disabled veteran small businesses in the United States, it remains apparent that the courageous men and women that own and work for these businesses face unique challenges in maintaining and expanding strong enterprises. Chair Snowe has taken numerous steps to help these businesses overcome those challenges.

1. *Advisory Committee on Veterans Business Affairs*—Congress has determined that the Federal Government must provide better assistance and support to veterans in their efforts to form and expand small businesses. In 1999, as part of this effort, Congress established an Advisory Committee on Veterans Business Affairs. Its responsibilities included providing advice to Congress and the SBA on policy initiatives that would promote entrepreneurship by veterans. Those duties were to be taken over by the National Veterans Business Development Corporation on October 1, 2004. The Advisory Committee's role is sufficiently beneficial that it should not be subsumed within the National Veterans Business Development Corporation. As a result, on July 8, 2003, Chair Snowe, and original cosponsor and Ranking Member Senator John Kerry, offered S. 1375, the SBA 50th Anniversary Reauthorization Act of 2003, which included a provision to authorize an extension of the Advisory Committee as a separate entity to continue its functions through September 30, 2006. This language was subsequently included in the Consolidated Appropriations Act of 2004.

2. *Reconfirming that the National Veterans Business Development Corporation is a Private Entity*—The National Veterans Business Development Corporation (the "Veterans Corporation") was established by Public Law 106–50. The Veterans Corporation is responsible for expanding and improving access to technical assistance regarding entrepreneurship for the Nation's veterans, and is charged with assisting veterans, including service-disabled veterans, with the formation and expansion of small businesses by working with and organizing public and private resources, including those of the Small Business Administration, the Department of Veterans Af-

fairs, the Department of Labor, the Department of Commerce, the Department of Defense, the Service Corps of Retired Executives, the Small Business Development Centers, and the business development staffs of each department and agency of the United States.

During the 108th Congress, a ruling by the Department of Justice concluded that the Veterans Corporation was a federal agency and thus subject to, among other things, federal administrative, personnel, and procurement laws. Congress, when it created the Veterans Corporation, never intended for it to be considered a federal agency. The legislation mandated sufficient fund-raising by the Veterans Corporation that would eliminate the need for federal funding. If the Veterans Corporation is held to the vast requirements of a federal agency, it will likely fail to ever become self-sufficient, or to provide the level of services to veterans that Congress had envisioned.

To honor Congress's original intent concerning the status of the Veterans Corporation, on July 22, 2004, Chair Snowe introduced S. 2724, originally co-sponsored by Ranking Member John Kerry, and Senator James Talent. S. 2724, which passed the Senate by unanimous consent, would reconfirm that the Veterans Corporation is to be considered and treated as a private entity and not an agency or instrumentality of the federal government. The language from S. 2724 was included in the Consolidated Appropriations Act of 2004.

XII. ASSOCIATION HEALTH PLANS (AHPS)

Much progress was made during the 108th Congress on Associated Health Plans (AHPs). On February 5, 2003, the Committee held a hearing to explore opportunities by which to reduce the number of uninsured Americans. In her opening statement, Chair Snowe began by outlining the contradiction that plagues the nation's small business sector: although small businesses play a significant role in the American economy, their well-being, and that of their employees, is consistently undermined by exorbitant health insurance costs.

Two-thirds of all Americans rely on their employer for health insurance and insurance premiums have been increasing rapidly for almost two decades. This rising cost acts not only as an anchor on company growth, but also prohibits businesses from providing adequate health coverage. In fact, the number of employers that cannot provide any health insurance is growing. Small businesses in particular are affected because they are forced to pay higher premiums than larger businesses—a debilitating comparative disadvantage. The created AHP legislation allows small businesses to negotiate better terms for small group health plans by utilizing the same group bargaining principles employed by unions and big businesses. This would be the first step to leveling the playing field and protecting millions of our nation's families and small businesses.

AHPs have gained increasing support and recognition. President Bush addressed his support of AHPs in his State of the Union address in January, 2004. In addition, President Bush continued to publicly urge passage of AHPs by the Senate throughout 2004, as did Secretary of Labor Elaine L. Chao. There is also growing bipartisan support of the issue. Senator Frist has expressed his support and Senator Byrd co-sponsored S. 545, the Small Business

Fairness Act of 2003. AHPs have also been included in the Senate Task Force on Uninsured's Report.

A. S. 545, "SMALL BUSINESS HEALTH FAIRNESS ACT OF 2003"

The Committee introduced this bill on March 6, 2003. This bill will amend Title I of the Employee Retirement Income Security Act of 1974 to improve access and choice for entrepreneurs with small businesses with respect to medical care for their employees. This bill was similar to a bill passed by the House. The bill was read twice and referred to the Senate Committee on Health, Education and Labor. This Bill has not passed the Senate.

XIII. REGULATORY ISSUES

A. S. 818, "INDEPENDENT OFFICE OF ADVOCACY ACT OF 2003"

This Committee introduced this bill on April 8, 2003. This bill was introduced for several reasons. Excessive regulations continue to burden U.S. small business concerns and Federal agencies are reluctant to comply with the requirements of chapter 6 of title 5, United States Code, and continue to propose regulations that impose disproportionate burdens on small entities. The Office of Advocacy of the Small Business Administration (referred to in this Act as the "Office") is an effective advocate for small entities, including small business concerns, that can help to ensure that agencies are responsive to small business concerns and that agencies comply with their statutory obligations under chapter 6 of title 5, United States Code, and under the Small Business Regulatory Enforcement Fairness Act of 1996 (Public Law 104–121; 106 Stat. 4249 et seq.). The independence of the Office is essential to ensure that it can serve as an effective advocate for small business concerns without being restricted by the views or policies of the Small Business Administration or any other executive branch agency. The Office needs sufficient resources to conduct the research required to assess effectively the impact of regulations on small business concerns, and the research, information, and expertise of the Office make it a valuable adviser to Congress as well as the executive branch agencies with which the Office works on behalf of small business concerns.

S. 818 was designed to ensure that the Office has the statutory independence and adequate financial resources to advocate for and on behalf of small business concerns. It requires that the Office report to the Chairmen and Ranking Members of the Committees on Small Business of the Senate and the House of Representatives and the Administrator of the Small Business Administration in order to keep them fully and currently informed about issues and regulations affecting small business concerns and the necessity for corrective action by the regulatory agency or the Congress. It would provide a separate authorization for appropriations for the Office and would authorize the Office to report to the President and to the Congress regarding agency compliance with chapter 6 of title 5, United States Code. This bill has not passed the Senate.

B. S. 2834, "THE SMALL BUSINESS COMPLIANCE ASSISTANCE ENHANCEMENT ACT"

The Small Business Compliance Assistance Enhancement Act (S. 2834) was originally developed as a regulatory reform component for the Republican Minimum Wage alternative package, and then was introduced late in the 108th Congress. Key components of this bill were drawn from shortcomings in current law identified in a GAO report #GAO–02–172, "Regulatory Reform: Compliance Guide Requirement Has Had Little Effect on Agency Practices", which described the poor job agencies have done in meeting the requirements of SBREFA, Section 212, which direct agencies to produce small entity compliance assistance guides for regulations that trigger a Final Regulatory Flexibility Analysis, essentially those that will have a significant economic impact on a substantial number of small entities. The GAO report showed that agencies all but ignored this provision, and when they did try to meet it, their efforts were meager at best.

The bill clarifies the terms of Section 212 such as when a compliance guide is required, what is meant by compliance assistance, the time frame for producing such a guide, and how the guide must be published. In addition, the bill makes explicit that while these guides may include suggestions for procedures to comply with the regulations, such suggestions are not to be the basis for enforcement. This bill has not passed the Senate.

C. EQUAL ACCESS TO JUSTICE ACT REVISION FOR OSHA

The House passed the Occupational Safety and Health Small Employer Access to Justice Act (H.R. 2731), which would allow small employers to be awarded attorneys' fees and court costs when they contest OSHA citations and prevail in court. Current law (The Equal Access to Justice Act, EAJA) only allows small businesses to recover attorney's fees in cases against the government if they win, and they can establish that the government's case was not "substantially justified." This has proven to be a difficult requirement for small businesses to overcome. H.R. 2731 eliminates this requirement, only as it applies to cases involving OSHA. At the same time, H.R. 2731 also reduces the number of small businesses who can recover their fees. EAJA allows small businesses up to 500 employees and $7 million net worth to seek recovery of their legal fees if they win their case and can prove the government's case was not "substantially justified." H.R. 2731 reduces the size of businesses eligible to only 100 employees and a net worth of $7 million. Therefore, it targets the relief to those who are truly in need of it and limits the impact on the government's ability to pursue their case.

Testimony at hearings held on this legislation in the House Committee on Education and the Workforce, revealed that it can easily cost $20,000 or more to litigate a challenge to an OSHA citation that is for $8,400. When presented with that choice, many small businesses will choose to settle, regardless of whether they think the citation is valid. This calculation undermines the fundamental principle of American law that an accused is innocent until proven guilty. If they knew that they would be able to recover their costs if they can win their case, small businesses would likely be more willing to challenge OSHA citations they did not think were valid.

Under current law, small businesses must win their case, and then prove in a subsequent proceeding that the government's case was not "substantially justified."

A review of the current EAJA statistics shows that since its enactment (1981–2003), only 111 small businesses have filed EAJA claims for OSHA cases, and of these, only 37 have been granted. This bill has not passed the Senate.

XIV. Miscellaneous

A. SMALL BUSINESS & CHINA'S CURRENCY MANIPULATION

Through the practice of pegging its currency to the dollar, China artificially maintains the yuan at 8.28 per dollar. Economists estimate that the yuan is undervalued by between fifteen and forty percent. The undervaluation makes Chinese manufactured goods cheaper in the U.S. while simultaneously making U.S. manufactured goods more expensive in China.

China's currency manipulation has greatly contributed to our nation's trade deficit, which we must get under control. As noted by the U.S.-China Economic and Security Review Commission in 2003, ". . . [t]he U.S. trade deficit with China constituted 23.2 percent of the total U.S. goods trade deficit and China was the largest single country component of the overall deficit."

The manufacturing sector, which is the sector most impacted by international trade, has experienced severe job losses in recent years as a direct result of China's unfair trade practices. Chair Snowe is deeply concerned with the affect that China's currency practice is having on U.S. small businesses. Throughout the 108th Congress, Chair Snowe took numerous steps, some of which are described below, to address this important issue.

1. *GAO Study on the Effect of China's Currency Manipulation on U.S. Exporters*—On July 23, 2003, Chair Snowe and Congressman Manzullo, Chairs of the Senate and House Small Business Committees, requested that the United States General Accountability Office conduct a study concerning China's currency practice and its affect on our nation's economy. The report has not yet been released.

2. *Letter to Secretary of the Treasury John Snow*—On June 15, 2004, in response to the U.S.-China Economic and Security Review Commission's 2004 Report to Congress, Chair Snowe sent a letter to Treasury Secretary Snow highlighting the findings in the Report, and urging Treasury to take speedy and decisive action to address the China currency situation. Chair Snowe's letter stated that China should take active steps to reform its banking system and financial markets so it can progress toward the goal of a market-based evaluation of its currency, and that it is imperative that in the interim the yuan be substantially revalued upward against the dollar.

