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The Impact of 8(a) Small Business Graduation

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Abstract

The 8(a) small business set-aside program is designed to support small business participation in the federal market and to foster small business growth. However, 8(a) graduates do not fare well over time, with more than 60% no longer receiving federal prime contract obligations less than 10 years after graduation from set-aside eligibility. Those who were still federal prime contractors gained very little additional government business, with the average contract obligation up only 3.3% to $6.25 million, from $6.05 million (showing a decline when adjusting for inflation). Additionally, 8(a) graduates still depended on set-asides for more than half of their federal prime contract dollars. Overall, they are not rewarded for graduation.

Introduction

For decades, it has been the policy of the U.S. government to support and promote the growth of small businesses in the American economy. Part of that support comes from awarding government contracts to businesses that fall below certain size standards and are therefore eligible for special consideration. Constraining eligibility for contracts to certain businesses are sometimes called "set-aside" programs. One group of such set-aside programs is the 8(a) Business Development program under the U.S. Small Business Administration (SBA). Under 8(a), the federal government limits competition for certain contracts to businesses that participate in the 8(a) Business Development program.[1]

Qualified businesses that are certified to compete for 8(a) set-aside contracts do not retain that eligibility forever. Participating companies need to complete annual reviews to maintain good standing in the program, and a firm's certification will last for a maximum of nine years. At the end of that period, companies may still compete for and win government contracts, but they will no longer be eligible for 8(a) set-aside contract awards, though in certain circumstances they may later regain eligibility.

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[1] For more information about 8(a) requirements and eligibility, see https://www.sba.gov/federal-contracting/contracting-assistance-programs/8a-business-development-program.

Through the SBA, the federal government tracks and reports on 8(a) set-aside contracts. What happens, however, to companies whose certification eligibility has ended? How successful are they in pursuing government contracts? Do they even stay in business? It appears that the SBA cannot answer these questions, because once a firm graduates from 8(a) eligibility, it's not tracked and reported on.

The Professional Services Council, under its Foundation, undertook an examination of these questions (illustrated in Figure 1). This paper describes the research question, the methodology, and the initial research results. It draws some preliminary conclusions and outlines further research needed.

