



Testimony of  
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House Committee on Small Business  
Subcommittee on Contracting and Infrastructure

“Concerns and Recommendations  
for Improvement of the  
HUBZone Small Business Program”

July 14, 2022

Chairman Mfume, Ranking Member Salazar, and Members of the Committee, thank you for the opportunity to testify before you today. My name is Brent Lillard, and I am the CEO and co-founder of GovSmart, Inc., an Information Technology Value-Added Reseller and HUBZone Small Business concern. In late 2009, my business partner, Hamza Durrani, and I started the company out of our kitchen in a rented house in the HUBZone of Charlottesville, VA. Today GovSmart has successfully completed over \$1 billion dollars in Federal prime contracts and hundreds of millions of dollars in Federal subcontracts. We currently have 72 full-time employees, and we continue to grow along with the Federal Government's HUBZone requirements. We are members of GovEvolve, the leading advocacy organization for small and midsize businesses that support government innovation. GovEvolve is committed to positive change for companies like ours that sometimes struggle under small business policies, and we are grateful for Madison Services Group's efforts in managing GovEvolve's policy priorities to bring our industry's concerns before you today.

As a thirteen-year HUBZone program member, I have observed the strengths and weaknesses of this program firsthand. I believe it can serve a crucial role in reaching underserved communities, like that of the Rose Hill neighborhood in Charlottesville, VA where our company's headquarters is located. I also believe the program has some endemic challenges that need to be addressed to maximize its reach. I further believe the HUBZone program is engaged in an unanticipated competition for Federal contracts with other highly-valued socioeconomic programs – and I believe it is currently losing that competition.

Today I will cover some of the challenges to success that I believe are endemic to the HUBZone program's structure and offer some ways the program can be improved to better serve those in our community who cannot currently benefit from the HUBZone program. I will also discuss some of the procurement-specific issues that have led the HUBZone program to historically underperform, and some ways I believe this Committee can address those issues. Finally, I will discuss some issues facing all small businesses who are also in the information technology industry.

## **I. Difficulty Hiring HUBZone Residents**

The HUBZone program was set up in 1977 with the passage of what became 15 U.S.C. § 657a with the intent of directing federal contracting dollars into areas where the residents experienced at least 25% poverty based on census numbers.<sup>1</sup> The method envisioned by the program was to certify HUBZone-qualified companies that commit to maintaining a workforce comprised of at least 35% HUBZone residents, with the hope that those employees would earn enough to throw off the burden of historical poverty and re-invest their wages into their communities to benefit the whole area.<sup>2</sup> The reality of how this program works in real communities is far more complicated.

In my experience, it has been very difficult to maintain 35% HUBZone residency for our employees due in part to the economic realities faced by our neighbors here in Rose Hill and other HUBZone locations in our city. Many of these residents qualify for and receive public assistance

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<sup>1</sup> See 26 U.S.C. § 42(d)(5)(B)(ii) (2020).

<sup>2</sup> See e.g. S. 208, The HUBZone Act of 1997: Hearing Before the Senate Comm. on Small Bus., 105th Cong., 1st Sess. 1-3 (April 10, 1997).

in the form of unemployment, food stamps, access to affordable housing, and other programs on which they have come to rely. After starting work with our company, many of these employees realized they would become ineligible for the public assistance. The GovSmart entry-level salary exceeded the maximum they could earn without losing such benefits. Faced with the economic conundrum that their earned wages did not significantly exceed their public assistance, they resigned from employment. In some cases, and as recently as last month, employees requested fewer hours than were available to keep from exceeding the public assistance thresholds. Many of the new employees left demoralized and convinced that employment with our company was not the saving grace they expected. Even our best efforts to retain employees – which include generous time off policies, a practically unlimited fully-stocked kitchen, very competitive compensation plans, and even dedicated prayer rooms – could not overcome this simple economic analysis.

Difficulty in hiring HUBZone residents has long been recognized by the HUBZone Program, and the SBA's new shift towards allowing "legacy" employees has helped tremendously.<sup>3</sup> Additionally, the ability for a firm to earnestly attempt to hire and retain HUBZone residents as employees without losing its program eligibility have softened the impact for firms that do not meet the requirement. However, the 35% requirement remains the baseline, and firms like GovSmart struggle to both attract new employees and stay compliant with the program.

One thing to consider is whether the HUBZone designation of the individual's residence is the only effective metric for identifying those suffering from economic hardship. In our city alone, we have seen struggling individuals who live below the poverty line and would make acceptable employees, but they do not live inside of HUBZone. We cannot hire them without risking the loss of our HUBZone status. To address this, we recommend the HUBZone program relax the residency requirement to include any member of the community that falls below the poverty line, regardless of whether they live in the HUBZone. This should also include those who currently lack a permanent residence at all.

## **II. Government Failure to Meet HUBZone Goals**

SBA HUBZone program participants expect to receive at least 3% of all Federal contracting dollars based on Congressional requirements in 15 U.S.C. § 644(g)(1)(A)(iii). This is the incentive for companies to become involved in the program. However, most agencies do not meet their HUBZone goals. In 2020, the Federal Government's Small Business Procurement Scorecard revealed that it only awarded 2.44% of procurement funds to HUBZone companies, short an amount equivalent to more than \$3 billion dollars.<sup>4</sup> The percentage awarded to HUBZone companies in 2020 was highest of the last five years, during which the average HUBZone percentage was only 2.02%.<sup>5</sup>

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<sup>3</sup> See Small Business HUBZone Program and Government Contracting Programs, 84 Fed. Reg. 6522 (Nov. 26, 2019).