3. *Letter to the United States Trade Representative and the Department of Commerce*—On June 15, 2004, Chair Snowe also sent letters to Secretary of Commerce Donald Evans and U.S. Trade Representative Robert Zoellick in response to the U.S.-China Commission's 2004 report, strongly encouraging the Administration to utilize, in conjunction with diplomatic efforts, all U.S. and International trade laws to the full extent possible in protection of U.S.

trade interests. Chair Snowe's letter addressed a number of areas in which China needs to improve to ensure fair U.S.-China trade. Chair Snowe's letter highlighted:

a. international property rights, including the rampant piracy of copyrighted U.S. material and its cost to U.S. industries;

b. China's direct and indirect subsidies to Chinese producers;

c. reports of forced transfer of U.S. technology in return for market access and regulatory approval; and

d. China's currency manipulation.

XV. Appendixes

A. HEARINGS OF THE COMMITTEE, FIRST SESSION

"The Small Business Healthcare Crisis: Possible Solutions", Washington, D.C., February 5, 2003

On February 5, 2003, the Committee held a hearing to explore opportunities by which to reduce the number of uninsured Americans. In her opening statement, Chairwoman Snowe began by outlining the contradiction that plagues U.S. small businesses: although small business plays a significant role in the American economy, their well-being, and that of their employees, is consistently undermined by exorbitant health insurance costs. Snowe pointed to a chart showing that two-thirds of all Americans rely on their employer for health insurance and that insurance premiums have been increasing rapidly for almost two decades. This rising cost acts not only as an anchor on companies growth, but it also prohibits businesses from providing adequate health coverage. In fact, the number of employers that cannot provide any health insurance is growing. Small businesses in particular are affected because they are forced to pay higher premiums than larger businesses—a debilitating comparative disadvantage. Snowe made it clear that creating legislation that allows small businesses to negotiate better terms, as unions and big businesses do, would be the first step to leveling the playing field and protecting millions of our nation's families and small businesses.

The hearing consisted of four panels. The first panel was made up of the Honorable Elaine L Chao, Secretary, U.S. Department of Labor. She provided the Committee with the President's proposals to address health care costs and lack of access. These included making medical savings accounts more available, medical malpractice reform, individual tax credit, and associated health plans (AHPs).

Secretary Chao focused on AHP's as the tool to break down many of the barriers that discourage small employers from offering health plans, namely cost, legal and market barriers, and the threat of fraud. Under AHP's, small businesses would enjoy greater bargaining power, economies of scale, and administrative efficiencies as well as the benefits of a uniform Federal regulatory structure. To combat fraud, AHP's would have to meet Federal certification standards and comply with the Department of Labor's ongoing oversight. Secretary Chao assured the Committee that the Department was adequately equipped to handle all oversight responsibilities.

After Secretary Chao's testimony, Senator Levin presented a letter from the Blue Cross-Blue Shield of Michigan which expressed concern that AHPs would increase cherry-picking and adverse selection. Secretary Chao recognized this possibility and felt that a final draft of AHP legislation would need to be crafted to avoid those particular consequences.

The second panel consisted of the Honorable Hector Barreto, Administrator, U.S. Small Business Administration. Administrator Barreto emphasized the cost of health care insurance as the major deterrent to small business employers' ability to provide coverage. Without being able to offer affordable, comprehensive plans, small employers are at a serious competitive disadvantage when trying to hire or retain employees from larger companies. However, Administrator Barreto felt that by removing legal barriers and allowing AHPs to flourish, small businesses would begin to see substantial cost savings-administrative costs would decrease and resultant prices would reflect the discounts brought on by high volume purchasing. He went on to address the impact that health care costs have had specifically on the Hispanic population and other minority small employers.

The third panel consisted of six witnesses. The first two were small employers from Maine: Kathie M. Leonard, Co-founder and President, Auburn Manufacturing, Inc.; and Anne Valentine, President, SmartCatalog. Both witnesses decried the steady trend of rising health insurance premiums and how they led to decreasing coverage and higher co-pays for their employees. Ms. Leonard believed that immediate action was required and to stem the tide of swelling costs AHPs need to be introduced. Still, she argued that more far-sighted approaches need to be developed.

Ms. Valentine related to the Committee that she had created an association of small businesses through which to purchase health insurance but that it was too small to be effective. She looked forward to the passing of AHPs because it would be good for her business as well as her employees. Outrageous insurance premiums demand so much money that small employers cannot afford to invest in their businesses and cannot retain or hire good employees who usually opt to work for a company that can offer decent, affordable health benefits.

The next three panelists were Jack Faris, President and Chief Executive Officer, National Federation of Independent Business; Terry Neese, President and Co-Founder, Women Impacting Public Policy; and Harry Alford, President and Chief Executive Officer, National Black Chamber of Commerce. All three witnesses felt that this insurance emergency required government intervention and looked forward to the passing of AHP legislation. Mr. Faris condemned the current administration costs associated with health insurance along with the ever-growing list of state mandates that increased costs for working families. Mr. Neese agreed and added that the cost of insurance to both employers and employees ate up disposable income that could otherwise be invested in ones business or be spent in other sectors of the economy thereby fueling growth for the whole nation. Mr. Alford added his support for AHP's right before the panel's last witness, Cliff Shannon, President, SMC Business Councils, representing the National Small Business United and SMC Business Councils, aired his suspicion.

Mr. Shannon, although he felt the concept of AHPs were a worthy pursuit, wasn't an advocate for the current legislation because it had weaknesses that made it harmful overall. According to him, the current AHP bill would allow for adverse risk selection, less coverage, and increased costs under state-regulated insurance panels.

The fourth and final panel consisted of three witnesses. The first was Judith L. Lichtman, President, National Partnership for Women and Families. Although she stated that women were disproportionately affected by the health insurance problems, she did not back AHPs as a solution. She felt that they would drive up premiums, decrease coverage, and increase fraud as tough consumer protection laws were replaced with minimal government oversight and solvency standards. She suggested small employer tax credits, an FEHBP or state employee pool, and allowing Medicaid and SCHIP and Medicare to cover the uninsured.

Next was Sandy Praeger, Commissioner for Insurance, State of Kansas, representing the National Association of Insurance Commissioners. According to Ms. Praeger, AHPs do not protect consumers against plan failures and fraud and cherry picking, nor do they reserve patients' rights. AHPs would also destabilize the states' small group markets which she wanted to expand.

The final panelist was Len Nichols, Vice President, Center for Studying Health System Change. Mr. Nichols claimed that AHPs were not worth the risk when there were other viable options. He felt that buying into existing pools like a state employee pool, FEHBP, Medicaid, or SCHIP was much safer and more effective. It would minimize administration costs, the enrollment apparatus would be simple, and the risk pool would be stable over time. He also suggested that the most efficient way to increase health insurance coverage would be to subsidize low-income workers directly and let them buy insurance on their own.

In closing, Snowe noted that since the advent of AHPs, the health care problem has turned into a crisis and the time to act on behalf of small employers, their employees, and the uninsured was now. She recognized that AHPs are not the exclusive option in the fight for affordable health care and encouraged the participants to remain involved as the Committee worked to provide a solution for the uninsured.

"Small Businesses Continue To Lose Federal Jobs by the Bundle", Washington, D.C., March 18, 2003

On March 18, 2003, the Committee held a hearing to explore the issues surrounding contract bundling. Chairwoman Snowe said that despite the Administration and Congress's efforts over the past several years to increase small businesses' access to federal procurement contracts, there has been a disturbing trend in the opposite direction. In effect, America's small businesses are being eroded by Federal agencies' practice of contract bundling which diminishes the role of small business in government projects. The Federal government does want to support small businesses it also has the contradictory goal of cutting costs and becoming more efficient. The challenge is to reconcile these two policy objectives of saving government funds and saving small businesses. The hearing sought to attract greater attention to the contract bundling issue, to examine the administration's actions concerning it, and to identify positive, constructive change that will ensure the Federal government continues to provide contracting opportunities for our small businesses while addressing the obstacles that remain. In her opening, Snowe specifically mentioned the Administration's e-government program as a means to make the government operate more efficiently and effectively by using best practices among government procuring offices to purchase goods and services faster and cheaper.

The first panel consisted of four witnesses. Hector Barreto, Administrator, U.S. Small Business Administration, led off by faulting the contract reforms of the mid 1990s for exacerbating an already difficult situation for small employers. Repercussions exist for the country as well, Administrator Barreto told the committee, because small business participation is necessary for innovation, cost-savings, and increased employment.

Improvements to the procurement environment, however, are being made thanks to the Administration's leadership and initiative. The SBA recently participated in an OMB report to the President that outlined a nine step strategy for increasing contracting opportunities for small businesses and for mitigating the effects of necessary contract bundling. This report proposed changes for the SBA and the FARC's respective regulations. The details of the report were submitted for the record.

Finally, to highlight other efforts the SBA takes to minimize the effects of bundling, Administrator Barreto listed some of their existing programs and informed the Committee of some new ones that included a matchmaking program, the establishment of the Small Business Procurement Advisory Council, and on-line procurement academies.

Following Administrator Barreto was Ms. Angela B. Styles, Administrator for Federal Procurement Policy, Office of Management and Budget. Administrator Styles agreed with many of the points made prior and she reiterated the detrimental effects contract bundling has on small business and the government and the taxpayers. In reference to the OMB report, she said that the nine strategic points can be grouped into three categories: promoting leadership and accountability; closing regulatory loopholes; and mitigating the effects of necessary and justified contract bundling. In response to the goals of this report, Administrator Styles stated that agencies are now reporting on a quarterly basis to the OMB on their actions to implement the report's nine recommendations and the OFPP has drafted a new set of bundling regulations for FARC and the SBA that will undo loopholes that previously allowed contracts to escape reform. Administrator Styles also expressed that oversight of each agency would best be handled by each agency's designated personnel.

The third witness was Ms. Deidre Lee, Director, Office of Acquisition, Department of Defense. Director Lee testified that due to the acquisition reform of the mid 1990s and the increased demands on the DOD, contract bundling does occur but only if market research and a benefit analysis indicate substantial benefit by doing so. Even still, she assured the Committee that in cases where contracts are bundled the DOD seeks to maximize small business participation. She pointed out that the number of small business prime contractors performing DOD contracts increased in the last year—evidence of the department's commitment to small firms and the Administration's goals. Concerning the recent OMB report, she said that the DOD puts emphasis on five areas: Orders previously placed under GSA schedules or other contracts which were not in the definition must be focused on; early involvement of small business specialist; find alternatives to bundling; suggested changes to the Office of Small and Disadvantaged Business; and strengthen the compliance with small business subcontracting plans.

In addition, the DOD prepared a supplemental policy letter to the OFPP report that stressed the need to emphasize those five points plus one extra: the accountability of senior agency membership to small business interests.

The panel's final witness was David E. Cooper, Director, Acquisition and Sourcing Management, U.S. General Accounting Office. Director Cooper told the Committee that the GAO supported the President's plan addressing contract bundling in theory but was skeptical about successfully implementing it. Specifically, the GAO would like to see a clearly established system of measuring of an agency's efforts to achieve the objectives of the plan and to hold senior managers accountable for those results.