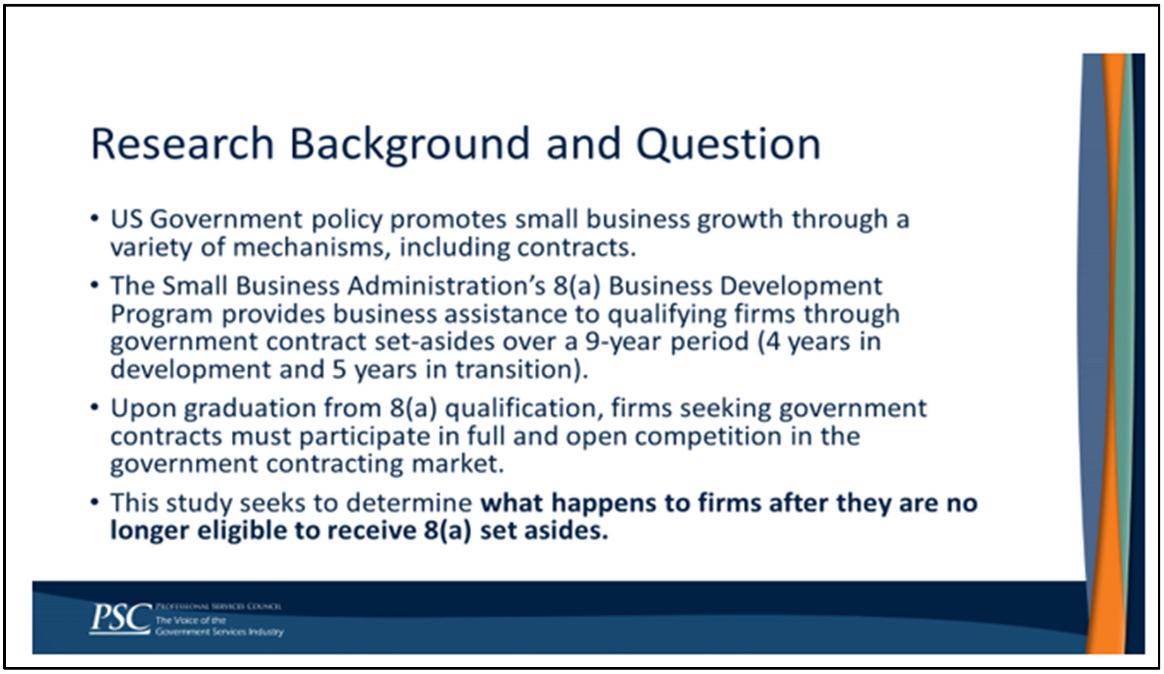

Figure 1. Research Background and Question

The 8(a) Program allows disadvantaged businesses[2] to compete for set-aside contracts, amongst other benefits. Firms may remain in the 8(a) program for up to nine years and may graduate from the program early in the case that they exceed size limits before the nine-year period of eligibility has expired.

The expiration of 8(a) eligibility for a company is commonly referred to as "graduation." From that point, previously certified firms may continue to pursue full and open competition for government contracts. This means they will need to be ready to compete with significantly larger and better resourced competitors. This study seeks to determine what happens to firms after they are no longer eligible to receive 8(a) set-asides.

Research specific to the 8(a) Business Development Program and its outcomes is relatively limited. However, there is a body of research that more broadly explores the role of

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[2] "Disadvantaged" is defined by Title 13, Part 124 of the Code of Federal Regulations (CFR) and focuses on socially and economically disadvantaged individuals.

set-asides in the government contracting industry both in the United States and internationally.

A 2013 study by Jun Nakabayashi sought to estimate additional cost to government of procurement via set-asides for public construction projects in Japan. The study estimated that roughly 40% of small and medium contracting firms would fall out of the market if set-asides were taken away. The study concluded, therefore, that procurement cost would likely increase as competition decreased (Nakabayashi, 2013). That conclusion may require further analysis and verification.

Further, a 2011 comparison of small business contracting in the United States and in Europe found an increasing interest in fostering small business procurements in the European Union and some of its member countries (Kidalov, 2011). Small business set-asides and other means of supporting the competitiveness of these firms may be an important component of a healthy federal contracting market. However, that success can be jeopardized if, after graduation, those firms have difficulty remaining competitive or even staying in business.