Director Cooper was also concerned that the SBA and agency offices of the SDBU would not be able to meet the added responsibilities that the plan gives them. This belief was founded on prior GAO reports. Consequently, the GAO recommends that the SBA strategically assess, evaluate and plan their staff needs in order for them to prepare for and carry out the administration's plan.

The second panel was made up of four witnesses as well, the first one being Mr. Eric Adolphe, Chief Executive Officer, OPTIMUS Corporation. As the owner of a small business, Mr. Adolphe knew first hand the obstacles to growth that contract bundling sets before small firms. He noted in particular that even though many large omnibus contracts are awarded partly on the pledge to subcontract a certain amount of work to small businesses, there is no legal recourse for small contractors when the pledges are not upheld. Also, small businesses are being shut out of many Federal contracts of a size that once went to small firms and they aren't being compensated for their bid and proposal expenditures. He then spoke out for the government and its taxpayers who he feels often receive lower quality goods and services at a higher price due to bundled contracts. Mr. Adolphe ended more positively by recognizing the improvement in the contracting best policies by the FAA and GSA.

The Committee then heard from Paul Murphy, President, Eagle Eye Publishers. His company had recently completed a study on contract bundling. Their findings showed that contract bundling was costing small business billions of dollars and making it increasingly difficult for small employers to compete and survive in the Federal marketplace. The service sectors i.e. manufacturing, R&D, and construction were the primary engine of growth for bundled contracts; and GSA schedules, multi-award contracts, BOAs, and indefinite delivery/indefinite quantity contracts were the most frequently used contract vehicles for bundling. The report concluded that in order to more accurately depict bundling activities, bundling's definition needed to be broadened to include the process of accretive bundling.

Testifying next was Michael Robinson, Defense Logistics Manager, Massachusetts Manufacturing Extension Partnership. He contrasted the Administration's plan to reduce contract bundling with S. 2466 introduced by Senator John Kerry. The bills' major difference was their proposed thresholds at which a contract was required to undergo unbundling actions. Mr. Robinson applauded both bills' effort to increase the quantity and quality of teaming arrangement opportunities, a necessary goal to satisfy the broad range of DOD procurement requirements. He continued by underscoring the DOD's responsibility in maintaining a healthy, domestic manufacturing sector. Many U.S. manufacturers are not only small businesses, but they account for a significant portion of this country's employment and it is essential that this sector has the capacity to support U.S. warfighters at all times.

The hearing's last witness was Ms. Carol Kuc, Women Impacting Public Policy. She reminded the Committee that the aim of PL 106–554, to assist agencies in awarding at least 5% of Federal contracts to women-owned businesses, had not been achieved. Keeping us from the objective were, Ms. Kuc thought, agencies structured to keep out small business contractors, and an anti-women's small business culture among contracting officers. To overcome this she recommended that the OFPP publish a monthly scorecard on awards to small businesses, and reward prime contractors who use small businesses or influence their subcontractors to seek out small business subcontractors. Other suggestions included: give SBA and OSDBUs the authority and resources to review contracts; clean up the CCR, Pro-net, and GSA small business databases to verify who is still a small firm; review contracts over $100,000 for small business participation; and federal certification should be created and accepted by states and localities.

In closing, Snowe thanked the witnesses and communicated that although she felt improvements had been made concerning contract bundling, more were needed. She hoped that the SBA reauthorization process would offer an opportunity to enact some of the suggestions given at the hearing. She assured the witnesses that she would continue to fight for the terms initiated by the administration on behalf of small business.

Roundtable Entitled "SBA Reauthorization: Non-Credit Programs", Washington, D.C., April 9, 2003

On April 9, 2003, the Committee held a roundtable to discuss the status of the Small Business Administration's non-credit programs with respect to the agencies 50th anniversary reauthorization. According to Chair Olympia J. Snowe, this roundtable was to provide information for the Committee, the Members, and the staff as they prepare for the reauthorization and continue the Committee's oversight of the agency. Specifically, the focus of the roundtable was on the SBA's Office of Advocacy, entrepreneurial programs, and government contracting assistance.

In her opening statement, Chair Snowe stressed the need to level the playing field for small business and make sure that it has opportunities in the Federal marketplace. The SBA's non-credit programs aid in achieving this goal by helping to cut regulatory costs, offering avenues for entrepreneurial development and assisting with government contracting opportunities. Chair Snowe stated the importance of improving these and other SBA resources and in keeping an active discourse concerning SBA programs. The roundtable discussion was intended to bring to light many key issues affecting the SBA's non-credit programs.

Tom Sullivan, Chief Counsel, SBA Office of Advocacy, started the discussion by giving a brief summary of operations and staff levels. The Office of Advocacy pursues an independent small business agenda in three ways: (1) through regional advocates that work at the street level to gather and prioritize issues facing small businesses; (2) a research team made up of economists and researchers who gather data on small business; and (3) a legal team that provides solutions and perspective from small business into the rulemaking process, which in FY 2002 resulted in a savings of $21 billion in fore gone regulatory costs. Staffing was adequate at the moment.

Following Mr. Sullivan, a number of participants voiced their feelings on S. 818 for the independence and nonpartisan workings of the Office of Advocacy. It was of general consensus that the Office of Advocacy should receive a separate line item for its budget, but that it should not function completely independent of the Administration. Giovanni Coratolo, U.S. Chamber of Commerce, commented that a line item would allow small business groups to defend the organization and encourage funding. Andrew Langer, NFIB, mentioned that a line item would create greater transparency for budgets. Jere Glover, Small Business Technology Commission, pointed out that it is good that the Office of Advocacy is part of the Administration; it allows Advocacy to educate decision makers and influence decisions. It was accepted that one-foot-in the Administration and one-foot-out would allow for more affective policy debate with the White House and Senior Administration.

The second section of the roundtable concentrated on the SBA's entrepreneurial programs. Karen Street, Office of Entrepreneurial Development, SBA, gave a brief overview of the SBA's entrepreneurial programs as a backdrop for the discussion. In 2002, the SBA's entrepreneurial programs, which include SCORE, SBDCs, Women's Business Centers, Business Information Centers and the new Native American Economic Impact Program, assisted 1.5 million clients. Ms. Street marked sustainability funding for Women's Business Centers, as well as, restructuring SBDCs to allow for broader competition of centers and ideas as major issues.

Susan Au Allen, US Pan Asian American Chamber of Commerce, raised the issues of how to increase the number of small and minority owned businesses that benefit from the SBA's programs, and how these firms can sustain business over time. She listed difficulty in replacing incumbent businesses and a lack of ample mentoring in management, financial processes and strategic alliances with other companies as key concerns.

Anne Sullivan, Women Impacting Public Policy, was worried that the SBA did not offer enough guidance on expansion and would also like to see sustainability grants beyond a five-year funding period. Ellen Golden, Association of Women's Business Centers, voiced caution in removing SBA grants or restructuring programs. She believed that: (1) SBA funding gives programs credibility and helps these programs to receive additional funds; and (2) that it takes time to become knowledgeable, gain trust in a community and create an affective infrastructure, which could be lost by restructuring.

Marilyn Nelson, National Women's Business Council, brought up the topic of reauthorizing the Women's Business Council. Ms. Nelson wanted to work to include language that would allow for the replacement of members when they leave their seats, along with allowing the Council to meet with Federal agency representatives to inform them of activities instead of reconstituting the Committee on Women's Enterprise. Ms. Nelson also would like to see more data and research done on women's business and offered the NWBC as a facilitator.

Pete Homer, National Indian Business Association, discussed funding for Native American Businesses. He drew issue with the SBA delivery of service provider and the SBA central administrative office for the program. SBDCs have not affective for NIBA. They would much rather have the SBA use the SBA Tribal Business Programs for funding, while having the SBA Washington, D.C. office and the Native American Affairs Committee oversee the programs.

Ken Yancy, SCORE, reported that SCORE would like to expand relationships with minorities, is increasing its recruiting, and is providing better Internet counseling.

Zach Gast, Association for Enterprise Opportunity, spoke on PRIME. These are very-low income clients and the investment focus to assist these clients should go towards human capital to help these businesses succeed.

Donald Wilson, ASBDC, concluded the second section of the roundtable stating that restructuring of the SDBCs should not be a viable option and that it would be like pulling the rug out from under these centers.

At the conclusion of this section Senator John Kerry added a few remarks relating to the independence of the Office of Advocacy and the restructuring of the WBCs and SBDCs. He echoed much of the sentiment regarding the independence of the Office of Advocacy and believed that change to the WBCs and SBDCs should be done very carefully.

The final section for discussion centered on government contracting and business development programs. Steve Denlinger, LAMA, first addressed the 8(a) program with particular focus on the artificially low entry criteria of $250,000 net worth. Suggestions were made that a study be conducted and new reasonable net worth criteria be created for each respective industry. Second, he spoke on the 7(j) program, believing it to be lacking in definition and funding, and stretched on a number of special programs. Thirdly, he proposed the resurrection of the advance payments program to support the growth and nourishment of minority enterprises just getting into the Federal-contracting arena. Next, the need for more PCRs was raised. Finally, Mr. Denlinger discussed size standards. He suggested a tiered approach to competing contracts, with levels of $1 to $10 million, $10 to $25 million, and $25 to $100 million.

James Turpin, American Subcontractor Association, questioned the government practice of bid shopping or reverse auctioning. He also mentioned that Federal pay protection should be expanded to include work done under Federal grants. One final concern addressed contract bundling; in particular, businesses have little knowledge as to who enforces the bundling and unbundling of contracts.

Major General Charles Henry, Veterans Corp, was wary of competition of contracts for competition sake, but felt it was effective to supply contractors with clear metrics. Discretionary authority of contracting officers was also a concern, in that the government wide goals have not been met because the goals have no teeth. A possible remedy being that if you do not meet your budget, you do not receive funding.

Ron Newlan, HUBZone Contractors National Council, offered a brief background of the HUBZone program. The design aspects of the program appeared to be solid, but implementation of the program has been quite flawed. The program is authorized $10 million annually, yet during its highest year of funding, only $2 million was appropriated in the SBA budget for the HUBZone program management and oversight. Duly noted, were concerns for inadequate funding of business certification oversight, and agencies failing to comply with contracting goals.

Some participants commented on reducing GSA scheduled paperwork to help small businesses. Others added that businesses should begin to look elsewhere for funding outside the Federal government.

Sen. Mike Enzi concluded the discussion with his statement, embracing the Technical Rural Outreach Program, anticipating comments regarding the SBDCs, and placing special interest in addressing government contracting issues and furthering the SBIR program.

Roundtable Entitled "SBA Reauthorization: Credit Programs (Part I)", Washington, D.C., April 30, 2003

On April 30, 2003, the Committee held the first in a series of two roundtables on the reauthorization of SBA credit programs. This initial gathering focused primarily on the 7(a) Loan Guarantee Program, a program Chairwoman Snowe said "has had a profound effect on America." Over the last three years, 7(a) lenders were responsible for $28 billion in loans to start-up and existing businesses. Regardless, however, of the program's successes and past improvements, i.e., the reduction of fees and the burden of paperwork, Snowe called on the participants to provide ideas for new improvements as well as a report card on the old ones.