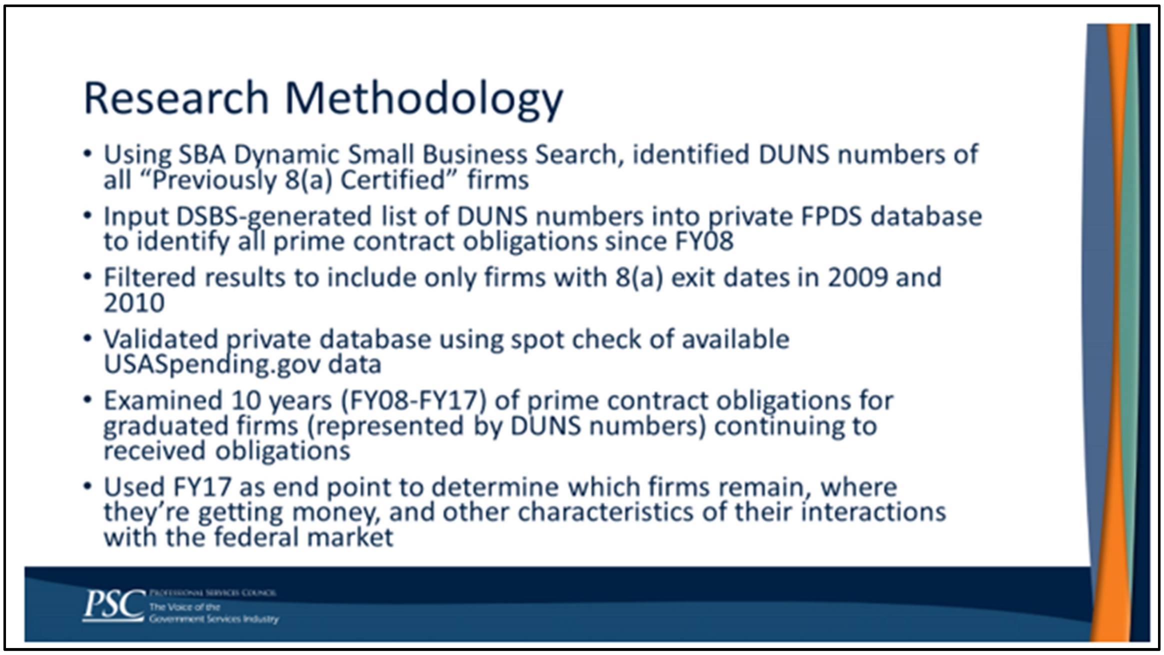


Figure 2. Research Methodology

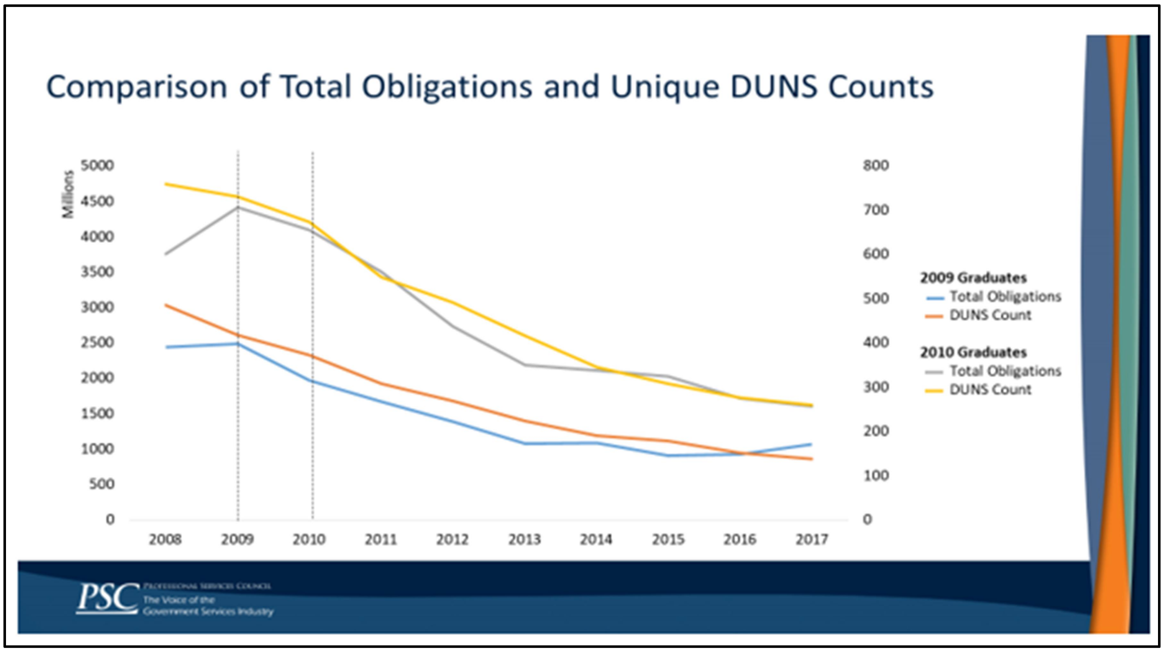
For purposes of this study, we narrowed our focus to those firms that graduated from 8(a) eligibility in 2009 and 2010. These two groups of firms will henceforth be referred to as "graduating classes," designated by their year of graduation.

We first identified firms of interest using the Dynamic Small Business Search (DSBS), furnished by the Small Business Administration. The search consisted only of previously 8(a) certified firms. The search did not include any firms with active 8(a) certifications. Due to the large number of firms that met this criterion, the DUNS numbers were gathered in groups of roughly five geographic states at a time. The resulting output from the DSBS included DUNS numbers and corresponding locations and 8(a) exit dates.

After compiling a complete list of previously 8(a) certified DUNS numbers, all relevant contract data since FY08 were queried within a proprietary database of federal obligations data, originally extracted from the Federal Procurement Data System (FPDS). To ensure the fidelity of the data, we spot-checked a sample of the selected DUNS numbers against obligations data available at USASpending.gov.[3]

We examined 10 fiscal years' worth of data for DUNS numbers continuing to receive obligations (Figure 3). We then used FY17 as an end point to examine who was still in the market, who their customers are, and other characteristics of their interactions with the federal market.

There are limitations when using obligations data provided by FPDS, with occasional errors and other inconsistencies within the data. Our work over the years with FPDS data shows, however, that such errors tend to be consistent over time and have little influence on long-term trends. Therefore, our analysis focuses on overarching trends within the data.



Note. This figure shows total contract obligations in current dollars, to the 2009 and 2010 graduates.

Figure 3. Comparison of Total Obligations and Unique DUNS Counts

One obvious metric for measuring the success of the 8(a) program is the number of firms remaining in the federal contracting market several years after their graduation from set-aside eligibility. There are, however, significant limitations to this approach. First, it is possible for a single firm to have more than one DUNS number, dependent on the services they provide and the customers they supply. It is also possible that a simple count of unique DUNS numbers will overestimate the number of firms participating in the market. Second, differences in spelling and format of vendor name entries in FPDS make it difficult to prevent overestimation using vendor names. Finally, there is nothing within FPDS data to indicate

[3] Because the data provided by USASpending are updated regularly, the obligations totals provided there and those provided by the proprietary database did not match exactly. However, the differences were minimal and deemed insignificant to the analysis.

why a DUNS number is no longer receiving prime contract obligations in later years. If a DUNS number is no longer receiving obligations after graduation, the firm may have failed and subsequently gone out of business, or it may have merged, been acquired, became only a subcontractor, or simply left the federal market. Further research will be required.

However, a count of unique DUNS numbers may provide insight into broader outcomes of the 8(a) program. The 2009 graduating class included 418 unique DUNS numbers. Members of the 2009 graduating class received nearly $2.5 billion in prime contract obligations in FY09. By FY17, only 138 unique DUNS numbers from the class of 2009 remained, representing a 67% decrease. In the same year, total obligations for this group had declined to $1.07 billion. Interestingly, this group experienced growth in total obligations over FY16, suggesting a potential rebound.

The 2010 graduating class included 673 unique DUNS numbers. These firms received roughly $4.1 billion in prime contract obligations in FY10. By FY17, only 291 of those unique DUNS numbers received prime contract obligations. At 57%, the attrition rate was slightly lower than that of 2009 graduates. Total prime contract obligations for the group declined to $1.61 billion in FY17 and did not show similar signs of rebounding.

There is a similar pattern in the decline in total prime contract obligations by class following graduation from 8(a) eligibility. For both graduating classes, the initial decline is steep, followed by a flattening out. Overall, only 39% of company-based DUNS numbers were still receiving prime contracts from the federal government in FY17. Contract obligations overall declined nearly as much, with FY17 totals being 41% of the funding in the year of graduation. In addition, the average size of contract obligations per DUNS number rose very little, from $6.05 million in graduation year to $6.25 million in FY17. Adjusted for inflation, the value of such obligations actually declined.