Tony Wilkinson, President and CEO of the National Association of Government Guaranteed Lenders (NAGGC), started the discussion by saying that the Administration's 2004 budget request of $9.3 billion for the 7(a) program was insufficient and if no more funds were allocated, steps to limit loan volume would have to be taken next year. Mr. Bews, speaking on behalf of the SBA, and the only dissident, disagreed with Mr. Wilkinson and said that $9.3 billion was an adequate amount and it agreed with historical numbers. Mr. Wilkinson replied by saying that the historical numbers are no longer accurate because current loan caps of $500,000 keep down lending activity and the incidents of September 11, 2003 have dramatically increased loan volume.

Mr. James Ballentine of the American Banker's Association stated that more lenders were joining the program and consequently more loans would be made. He pointed out that such a situation calls for more money if we want to avoid loan caps that will make funds available to only smaller borrowers while neglecting the needs of the larger ones. In defense, Mr. Bews repeated his earlier statement and added that smaller loans generate more jobs, therefore more small loans at the expense of larger ones was acceptable—especially in today's environment of high unemployment. Mr. Ballentine countered that job retention is as important as job creation and often requires larger loans. The 7(a) program is a long-term credit program and, in particular, manufacturers use it to buy expensive specialty equipment that requires larger loans.

Concerning the Preferred Lender Program (PLP) and the Express Program (EP), Mr. Byrnes, a small business lending manager from Maine, spoke first. He was advocating for the expansion of both programs. Since the latter program's introduction in 1998, SBA loans have increased more than tenfold. This is because the EP reduces paperwork, streamlines the loan process, and significantly decreases the closing costs. Mr. Bew elaborated on some of the recent changes made to the EP, especially those that have resulted in increased minority lending, such as the making available of smaller loans.

Deryl Schuster, Business Loan Express, was not so pleased with the PLP, or more specifically, with the administering of its expansion and membership renewal. He felt that the expansion and renewal processes currently drove good lenders from SBA loan participation, discouraged lenders from committing resources to loan programs, and made it very difficult to maintain approval as a PL. His suggestion, one that others supported, was to create a national PLP that had stringent standards. Ms. D'Agostino, GAO, reminded all present that it was important to have strong oversight of the PLP because it lends out a very large sum of money each year. In FY 2002 it lent $7 billion in government guaranteed loans which amounts to significant exposure for the taxpayer. The GAO conducted a study to evaluate SBA's oversight and found that the program does not adequately focus on the 7(a) portfolio risk at both bank lenders and the SBLCs. The GAO has made several recommendations that the SBA agrees with. The GAO is also studying the new 7(a) credit subsidy model and SBA's transformation initiatives.

Another issue raised concerned the Microloan Program (MP). Mr. Corbet, Executive Director, Go Connection, felt that the MP is underfunded. The current allocation doesn't meet the AEO's recommendation to the Committee, especially for the MP's technical assistance. Collectively, MP businesses owe the government $96 million and many will go out of business without technical assistance. The allotted amount also threatens the MP itself, a program that has created 34,000 jobs in four years and offers capital to a type of borrower that no one else lends to. Even the Community Express Plan, a supposed cheaper alternative to the MP, will not aid these microborrowers. Mr. Corbet also expressed concern about the consolidation of technical assistance programs.

If the MP has to share a budget, they will not be able to provide the level of aid necessary as their concerns get less priority. Mr. Bew responded by saying that the MP needed to become more efficient and productive. Blake Brown, CFO, Coastal Enterprises, agreed with Mr. Corbet's funding concerns and also expressed a desire for a more uniform interest rate among loans and the elimination of state funding restrictions. Others continued to extol the work of the MP and its unique and powerful affect on communities and the economy as a whole. For the exception of Mr. Bew, all lobbied for increased funding for the program that earns over two dollars for every one spent on it.

Paul Merski, Independent Community of Bankers, spoke about the current fees for banks who work with SBA loans. Mr. Merski represented all participants when he said that the fees could not be raised. This was one of the points that David Bartram, President of the SBA Division, U.S. Bank, highlighted from NAGGL's ten point legislative package. The reason for this is that SBA loans are only marginally profitable and any raise in the fees would eliminate any incentive for banks to take part in the programs.

Mr. Hearne, Credit Union National Association, wanted to cheer the recently adopted rule allowing credit unions more lending participation. He felt that with more lenders it would increase access to capital for the public. Mr. Merski was not so enthusiastic. The entrance of credit unions may raise the default rates on loans because credit unions have little to no experience in commercial lending. He requested that a database be kept on the default rate for credit unions versus current program lenders.

Greg Feldman, Gryphon Capital Advisors, promoted the idea of loan pooling. He illustrated the problems facing community bankers and how they are dealing with low levels of deposits due to bank consolidation and are thus struggling to find money for loans. He said that the SBA should add a compliment to the 7(a) program, a limited forum of guaranteed loan lenders, that would allow poolers and aggregators of small business loans to purchase those loans from the community banking system, sell them into the capital markets, and over a period of time have business loan category become much like the asset-backed categories of mortgages and auto loans. Mr. Bew said that the SBA had been exploring this option.

Roundtable Entitled "SBA Reauthorization: Credit Programs (Part II)", Washington, D.C., May 1, 2003

On May 1, 2003, the Committee held the second and final roundtable on the reauthorization of SBA credit programs. This event focused on the following programs: 504, Disaster Loan, and venture capital. Chairwoman Snowe opened by touting the programs' successes and hailed them as a source of growth for our economy and small businesses. In the last three years, Snowe cited, the 504 program created 325,471 jobs and SBICs invested over $17 billion in small businesses that in turn created and retained about a half-million jobs. She also pointed out the improved efficiency of the disaster assistance program's loan application process which was able to provide timely funds to many businesses affected by the terrorist attacks of September 11th.

The discussion began with Christopher Crawford, Executive Director, National Association of Development Companies (NADCO), a 504 trade association. He stressed the importance of the 504 program saying that over its lifetime it has created over a million jobs and the demand for its loans are growing. Loan volume grew 22 percent this year and 15 percent last year. He also expressed a dislike for the Administration's proposal to reauthorize the program every six years. Mr. Crawford reasoned that business lending is too dynamic a process to go unchanged for six years and needs to remain on its current reauthorization schedule of three years. There was a general consensus on these points.

Mr. Crawford also started debate about the subsidy model and the centralization pilot program. He felt that the subsidy model is inaccurate because it forecasts a lowly seventeen percent recovery rate on defaulted loans. He referenced a study that NADCO did where Certified Development Companies (CDCs), not the SBA, did their own liquidations. The result was a better than fifty percent average recovery on outstanding, guaranteed loans. The study also found that the SBA's Portfolio Management staff had workloads seven times greater than that of commercial banks' staffs. In the 106th Congress the committee authorized a liquidation pilot that allowed CDCs to do their own recoveries but we are still awaiting the regulations on that pilot that would make the program available to all qualified CDCs. Ron Bew, Associate Deputy Administrator, Office of Capital Access, SBA, said he would look into why that has not been done.

Concerning the centralization pilot, Mr. Crawford said that where it has been tried it has reduced loan processing time from 14–40 days down to 2–3. In support, Sally Robertson, Executive Director, Virginia Asset Financing Corporation, displayed the enormous amount of paperwork required for applying and closing a loan. She ventured that all CDCs are in favor of centralized processing. Others added that the paperwork adds to the costs of a business, delays getting money when its needed, and puts great administrative demands on both lender and borrower.

Julie Cripe, President/CEO, Omnibank, brought up that many daycare centers have a hard time getting 504 loans due to their non-profit status, even though she and Ms. Robertson have never had a daycare default on a loan of theirs. Ardith Wieworka, Commissioner, Massachusetts Office of Child Services, also wanted 504 loans to be made available to daycares because not only would such loans accomplish the spirit of the loans—provide jobs and allow others to seek jobs—but communities and children depend heavily on daycare services and these businesses need to be able to expand and accommodate communities' needs. Mr. Bew replied that, by statute, 504 loans are for for-profit companies only. Mr. Crawford added that lenders are wary of loaning to non-profits because if the establishments lose money then the lending prices go up and demand for loans goes down. He was willing, though, to support a pilot program.

With respect to the Disaster Loan Program, Davi D'Agostino, Director, Financial Markets and Community Investments, GAO, remarked positively that the program approved a tremendous amount of loans for 9/11 victims in a short amount of time, and that their performance goals were succeeded. And, although she recognized that the SBA was conducting a customer service survey to find areas in which they need to improve, she listed where GAO thought they needed to work on: protection of borrowers whose loans are being sold to the private sector, tracking of these borrowers' complaints, accounting of operational benefits achieved from loan sales, and explaining the significant decline in the subsidy allowance account for disaster loans. She mentioned that the SBA is addressing some of these suggestions and the progress of their actions was discussed.

Snowe raised the question if there was a need for distinguishing between the 7(a) and 504 programs? Although Mr. Bew pointed out that there was some overlap, the others agreed that the two programs serve their own unique purposes.

Snowe was forced to leave toward the end of the roundtable but her staff director, Mark Warren, took over in her stead. Mr. Warren began by addressing investment capital programs and he asked Lee Mercer, President, National Association of Small Business Investment Companies, to list the main issues. Mr. Mercer said that they hope to: maintain a zero subsidy rate, keep three year authorizations, clarify the SBA's intention in capital impairment, change the participating security distribution laws which will positively impact the subsidy rate, maintain the leverage cap, and take away the statutes that say all SBICs must invest 20 percent of their money in smaller funds because for larger SBICs it forces them to invest in far more portfolio companies than they have personnel to handle.

Mr. Warren followed up by posing the question whether the SBIC and NMVC programs were virtually the same? Participants answered no. They said that SBIC focuses more on funding small businesses while NMVC tries to fund low-income communities. Many felt that the strength of NMVC was that it reached under invested areas more effectively than SBIC but Mr. Mercer reminded those present that SBICs have supplied loans to a surprisingly diverse amount of areas, low-income included. Another difference in the programs is that NMVC provides a level of technical assistance the SBIC doesn't.

"SBA Reauthorization: Programming for Success", Washington, D.C., June 4, 2003

On June 4, 2003, the Committee held a hearing on the reauthorization of the Small Business Administration (SBA) and the programs it supports. Chair Senator Olympia Snowe and SBA Administrator Hector Barreto discussed the successes and challenges facing the SBA. Chair Snowe also explained that the Reauthorization hearing was one is a series of hearings convinced by the Committee to examine SBA programs. She then reviewed those hearings.

In March 2003, the Committee held a hearing on contract bundling that outlined significant changes federal agencies need to make in order to meet the goal of 23 percent of federal contracting dollars going to small businesses.

Then, in April and May, the Committee conducted a series of roundtables to review different SBA programs designed to help individuals start small businesses including, the Small Business Development Centers (SBDC), Women Business Centers (WBC) and the Service Corps of Retired Executives (SCORE). The roundtable concluded that the SBA's Office of Advocacy is an invaluable voice representing small businesses with the Administration. But, there are some SBA program insufficiencies that need to be addressed to help small businesses start up operations and receive assistance once operating, including access to SBA personnel with experience in government contracting.