Total Obligations: Department of Defense

	2009	2011	2013	2015	2017
2009 Grads					
Army	737,864,519	356,425,288	214,620,537	105,488,964	122,804,981
Navy	302,180,864	205,579,187	141,215,994	113,880,067	105,556,071
Air Force	231,395,296	150,942,102	84,576,524	97,717,288	150,525,213
DoD Total	*1,433,090,507*	*831,879,516*	*505,882,192*	*401,129,564*	*516,657,411*
2010 Grads					
Army	1,289,416,635	878,477,779	454,728,895	505,338,917	415,838,489
Navy	815,069,314	588,838,673	362,027,167	269,982,826	255,715,927
Air Force	429,784,321	235,350,617	106,877,148	116,101,649	110,308,171
DoD Total	*2,680,988,601*	*1,868,888,722*	*990,488,557*	*946,492,795*	*822,010,449*

Note: Obligation amounts identified by "contracting agency"

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Figure 4. Total Obligations: Department of Defense

In examining the general decline of 8(a) graduates, it is important to note that this decline does not occur uniformly across graduating classes or contracting agencies. Figure 4 shows trends within the Department of Defense (DoD). There are differences in how 8(a) graduates have fared in working with each military department. The seven-year decline was relatively uniform for 2010 graduates, between 10% and 11% per year for each military department. For 2009 graduates, the largest decline occurred in contracts with the Department of the Army, with a compound annual growth rate of -14.12% over the seven-year period from FY11 to FY17. Alternatively, the seven-year decline was less than 1% for contracts with the Department of the Air Force. Overall, 2009 graduates experienced a 6.58% annual decline in obligations from the DoD between FY11 and FY17.

Additionally, 2009 graduates experienced a significant rebound in prime contract obligations from FY15 to FY17, with the largest growth occurring in contracts with the Department of the Air Force at 15.49%. Contracts with the DoD grew 8.8% over the same period for 2009 graduates. The 2010 graduates did not experience the same rebound between FY15 and FY17, however it is possible that these firms may experience similar growth in FY18.

Total Obligations Amongst Other Agencies

	2009	2011	2013	2015	2017
2009 Grads					
Dept. of State	26,102,914	34,629,639	18,427,001	20,085,687	3,225,553
Veterans Affairs	23,702,739	15,130,194	19,458,063	7,763,811	3,373,248
Dept. of Energy	34,166,782	15,989,055	2,538,206	1,666,730	5,638,490
Other	967,001,895	777,594,461	533,311,172	482,901,276	542,147,095
2010 Grads					
Dept. of State	78,324,034	72,138,760	79,716,915	128,726,033	76,662,238
Veterans Affairs	89,524,637	54,443,534	96,202,468	88,899,068	28,881,349
Dept. of Energy	52,605,523	35,268,168	8,`173,652	19,792,959	36,706,706
Other	1,517,879,364	1,470,772,671	1,016,156,189	843,952,314	643,326,531

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Figure 5. Total Obligations Amongst Other Agencies

Figure 5 shows declines contract obligations for 8(a) graduations from the Department of State, the Department of Veterans Affairs, and the Department of Energy. There is no uniform trend across these agencies.

For the Department of Energy, 2009 graduates experienced a seven-year decline of roughly 14%; they experienced 50% compound annual growth in the three-year period from FY15 to FY17. Prime contract obligations to 2010 graduates working with the Department of Energy were essentially flat from FY11 to FY17, however these firms experienced 23% in compound annual growth from FY15 to FY17.

The Department of State showed a significant decline in prime contract obligations to 2009 graduates over both the three-year and seven-year periods. However, though they experienced a decline from FY15 to FY17, contract obligations to 2010 graduates have remained flat at the Department of State over the seven-year period from FY11 to FY17.