Roundtables on April 30th and May 1st focused on SBA's lending and capital investment programs. These programs help small businesses to grow and expand through loans and capital investing. These programs have created and retained over 2 million jobs. Chairman Snowe stated that the Senate Small Business Committee hopes to work with the SBA to make SBA programs more user-friendly and efficient. She also observed that she looked forward to hearing how SBA Administrator Hector Barreto would respond to the challenges facing existing small businesses as well as working with him during the reauthorization process.

Mr. Barreto testified about the many different initiatives and programs undertaken by the SBA to strengthen small businesses, stating that the SBA's three strategic goals are, minimizing the small business regulatory burden, empowering entrepreneurs by increasing access to capital and information, and helping businesses recover from disasters. Mr. Barreto then listed a series of SBA accomplishments including; improvements in the econometrics model for the 7(a) loan program, changes in the way the SBA delivers services to customers, and a contract with Dun & Bradstreet to develop a more modern oversight system for SBA's lending partners.

For FY 2004, the President proposed that $797.9 million be appropriated for the SBA, maintaining spending at 2003 spending levels. The budget allocated $4.5 billion in 504 Certified Development Company Programs loans. The budget requested level funding for SCORE, SBDC, WBC and business information networks and continued funding for Disaster Assistance Programs. This budget would provide $20.8 billion in small business capital, and $760 million in new disaster loans for natural disaster victims.

The budget proposal aimed to serve small businesses efficiently and assist job creation. Some examples given of serving small businesses more efficiently include changes in the 7(a) Loan Guarantee Program to reduce the program's fees and an emphasis on smaller loans achieved through capping 7(a) loans at $500,000 per loan. Because of these caps the SBA 7(a) program, in FY 2003, had lower default rates, and assisted more small businesses while also creating more jobs. The 7(a) program was also to expand to include credit unions as lenders.

The SBA legislative proposal for reauthorization asked Congress to make the re-authorization a six year cycle and to make changes to existing programs permanent including the clarification of the SBA's authority over the 7(A) loan program, changes to the Microloan program regarding eligibility, changes to the 504 Premier Certified Lending Program's loan loss reserves, and statutory changes to the SBIC participating securities program that increases fees in order to maintain the program's zero subsidy and allow SBICs to invest idle funds in securities.

The budget also sought to update and increase the capacity of SBDC and WBCs. The SBA proposes using competition in the SBDC program, like the competition measures already used WBCs, so that the strongest most successful centers remain, while weaker centers are closed. The SBA also wanted to use the budget proposal to expand the number of WBC centers available to serve business women.

Mr Barreto explained how SBA programs creates jobs, and the success of different lending programs like SBAExpress in creating jobs on smaller loan amounts. He concurred with Chair Snowe that the resources available through the SBA are not sufficiently well known or understood within the small business community. He stated that the SBA intends to use the SBA's 50th anniversary as a reason to increase its marketing and outreach to small businesses.

The budget includes $8.8 million for SBA transformation with transformation focusing on helping the SBA field offices give more attention to their relationships with customers and resource partners. This transformation plan is linked to the President's management agenda with five areas of focus: human capital, competitive sourcing, E-government, integration of budget with performance, and improved financial management. As part of the transformation request the SBA asked for $2.3 million dollars to streamline its internal business procedures and improve the technology infrastructure.

The purpose of the SBA transformation initiative is to free SBA employees from the increasing bureaucracy and administrative duties. The SBA's goal is to work more with the small business community helping business owners access more capital and technical assistance. The SBA transformation would train existing employees, who previously spent time doing paperwork, to network with small businesses, their local Chambers of Commerce and industry organizations.

Separate from the budget issues, Chair Snowe and Administrator Barreto discussed concerns about the SBA's accounting. Specifically, the SBA disaster loan programs had three consecutive years, 2000, 2001, 2002 of unfavorable opinions on financial statements and loan asset sales. To fix the problem the SBA changed the CFO in charge of these financial reports and is working with the GAO to improve the credibility of these financial statements. Administrator Barreto also testified that the SBA is working to implement a permanent correction that fixes problems in the existing internal systems. The Agency hopes to accomplish this through an effective loan monitoring system designed by Dunn and Bradstreet.

Chair Snowe was concerned that the $9.3 billion dollars worth of funding for the 7(A) loan program would not be enough to service the demand for small businesses loans. Administrator Barreto explained that though in 2003, the 7(a) program ran short of loan money, in 2004, the SBA's focus on smaller loans would prevent a similar year end funding shortfall. He explained that by making smaller loans to more businesses, through the SBA Express Program, the SBA has reached 10,000 more small businesses year to date.

Ordinally, many predicted that banks would not participate in the SBA Express Program offering these reduced 7(a) small business loans. But, small lenders like credit unions, community lenders and rural lenders were able to use SBA Express to make the program a success. These lenders are considered an important part of the SBA's outreach and marketing plan to drive up small businesses demand for SBA lending.

Administrator Barreto discussed the SBA actions on contract bundling. When the ProNet and CCR contracting databases were merged, some companies, that were no longer small businesses, were still listed on the ProNet database. These glitches and other problems created the perception that large companies were taking contracting opportunities away from small businesses. The SBA scrubbed the database trying to eliminate large businesses, but found that sometimes business qualify as a large business in one contracting category and a small business in another. The SBA is policing the database, pursuing criminal charges for abusers, as well as fines and other penalties. Small businesses are also encouraged to help monitor the database to assure that only small business compete for small business government contracts.

Finally, in closing, Chair Snowe noted her preference for a three-year reauthorization time line for SBA programs over Administrator Barretos proposed, six-year reauthorization. She thanked Administrator Barreto for his testimony and stated she looked forward to working with him on the reauthorization process.

"Small Business Manufacturing in a Global Market", Lewiston, Maine, October 9, 2003

Chair Olympia Snowe, after welcoming the attendees, emphasized how important reviving the manufacturing industry was to her as a Senator from Maine, and the Chair of the Senate Small Business Committee and Co-Chair of the Senate Task Force on Manufacturing. Her opening remarks addressed many of the difficulties Maine's small manufacturers face. She stated that a healthy manufacturing sector is essential to our national security. But, that unfair trade practices, including China's manipulation of its currency, threatened the U.S. manufacturing base and manufacturing jobs. She also explained how two pending Senate measures, the reauthorization of the Small Business Administration (SBA) and efforts to reform the FSC/ETI export tax, would help small manufacturers.

The Honorable Michael H. Michaud made a brief statement. He explained how the closure of large- and medium-sized businesses can have devastating economic consequences on Maine as small manufacturers lose jobs and capacity. He emphasized the need for an Assistant Secretary of Commerce for Manufacturing, and bipartisan work, to create policies that address the forces hurting the manufacturing industry.

Grant Aldonas, the Commerce Department's Under Secretary for International Trade discussed the President's efforts to create a strong economic environment for small- and medium-sized manufacturers. He explained that the U.S. needs to "keep our side of the street clean," by addressing rising health care and pension costs and the pervasiveness of personal injury suits that reduce small business profitability and viability. He also addressed concerns he heard during meetings with small manufacturers on how regulatory and tax burdens reduce the competitiveness of domestic small businesses.

Under Secretary Aldonas talked about international trade and the lack of economic growth abroad. He also addressed manufacturers' concerns about export trade with China, explaining how the Administration is pressuring China to correct structural issues that create unfair trade practices, such as pegging the yuan to the dollar.

He said that the Administration is taking the most vigorous stance he has seen in dealing with trade issues. He wants to address trade problems before an industry is harmed. He believes the U.S. should act aggressively to protect domestic manufacturers. He expressed that trading partners should decide if they want to comply with U.S. trade rules and play fair, or not trade with the United States.

In her testimony, Pamela Olsen, Assistant Secretary on Tax Policy for the Treasury Department discussed current tax issues affecting small business manufacturers in a global market. She explained that small businesses' role in global manufacturing has steadily increased since the 1960s and that many small businesses are directly or indirectly engaged in exporting their goods abroad. She asserts U.S. tax policy must raise revenues in a way that creates as little burden on tax payers as possible. She stated that among the Administration's tax goals are plans to ease small businesses' tax burden and streamline the tax process.

Assistant Secretary Olsen outlined how the Administration's legislative tax agenda would benefit small businesses and manufacturers. These initiatives include making the research and development tax cuts permanent, reviewing the current system of tax deprecation to assure that small businesses invest in their most productive endeavors, reforming the corporate Alternative Minimum Tax (AMT), simplifying corporate accounting rules, and simplifying tax regulations.

During the question and answer period many issues related to manufacturing, China, taxation and competitiveness were discussed. Chair Snowe asked Grant Aldonas about China, and how long China would be allowed to be noncompliant with WTO rules. She explained that one of the primary concerns she heard from manufacturers is that China is violating it's fair trade obligations. She urged the Administration to take a firm stance against unfair trade practices.

Mr. Aldonas explained that the United States needs to convince China that it is in their best interest to work with the U.S. under a model of openness and enforcement of trade agreements. He reiterated that he believes that the Administration is taking strong action against China.

Mr. Aldonas also addressed other domestic issues that affect U.S. competitiveness. He observed how many small manufacturers will reduce their costs and increase their profitability only to see those savings eroded by increasing health care and energy costs. He talked of Commerce Department Initiatives that aimed at helping small businesses find niche markets to compete. He explained how declines in the U.S. shipping industry hurt U.S. manufacturers and Maine's economy.

Assistant Secretary Olsen discussed the impact of U.S. taxes on the competitiveness of U.S. industries. She used the example of the U.S. shipping industry's decline after the 1960's imposition of taxes on world wide earnings to show how tax policy can negatively impact. She observed that, because other major world economies are stagnant, the world currently relies on the U.S. economy for both growth and consumption.

During his testimony, Bruce Pulkkinen, President and CEO of Windham Millwork Inc., outlined the difficulties facing small manufacturers. He stated that small manufactures have fifty percent of their profits eaten up by state, local and federal taxes. This reduces the money companies have to invest in growth. Additionally, manufacturers must continuously become more competitive to compete with countries that use unethical trading practices. He believes that if the trade deficit between the U.S. and China continues to increase, U.S. small manufacturers will be eliminated within five years.

Mr. Pulkkinen stressed the importance that the Manufacturing Extension Partnership's (MEP) program to be fully funded, so that it can continue to help small manufacturers. He explained that manufacturers take inexpensive natural resources and by adding value, create wealth. If the U.S. imports more goods than it exports it builds other countries wealth, not domestic wealth. He believes that tax changes, advancements in technology and leaders who understand the issues facing manufacturers are necessary to reinvigorate the manufacturing sector.

Mr. Thom Labrie, President of former Augurn Machinery, Inc., stressed the importance of protecting U.S. manufacturers' intellectual property rights. Mr. Labrie testified that while at trade shows, foreign competitors would view his company's products in an effort to illegally copy their technology for their own use.

In her testimony, Lolisa Bonney, the CFO and general manager for Winderosa Gaskets, discussed how her company competes in the world market and the difficulties they face. She explained that companies like hers demonstrate the potential, positive impact international trade can have on remote communities. She explained the importance of the MEP in helping her business be competitive internationally and the need for schools to educate students on how to work in the manufacturing industry.