Neither graduating class experienced growth in prime contract obligations with the Department of Veterans Affairs. The largest decline occurred for 2010 graduates between FY15 and FY17 at 31%. The 2009 graduates experienced a 24% decline over the same period.

The number of 2009 and 2010 8(a) graduates receiving federal prime contract obligations receiving federal prime contract obligations declined more than 60% by 2017, and the total value of their contracts by nearly the same amount. However, to understand the viability of 8(a) graduates, it is also important to consider the sources of their contract dollars. Figure 6 shows those sources for 2009 graduates.

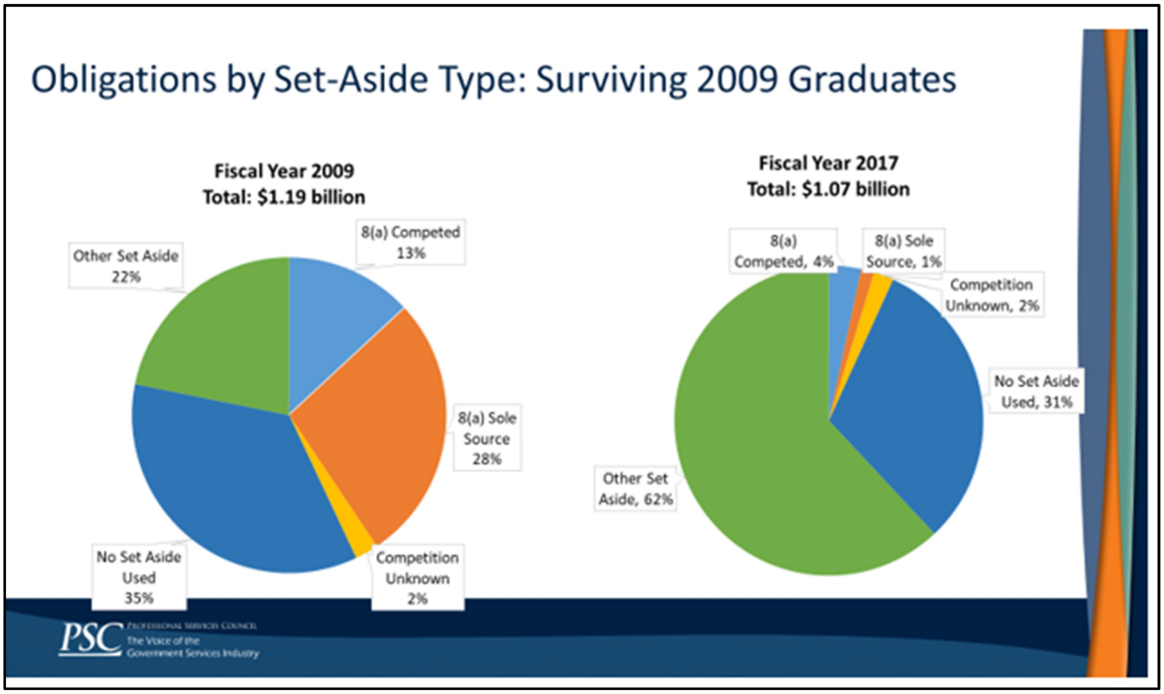

Figure 6. Obligations by Set-Aside Type: Surviving 2009 Graduates

The 2009 graduates received nearly 50% of their prime contract obligations from 8(a) program set-asides in their graduation year. It is also worth nothing, though, that roughly one-third of prime contract obligations for these firms came from full and open competition in FY09.

By FY17, however, the percentage of obligations for 2009 graduates from full and open competition remained the same as in FY09, roughly one-third. The proportion of obligations from other set-asides, on the other hand, more than tripled compared to FY09, from 19% to 62%. In other words, many of these businesses depended on other set-aside programs. A majority of the funds obligated through other set-asides came from general small business set-asides.