In his testimony, Rodney Rodrigue, the President and CEO of the Maine MEP, testified about the importance of technology transfer from the government and universities to small businesses. He explained that government should strive to eliminate barriers to technology transfer and help small manufacturers compete by focusing its resources into a single program that is designed to support and reinvigorate manufacturing.

In his testimony, Randy Cousineau, owner and president of Cousineau Inc., explained the difficulties faced by Maine's lumber and paper mills. He explained that his company incurs many costs that his foreign competitors do not have to pay, including workers compensation insurance, higher per unit cost of electricity and the unsubsidized costs of machinery upgrades. He explained that low cost lumber from Russia and Asia decreases his company's orders.

In his testimony, Allen Cairns, managing partner for Creative Mold Company explained the difficulties U.S. manufacturers face as they compete with lower cost labor abroad. U.S. manufacturers have used automation, computers and other means to make their manufacturing process more efficient. These processes have been exported overseas, reducing the technological competitive advantage of U.S. companies and reducing competitiveness to costs of labor. He argues that when companies compete on labor cost alone, U.S. companies loose.

In his testimony, John Wentworth, the president of Moosehead Manufacturing, addressed different issues affecting domestic wood furniture manufacturers. He explained that the cost of regulations, like those created by OSHA, the EPA and the Consumer Product Safety Commission, force small companies to spend their limited resources on regulatory compliance, reducing their profitability and survivability. He talked about the negative affects of increasing healthcare costs and China's dumping of wood furniture in the U.S. market on his business.

In his testimony, Bernard Featherman, Chairman of the Biddeford-Saco Chamber of Commerce, testified about the difficulties facing Maine small businesses. He explained that small business owners need more federal grants to train workers for manufacturing jobs. Like many panelists, he was concerned about the high cost of healthcare. He suggested that the government should address questions of liability reform, tax code revisions and a national energy policy. He also sought government attention to small business financing and capital assistance.

B. HEARINGS OF THE COMMITTEE, SECOND SESSION

"The President's FY2005 Budget Request for the SBA", Washington, D.C., February 12, 2004

On February 12, 2004, the Senate Small Business Committee held a hearing to review and make recommendations to the Small Business Administration's (SBA) budget proposal for fiscal year 2005. In her opening statement, Chair Olympia J. Snowe examined the critical role the SBA's lending and technical assistance programs have played in aiding America's small businesses during a time of economic recovery. With two-thirds of all new jobs created by small businesses, the SBA continues to prove its investment in America's economic future, having created or retained more than 6 million jobs since 1999.

The agency's budget proposal represented a 15 percent decrease from the Administration's budget proposal submitted in fiscal year 2004. In order to assure that vital job creating programs were not sacrificed, Chair Snowe stressed the success of programs such as the 7(a) loan guarantee program, the Small Business Investment Company Program, and SBA's Technical Assistance Programs.

The Honorable Mike Crapo, U.S. Senator from Idaho provided in his opening statement that while he supports balancing the budget, he does not believe the SBA is a good place to start making cuts, especially with small business being the center of job creation in this country.

The Honorable Mark Pryor, U.S. Senator from Arkansas, in his opening statement expressed his concern for that the SBA budget did not include funding for the 7(a) guaranty program, the Microloan program and cut funding for both the Women's Business Center program and Small Business Development Centers. He acknowledged the important role the SBA plays with small businesses, and in turn the role that small businesses play in our economy and job creation.

The first witness to testify before the Committee was the Honorable Hector V. Barreto, Administrator, U.S. Small Business Administration. He briefed the Committee on the SBA's Fiscal Year 2005

Legislative Proposal and Budget Request, which included increasing the 7(a) loan guarantee authority to $12.5 billion. More importantly, Barreto spoke about the SBA's goal to move the 7(a) program to a zero subsidy level, thereby decreasing the SBA budget by $100 million, and minimizing the time it takes for businesses to complete the application process. Additionally, Barreto spoke about the budget requests for other SBA programs including: $88 million for Small Business Development Centers, $5 million for the Service Corps of Retired Executives, $12 million for Women's Business Centers, $750,000 for Veterans Outreach, and $1.5 million for 7(j) Technical Assistance.

During the question period, Mr. Barreto explained to Chair Snowe that the shutdown of the 7(a) program in January was due to the volume of large-scale loans at the end of 2003, which used up the remaining budget money while the agency was under a Continuing Resolution. Chair Snowe expressed concern regarding the low amount requested for 7(a) loan guarantee authority. By not requesting the $16 billion provided in legislation, the agency was taking a chance of exhausting its funding and capping business growth. In response, Mr. Barreto made the case that the program consistently provided approximately $9 billion in loans and the requested $12.5 billion loan cap was actually an increase.

Senator Pryor questioned Mr. Barreto regarding the SBA's transformation initiative and its effect on the SBA's loan program. Mr. Barreto explained that the relocated employees were liquidators and not employees giving loans. Furthermore, the transformation process will reduce the time it takes for businesses to complete this process.

Other issues discussed included fees on 7(a) loans, the Microloan program, and the HUBZone program. Mr. Barreto concluded his testimony by addressing the SBA's plans to reach zero-subsidy for the 7(a) program and that the change would make it even more possible for small businesses to secure loans.

The first member of the second panel to testify was Mr. Tony Wilkinson, President and CEO of the National Association of Government Guaranteed Lenders. Mr. Wilkinson cited the recent House Small Business Committee hearing in which business owners testified that the 7(a) program shutdown did not allow them to receive loans that were approved. Furthermore, these applicants were unable to resubmit for their loan because the amount exceeded the loan cap of $750,000. His testimony discussed that capping loans, prevented small business from participating in the loan program which could negatively impact the number of jobs they can create. Mr. Wilkinson also indicated that the shutdown could have been avoided, if the SBA increased its lending authority to $12.5 billion which was the predicted lending volume for Fiscal Year 2004.

Next to testify was Mr. David Coit, Chairman, National Association of Small Business Investment Companies. Mr. Coit called on the committee to consider NASBIC's proposal to continue the Participating Securities Program. The proposal seeks to remove elements that discourage institutional investors and will subsequently bring additional sources of capital to the program.

Ms. Mary Mathews, former board chair of the Association for Enterprise Opportunity, provided testimony supporting the SBA

Microloan program and PRIME. She argued that loans covered under the Microloan program would not be picked up by the 7(a) program as Mr. Barreto suggested, and that theses types of loans were too risky for banks to approve under the 7(a) program.

The final member of the panel to testify was Ms. Ellen Golden, Association of Women's Business Centers. Ms Golden stated that the President's budget request of $12 million for the Women's Business Center program was insufficient. Under the budget request, the centers were being expected to provide additional services, including training SBA personnel to assist Native American communities and provide Microloan technical assistance, with no additional funding. Ms. Golden indicated that $14.5 million for Fiscal Year 2005 would be an appropriate funding level. Additionally, Ms. Golden expressed concern that the Women's Business Center Sustainability Pilot program is expected to expire without reauthorization, and two-thirds of the most experienced centers would not have the ability to renew their grants.

"Accessing Capital and Business Assistance: Are Current Programs Meeting the Needs of Rural Small Business?", Coeur d'Alene, Idaho, February 16, 2004

On Thursday, February 19, 2004, Senator Mike Crapo presided over a field hearing, in Coeur d'Alene, Idaho entitled "Accessing Capital and Business Assistance: Are Current Programs Meeting the Needs of Rural Small Business?" for the Committee on Small Business and Entrepreneurship. Senator Crapo stated that the findings of a recent SBA study were disturbing and worrisome for small businesses. The study showed that 80 percent of all small business lending occurs in urban areas, although loans to rural businesses are increasing at a faster rate than loans to urban businesses. Unfortunately, the study also shows that a significant problem remains. Small businesses in rural areas nationwide (20 percent of all small businesses) have less access to credit than those operating in urban areas. Senator Crapo hoped that by raising some important questions this meeting would result in helpful responses and actions.

The SBA's recent decision to suspend, cap and restrict its flagship 7(a) loan program has caused a lot of problems and raised a lot of questions. SBA programs may be putting small business lending in rural America, and elsewhere, in jeopardy of obtaining access to capital necessary for the beginning and expanding of their business. There are four main areas of concern: funding, restructuring of existing rules and procedures, centralization of loan processing, and the possible elimination of SBA-supported consulting services.

The funding of the SBA loan programs seems to be an issue almost every year, especially for Robert Beck, the Vice President of Mountain West Bank. He believes the funding crisis could be avoided if the SBA would form a dialogue with their lending partners and other experts in the field such as NAGGL. The current budget of $9.5 billion will probably not be sufficient and will, in all likelihood, be $3 billion short for the fiscal year 2004.

Caps of $500,000 and $750,000 have been put in place in recent years and, in addition, the recent elimination of the piggyback loans is causing problems. Constituents suggested that the piggyback loan structure be put back in place immediately and the maximum of the $2 million loan be reinstated as quickly as possible.

The SBA is beginning to get a reputation of on again and off again. Consistency and integrity is a must. Lending partners must be willing to explain to small business owners clearly and precisely the rules and regulations. It is important to immediately reestablish what the SBA loan guarantee program is about providing capital to small businesses that would otherwise not be able to get funding and business assistance without an SBA loan guarantee.

The SBA recently proposed to fully fund the program but only by providing much less of a guarantee and charging less than guarantee fees. This will have a dramatic effect of reducing capita to small businesses. Lending partners will be unwilling to lend the less of a guarantee due to lack of collateral especially with start-up businesses or expanding businesses that have less than adequate liquidation values to support the loan.

Many who work with the SBA believe that the agency is planning to centralize all loan processing; eliminating 138 loan officers in favor of 36 centralized loan decision makers. Even though local banks participate in the Preferred Lending program, many constantly rely on the district office to provide guidance and answer questions. It is important to preserve our SBA loan office so they can continue to provide service to small businesses as well as lending partners.

Many bank policies preclude lending to small businesses without that 2-year historic debt service. Without the aide of the U.S. Small Business Administration loan programs, many of these small businesses would not be able to obtain their financing that they would need to create these jobs that are so needed in our economy. The Small Business Administration lending programs are indispensable for this country's economic health. It is common knowledge that the majority of all jobs are created from the small businesses.

In most years, the SBA loan program has been able to meet the needs of both the lenders and the businesses. The recent shutdown of the SBA's 7(a) loan program, many banks, many businesses, estimated at about 200 have been caught in the middle with no place to go. This shutdown and this subsequent capping of the loans at $750,000, along with the first-time ever prohibiting the piggyback loans, has caused the SBA to slam the door on at least $1.3 million loan requests as of December 30, 2003. Many of these small business owners do not qualify for other loan programs. But when they contact the SBA office they are told to find a 504 lender.

The 7(a) program is a huge asset for North Idaho and it's especially good for the small community banks that cannot afford the risk and also need the ability to sell loans to provide capital for their other borrowers. The 7(a) program also allows restructure and consolidation. These requests are not allowed in any of our other PAC programs.

The SBA is changing the character of the Certified Development Companies, the CDCs, that originate and service the SBA 504 loans. The CDCs were established originally with a given geographical area, a local board, a local loan committee to address local needs. Recent changes are allowing CDCs to cover the entire state and also allow large CDCs to cross state lines. These changes do not require local boards, or at least local committees. This change will enable the large CDCs to "cream" the loans and only go to the areas where they're going to see larger volume and tend to loan to more risk-free businesses. It's very hard for rural CDCs to meet production goals with their limited resources. Many more CDCs will disappear in the rural areas. These smaller CDCs also rely on the servicing income from the large 504s to fund the staff that also administers the smaller micro and USBA loans. Competition for the USDA Rural Development Loan pool money is also difficult for smaller economic development groups. Performance points used to be adequate to obtain the money.

The administration says the microloan can be replaced by use of the SBA Community Express. However, the Community Express program does not pay for technical assistance, even though the SBA web site recognizes that this assistance is crucial to the success of a new business. Borrowers must receive pre- and post-closing technical assistance from non-profit providers or the lender. This assistance is to be paid for by that Community Express lender. But, how will non-profits carry this cost burden and are banks willing to do so for a modest sized loan.

The biggest challenge facing the Small Business Development Center is to try and meet the increasing demands for our services, according to John Lynn, the Director. Grant funding from the SBA has been flat since 1997. But they request more services every year and the number of people we see and the number of training hours that we deliver. Our rural outreach, being an important part of the SBDC mission, is becoming increasingly difficult to provide SBDC services to rural North Idaho that has an economic development impact.

Our challenge is to try to leverage our resources with other economic development organizations to provide business development services outside of Kootenai County. Infrastructure needs to be developed, access to capital needs to be improved, and a concentrated and coordinated effort must be developed between the economic development service providers.

Our office works very closely with the various banks and loan funds and economic development agencies in the Idaho Panhandle; and without the SBA loan programs, the 7(a) program in particular and the microloan program, access to capital for start-up for existing small businesses would be nonexistent. Well over 90 percent of our clients that receive loans have an SBA guarantee associated with it in some way or another.

The SBDC program in Idaho is being required to meet ever-increasing milestones from the SBA without any increase in resources. Rural businesses face challenges that simply aren't imposed on urban or suburban businesses. However, when a rural business seeks capital for operating challenges or expansion, they're credit-scored against a standard established primarily by urban businesses. The financing standards therefore compound the challenges faced by rural businesses.

Additionally, in a recent move by the SBA to eliminate the community aspect of 504 lending, this may cause a reduction of this program's availability to rural businesses. The new ruling simply has removed the requirement of local credit involvement; and in fact, encourages large, multi-state certified development companies, without any local interest, to dominate the 504 markets. The multi-state development companies will have to concentrate on urbanized areas for efficiency and for the great availability of deals. The result may be that the rural areas will be ignored or can't compete against the credit scoring or urban deals.

The SBA has the responsibility to operate their programs as efficiently as possible; and with the idea of only having to deal with a few large multi-state certified development companies, that's an appealing prospect. However, the potential loss of service to rural communities can have a significant impact on the availability of rural businesses, availability of capital for rural businesses.

The Small Business Intermediary Loan Pilot program addresses a capital gap that we see in our lending by filling a niche not currently served by the SBA microloan, 7(a) guarantee, Express, or 504 programs in terms of underwriting criteria. The pilot would enable community-based lenders like Panhandle Area Council to provide loans between $35,000 and $200,000 that would be more flexible in terms of collateral and general underwriting requirements.

Senator Crapo raised the point that over the last 4 years, the SBA budget has gone down about 24 percent. However, of all of the Federal agencies, there are only four other Federal agencies in the entire Federal Government over that same 4-year period of time that have had their overall budgets reduced. The others have all continued to grow, although maybe at a lower rate than they would like to have grown. Of those five agencies, including the SBA, that have actually gone down in size, none of the other four have approached the 24-percent reduction that the SBA has seen. That is a concern given the fact that small business is the engine driving jobs in this country,

There are problems and it is important to identify what is needed in rural communities nationwide and those areas where the Federal Government can properly play a role. Infrastructure is the important first step, to make certain everything is in place. It is also important to work on the development of adequate access to capital and the communication between those capital providers. Hopefully when those areas are improved, small businesses in the rural communities will flourish.

"Small Business Assistance in Arkansas: Access to Capital and Service Delivery", Little Rock, Arkansas, February 19, 2004

On February 19, 2004, the Senate Small Business Committee held a field hearing in Little Rock, Arkansas, Senator Mark Pryor presided. In his opening statements Senator Pryor thanked those who set up the hearing, Chair Snowe, and the people who came to testify. He commented that in 2003 economic and job growth were sluggish and that he disagreed with the direction the Administration's FY 2005 budget would take the Small Business Administration (SBA). He was concerned with the SBA's consolidation of loan liquidation staff to Herndon, Virginia, and the elimination of SBA employees in Arkansas regional offices and in other states. He expressed his concern about the zero appropriations level for the 7(a) loan program and the elimination of the micro-loan program. He stated his belief that eliminating SBA programs that stimulate the economy, would hurt job creation and economic growth.

Mr. Joe David Watts, a former liquidation officer for the SBA in Conway, Arkansas testified about the SBA buyout. In December

2003, he received notification of his selection for reassignment to Herndon, Virginia. Initially, he accepted the reassignment, but in January 2004, he withdrew his acceptance and decided to resign from the SBA. He was concerned that the reorganization left the Arkansas district without a district Director.

Mr. Keith Grimes, a commercial loan officer for Pine Bluff National Bank of Arkansas testified about the effects of the SBA consolidation of liquidation loans on his bank, and small business lending in general. He stated that the SBA did not inform his bank about the loan reorganization, and that the lack of coordination delayed many loan liquidations. Mr. Grimes said delays would force some banks to write fewer SBA guaranteed loans. He urged the SBA to staff the new National Liquidation Guaranty Purchase Program as quickly as possible.

Janet Roderick, the State Director of the Arkansas Small Business Development Center (SBDC), testified about the SBDC's positive effect on Arkansas' economy. She stated that over the last five years the SBDC created over 4,000 new jobs and helped small businesses obtain over $200 million in funds. She discussed the many ways the Arkansas SBDC worked to increase results with decreasing resources. These innovations included consolidating their service area from twelve offices to seven, and the early adoption of a website offering small business owners online resources, including the ability to download information on how to start a small business.

Eduardo Gomez, owner of Adina Cafe and Coffee Roastery LLC., explained how he started his small businesses, and the difficulties he experienced getting SBA loans. He explained that many small entrepreneurs lack the business experience needed to qualify for SBA loans. He said the willingness of the owner to invest "sweat equity" along with their desire and business acumen are what make small businesses successful. He stated that small business start up loans are the key to entrepreneurship, and that certain parts of the U.S. business community provides peer-managed loans that focus on small business owners with motivation and drive when making lending decisions. He suggested this was a model that the SBA consider for lending.

During the question and answer period panelists answered a range of questions. They explained that, because of the amount of paperwork required by the lender and the seller, for nonperforming SBA loans, the average liquidation time is around 150 days. Panelists reiterated how necessary and important they thought local SBA employees are to small business success. They emphasized how important it is to have hands on, one on one time with business owners. They also stated that they have had difficulty dealing with the SBA's new Herndon Liquidation office. Panelists were unsure if the SBA would dedicate specific representatives to working with liquidating loans in Arkansas. They do not believe a one size fits all strategy is helpful to small businesses. They also stated that government loans can help revitalize rural areas and are a good return on the government's investment.

Daniel Blair, the General Manager of Daniel Utility Construction of Little Rock, Arkansas, testified about his difficulty getting a 7(a) loan to help with company cash flow issues. He explained that his company laid off workers in 2003. When the economy picked up in

2004 he applied for a 7(a) loan to help his expand. Originally, he applied for a loan of about 1 million dollars. He expects to grow 50 employees over the next year, but will have difficulty with cash flow because his loan fell through. He believes there are many other small businesses like his that are ready to take off but lack the funds to do so.

C. Sam Walls, Chief Operating Officer of Arkansas Capital Corporation, testified about the banking and business community's need to understand the SBA's direction and intentions. He explained that lenders need to be able to rely and plan on the SBA acting in a predictable way. He explained that in Arkansas small and medium size businesses have the highest potential for economic growth. He expressed his concern that small businesses can not afford a lending holiday or further cuts to the 7(a) program.

Phillip Knight, the Executive Vice President for Small Business Lending at Arkansas National Bank, explained how current changes to the SBA may discourage local community banks from lending to small businesses. He mentioned a number of recent SBA actions that hurt small businesses and cause them to question the SBA's credibility and stability. Among the actions he mentioned were: the instability of the 7(a) loan program, in which caps and the suspension of lending had detrimental effects on small business borrowers, the consolidation of loan liquidations to Herndon, Virginia SBA employees' reluctance to answer questions on liquidated portfolios, and the future reduction in the percentage guarantee for community lenders making SBA loans.

Kevin Hester, Executive Vice President of the First State Bank of Conway and a member of the National Association of Government Guarantee Lenders, spoke about the need for the Administration and Congress to support the SBA's 7(a) lending program. He observed that if the administration wanted to support the 7(a) loan program, and capital lending to small businesses, it would request up to the 7(a) authorized limit of $16 billion dollars for the program.

Samuel W. Hinton, the Small Business Executive of Metropolitan National Bank in Little Rock, Arkansas, testified about the human factor's importance when dealing with the SBA. He said he understands why the SBA wants to pursue economies of scale and processing efficiencies, he doesn't feel that reducing human interaction with the SBA helps small business owners. He wants the SBA to understand that unexpected changes in the 7(a) loan program hurt small business owners. He doesn't believe the cutting of the Microloan program will be as detrimental as losing the 7(a) program.

Odies Wilson III, the Intergovernmental Relations Manager for the city of Little Rock, testified about the importance of SBA programs to small minority businesses. He explained how he works with different programs of the SBDC to enhance business development practices for minority and other business owners. He spoke about the importance of micro-lending programs in developing small businesses with receipts under $10,000 per year and the need for personal support and help for individual entrepreneurs.

Samuel L. Harris III, the Executive Vice President of Arkansas National Bank of Springdale, explained why he feels it is very important for the SBA to keep a district office in Little Rock, Arkansas. He explained that having high quality SBA people in Little

Rock allows the Agency to make solid lending and servicing decisions and leads to fewer loans losses. He believes that decisions made locally, by locally based professionals, help the SBA and the government earn a greater return on the money invested in the programs.

Tyronne Davis, owner of Davis Oil and Petroleum, testified about how the SBA helped him start his small business. He also participated in SCORE and used a program called the Small Business Academy in which local graduate students helped him develop a strategic business plan. He asked Senator Pryor to do all that was possible to save the local SBA district office.

Charles King, Executive Director of the Arkansas Regional Minorities Supply and Development Council, explained how this private organization develops business opportunities between minority businesses, corporations, and government agencies. The organization helps produce qualified certified minority businesses. He believes that minority businesses need assistance learning how to access available resources as much as they need access to capital. He requested that the SBA, and SBA programs, not be eliminated by the administration so that the work of these important programs can continue.