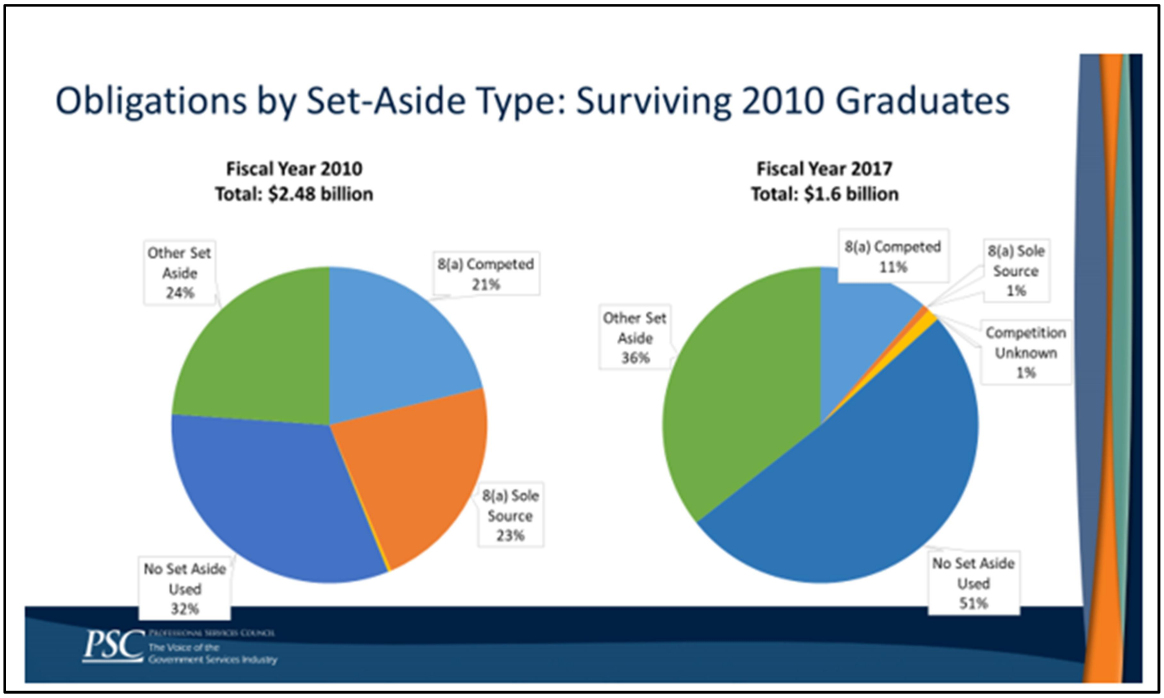

Figure 7. Obligations by Set-Aside Type: Surviving 2010 Graduates

In FY10, 44% of prime contract obligations for 2010 graduates came through 8(a) set-asides. This proportion is nearly identical to 2009 graduates in their graduation year. The 2010 graduates also received a near identical proportion of obligations through full and open competition in FY10. They received a slightly larger proportion through other set-asides.

Unlike 2009 graduates, however, by FY17 there was significant growth in the proportion of prime contract obligations awarded through full and open competition, from 32% in FY10 to 51% in FY17. Contract obligations from other set-asides rose 50%, a far smaller increase than for 2009 graduates.

Conclusion

The 8(a) small business set-aside programs are designed to support small businesses and foster their growth. However, 8(a) graduates do not fare well over time, with more than 60% no longer receiving federal prime contract obligations. Those who were still federal prime contractors grew very little, with the average contract obligation up only 3.3% to $6.25 million from $6.05 million (if we adjusted for inflation, the average would show a decline). Finally, 8(a) graduates still depended on set-asides for more than half of their federal prime contract dollars. Overall, they are not rewarded for graduation.

This suggests that, in general, even 8(a) graduates who are still receiving federal prime contracts are not growing. Further research is needed, particularly to identify which firms have grown and to determine the nature of that growth. Until then, it seems that 8(a) set-asides do not position graduates for growth.

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Acknowledgements

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