During the question and answer period the panelist commented on the partnership relationship that lenders have with the SBA. They were concerned that a new zero subsidy rate loan program even with new higher fees, would be unable to fund itself. They also commented on the viability and importance of the micro loan programs for developing entrepreneurs and the fact that the microloan program in Arkansas has a zero default rate. They talked about the need and the importance of the 7(a) loan program and how it promotes economic growth and provides loans to businesses that would have a difficult time getting loans if not for the SBA loan guarantee.

In the second part of her testimony, Ms. Roderick explained how the 7(a) freeze affected small businesses. She explained that when the freeze happened they quickly surveyed their businesses and found that twenty-five businesses, with a little over $8 million dollars in pending loans, had applications frozen. When the freeze was lifted, clients who previously qualified for loans above the $750,000 no longer qualified for their loans, forcing these businesses to put expansion and development plans on hold. Additionally, she explained how the SBA lowering of the guarantee rate on 7(a) loans to fifty percent would negatively impact small business lending in rural Arkansas. She explained that local rural banks would not be able to finance start up businesses with only the fifty percent guarantee rate. She worried that the effect of this lower guarantee level for small business financing would force businesses to use their credit cards to pay for start up costs or accept loan terms that may jeopardize their company's future.

"The Role Small Business Should Play in Maintaining Forest Health", Cody, Wyoming, February 19, 2004

On Thursday, February 19, 2004 the Committee held a field hearing, in Cody, Wyoming entitled "The Role Small Business Should Play in Maintaining Forest Health," Senator Mike Enzi presiding. The hearing examined the influence that federal land management agency decisions have on the success of Wyoming's small business community—particularly as those decisions apply to the management of the State's federal forest lands. It established that we need more partnerships between federal agencies and local small businesses to restore our forests to a point where all of the many uses of our forest lands can exist free of the significant threat of destruction by catastrophic wildfire.

The hearing put to rest the notion that using our forest products industry to restore our forests to a state of health creates a conflict with any other use. The reality is that our forest products industry is not in conflict, but is in fact one of our best tools to maintain and preserve the entire forest ecosystem.

There are more than 100 million acres of Federal forestlands that now exist under an unnaturally high risk of catastrophic wildfires and large scale insect and disease outbreaks because of unhealthy forest conditions.

Catastrophic wildfires not only cause damage to the forests and other lands, but place the lives of firefighters at risk, pose threats to human health, personal property, sustainable ecosystems, and air and water quality. Both our forests and our communities are ripe for destruction, our forests by fire, and our communities by economic decline.

This problem wasn't always as bad as it is now. There was a time when Mother Nature and Native Americans took care of thinning our forests by regularly starting wildfires. Because the fuel loads weren't allowed to grow as dense as they are today, the fuel ladder didn't reach all the way up to the big trees. Fires would burn up the tinder and thin out the intermediate and dead and dying trees. This promoted biodiversity, kept the intensity of the forests down and, in times of drought the competition for limited water resources was dramatically less than it is today. We now have forests that historically had 40 or 50 tree stems per acres that are now over 200 stems per acre. This is a 300 percent increase.

When a fire starts in forests this dense it quickly climbs the fuel ladders and races out of control. These crown fires are all but impossible to stop. The heat generated from all rungs burning at once sterilizes the soil and leaves nothing but desolation in its wake. This is only made worse with the added factor of drought. By adding to the mix stands of dead trees that are as dry and volatile as the tinder on the forest floor you can just imagine the threat this kind of fire could have on the forests and their surrounding communities.

It is a much better conservation practice, therefore, to step in and duplicate the effect historic, healthy fires had on our forests by using what is called mechanical thinning. This is a practice where our land management agencies can hire experienced timber companies to remove the dense underbrush and carry out the smaller and intermediate trees thereby leaving a forest that is healthier, more bio-diverse, more fire resilient and with a better mix of older and younger trees.

If we are going to save our forests we must increase our number of timber sales. There is no reason, however, that these sales cannot be structured to improve forest health by including in the terms of the contracts a requirement to thin out the underbrush and leave our forests in a healthier, more sustainable condition.

The hearing demonstrated that in Wyoming, US Forest Service timber sales should be restructured to improve the forest thinning process. Wyoming's small businesses have the flexibility and the capacity to create innovative solutions to any problems that may arise on Wyoming's challenging landscape. But their innovation could just as easily be forced to leave the state to find other regions to develop. There is a larger role that can and should be played by our small businesses as we strive to create healthier forests.

"Impact of Stock Option Expensing on Small Businesses", Washington, D.C., April 28, 2004

On April 28th, 2004, the Committee met to discuss the Financial Accounting Standards Board's (FASB) rule 123 (FAS 123). Senator Enzi opened the meeting by acknowledging FASB's importance. He worried, however that small businesses would find it difficult to implement FASB's stock option expensing rule and that the rule would negatively affect small businesses. He further commented that it was likely that small business concerns would not be addressed during FASB's proposed bi-annual advisory committee meetings. The Senator expressed his displeasure with the amount of lobbying in favor of stock option expensing done on behalf of FASB. Senator Enzi noted that FASB failed to explain how stock option expensing would affect the stocks of 1.4 million small businesses. Finally, Senator Enzi acknowledged the need to limit executive compensation. He argued, however, that because executives would find a way around FASB restrictions, the ruling would hurt small businesses without solving the original problem it intended to fix.

In his opening statement, Senator Levin argued that stock options can be valued and that they are often valued in order to take tax deductions. He expressed his concern that, because companies do not have to list stock options as an expense, Enron was allowed to report large profits without paying taxes on these profits. He went on to point out that only 3% of small businesses use stock options, and only publicly traded companies must follow Generally Accepted Accounting Principles.

In his opening statement, Senator Allen explained that giving workers a direct interest in the success of their company by using stock options was "a great idea." He explained that FASB's rule could have adverse affects on the productivity of all companies regardless of their business size. Senator Allen challenged the idea that company stock options can be given a value. He explained that these options are not freely traded and there is no way to predict the stock's price at the unknown point in the future when the option may be exercised.

In his opening statement, Senator Bayh explained the tremendous impact that changes to the accounting rules for expensing stock options could have on the economy. He emphasized the importance of creating policies that balance the need for business transparency with the need for stock incentives that reward risk taking and produce business growth.

In his opening statement Senator Ensign made it clear that, because the available methods of stock option valuation are inaccurate, he did not agree with the expensing of stock options. He argued that FASB sets companies up for future litigation by making public companies choose between these flawed expensing options.

On panel one, Robert Herz, Chairman of the FASB, spoke first. Mr. Herz made the position of FASB clear by saying that the exception for fixed-plan employee stock options to not be expensed results in reporting that ignores the economic substance of those transactions and distorts reported earnings, profitability, and other key financial performance metrics. This also makes companies, both domestically and internationally, financially incomparable when they choose to compensate their employees in different ways.

Another FASB board member, George Batavick, spoke on the special provisions of FASB's proposal for small businesses, of which there were three. First, most small businesses will be able to measure compensation costs with a simpler, less costly intrinsic value method, rather than the fair-value-based method. Second, most small businesses would have a less costly prospective transition to the new requirements and lastly, the effective date for the proposed standards would be delayed a year for non-public enterprises.

The last speaker on panel one was Dr. Douglas Holtz-Eakin, Director, Congressional Budget Office. He highlighted the three main points of the CBO's recently released study on the economic implications of accounting for stock options. The first point was that expensing stock options brings accounting closer to the economic reality of total firm expenses and net income as the granting of stock options is a cost to the firm. The second point was that although valuing stock options is more difficult than valuing many other costs, this does not preclude the recognition of their fair value. The final point was that if FASB's proposal was enacted, the only channel for any real economic effect would be changes in investors' valuations of firms.

The first of seven panelists on panel two was Dr. Keith Carron, Founder & President, CC Technology, who sought to explain the role of stock options in the development of his company and why FASB's proposal would be detrimental to his business. Dr. Carron related that in a start-up business cash is short but much needed to run the business and to recruit qualified employees. One way to preserve cash is to replace cash incentives with stock options. But by expensing stock options, the company's profitability is reduced, thus making the grantee less likely to exercise their options and invalidating the notion that the company has incurred an expense.

Also, start-up companies rely on their profitability to attract working capital which they need to grow. Expensing stock options reduces their profitability and endangers their ability to raise capital. The failure rate for start-ups is already high; FAS 123, according to Dr. Carron, will increase that rate.

The second panelist was Mr. Stephen Diamond, Law Professor, Cornell University. His main argument was that there is a conflict of interest between option holders and shareholders. There is the assumption that options motivate their holders to run a company in such a way that is good for the company as a whole and this includes shareholders. However, this assumes that options are like stock. Options often represent, in comparison to stock, a shorter-term interest and options often get paid for by shareholders in the form of debt. So, there is an antagonism and mistrust between option holders and stock holders. In the interest of fostering a better relationship between investors and companies, expensing stock options is a good idea and could lead to increased investment.

Following Mr. Diamond was Mr. Jere Glover, of Brand & Frulla. Mr. Glover characterized FAS 123 as an unnecessary regulation on small businesses that would ultimately impact their ability to grow, innovate, and create jobs. His reasons were that many companies would simply stop using stock options and thus not be able to attract valuable employees. Second, the cost of compliance will be very high. Thirdly, many companies would show negative net worths and it will make it extremely difficult for them to qualify for loans, attract other capital, and bid for government contracts.

Mr. Glover argued that the controversy surrounding FAS 123 could have been avoided had FASB paid more attention to the particular concerns of small businesses.

Mr. Marc Jones, President & CEO, Visionael Corp., of Palo Alto, California, testified that FASB's stock option expensing proposals may eliminate small business owners' ability to use options as an incentive to attract employees. He explained that, because of the possible negative affects of stock option expensing on small business owners' access to capital etc, most small business owners are opposed to expensing of stock options on their financial reports.

In his testimony, Mr. John Kavazanjian, the President and CEO of Ultralife Batteries Inc., explained how stock option expensing will disproportionally hurt small businesses, while not solving the problems of excessive executive compensation. He argued that stock option expensing will make it more difficult for investors to analyze the financials of small companies' stock and discourage them from investing in small companies. He further argued that stock option expensing will make it difficult for small companies to attract new talent, to innovate and create new jobs.

Mr. Christopher Schnittker is the Senior Vice President and CFO of Cytogen Corporation, an oncology research company. In his testimony he explained that his company, and many other small companies, use stock options to motivate and retain highly qualified and in-demand employees. He feared that stock option expensing will deny small companies one of the only financial incentives they have that levels the playing field between large companies and small companies when attracting talented employees.

In contrast to the previous statements, Mr. Robert Mendoza, Chairman, Integrated Finance Ltd., spoke next in favor of FAS 123. He argued that options are undeniably an expense and thus should be accounted for more explicitly. He further stated that the rule would benefit small businesses and encourage start-ups by attracting more capital because investors would be better able to judge their potential investment return by having a more accurate valuation of each company.

Senator Enzi ended the hearing by issuing a warning that if FASB proceeds with the potentially harmful stock option expensing regulations, many small businesses may be lost before the rules can be changed to save them. Before thanking all the participants for their time and adjourning the hearing, Senator Enzi expressed his concern that FASB appeared to have already decided on its course of actions and was not paying attention to the way the proposed expensing rule would negatively affect small businesses.

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