<sup>4</sup> The SBA records the amount of total contract dollars eligible for Small Business set-aside contracts for FY2020 as \$560 billion. By awarding only 2.44% of such funds to HUBZone firms leaves a shortage of 0.56%, or \$3.136 billion. See FY2020 Government-Wide Scorecard Summary available at <https://www.sba.gov/document/support-small-business-procurement-scorecard-overview>.

<sup>5</sup> We believe the increase in 2020 is at least partially attributable to the SBA's changes to the HUBZone program in 2019 (see FN3 above).

During each of these years, the government-wide scorecards received a grade of “A,” indicating that in each year the overall contract dollars awarded to small businesses of any designation exceeded 100% of the Congressionally required amount. This result comes even though billions in funds intended for HUBZone companies were redirected to other small business programs. This disparity – receiving an “A” grade while underperforming in HUBZone awards every single year since 2007<sup>6</sup>– comes from the SBA’s scorecard analysis algorithm, which allows extra credit to make up for shortfalls in one socioeconomic program by overachieving in other programs.

For the past 5 years the Federal Government nearly doubled its requirement for Small Disadvantaged Businesses (SDBs) each year. Despite a 5% goal for awards to SDBs, the government-wide scorecard shows an average achievement of 9.8%.<sup>7</sup> This indicates that something in the procurement system has skewed procurement dollars in one direction over another.

### **III. Program Rule Changes Not Following the Administrative Procedure Act**

One major complexity experienced by HUBZone companies lies with the ever-evolving standards for eligibility that are often changed outside the requirements of the Administrative Procedure Act.<sup>8</sup> It has become common SBA practice to announce substantive changes to material rules by updating the Agency’s Frequently Asked Questions (FAQ) page, rather than publishing such rule changes in the Federal Register, evaluating comments from affected parties, and then issuing final rules.<sup>9</sup>

An example of this concerns the SBA’s welcome change adding HUBZone “legacy” employees to the roles of qualified HUBZone residents for the purpose of meeting the 35% residency requirement. The rationale for this change is strong and appropriate: HUBZone residents who work hard and earn sufficient funds to move out of a HUBZone area should not then count against the HUBZone firm that yielded them the opportunity to improve their lives. The new rule allowed HUBZone companies to count any employee that qualified as a HUBZone resident in the past, but later moved out of the HUBZone, towards that company’s 35% requirement. As announced in the Federal Register, this rule became final on December 29, 2019.

After the new rule was announced, and out of an abundance of caution, GovSmart contacted the SBA’s HUBZone Program office and specifically asked whether legacy employees would count regardless of how long ago they lived in the HUBZone, so long as they qualified as a resident per the SBA’s residence rules at the time. GovSmart was advised in writing that employees who met the residence requirements as of any previous certification or recertification date would be allowed

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<sup>6</sup> The SBA publishes scorecards only back to 2007 on its website (see FN4 above).

<sup>7</sup> The SBA records SDB awards for the years of 2016-2020 of 9.53%, 9.10%, 9.65%, 10.29%, and 10.54% respectively.

<sup>8</sup> 5 U.S.C. § 553 (2021).

<sup>9</sup> For the relevant F.A.Q., see <https://www.sba.gov/brand/assets/sba/resource-partners/hubzone-program-improvements-faq-508.pdf>.

to count as legacy HUBZone residents. On that advice, we were able to hire additional staff and continue growing – but always staying within the 35% requirement.

However, in an update to the SBA’s Frequently Asked Questions (FAQ) published on June 24, 2021, the SBA included a rather earth-shattering qualification that employees must have established their “legacy” residence within the HUBZone only after December 29, 2019 – the date the rule became final. This change was not made pursuant to the Administrative Procedure Act, and was not publicized beyond the FAQ update. Nevertheless, the consequences of that change are profound. Companies relying on pre-2019 legacy HUBZone residents may find themselves outside the requirement through no fault of their own. Such companies must take drastic and immediate measures to ensure program compliance. By far the quickest path to compliance for most companies facing this issue is to fire as many non-HUBZone employees as necessary to ensure the remaining personnel meet the 35% program requirement.

This ad-hoc rulemaking process of introducing substantive policy changes, sometimes contrary to previously-issued legal advice on which companies like GovSmart were led to rely, makes compliance with HUBZone Program rules very difficult. The overall effect of this process is to keep HUBZone companies in constant apprehension of running afoul of rules that may change at any time. I respectfully request this Committee take steps to ensure the SBA conforms to the established procedures mandated by the Administrative Procedure Act and halt the process of changing substantive rules announced only in FAQ documents.

#### **IV. Procurement Policy Challenges to HUBZone Success – Parity with the 8(a) Program**

The clear explanation for why agencies are drastically over-performing when it comes to Small Disadvantaged Business (SDB) awards comes down to administrative efficiency. It is much faster and easier for a contracting officer to complete an SDB direct-award contract than it is to hold a competition, evaluate proposals, select a contractor, and handle any resulting bid protests that may arise. In a fraction of the time it takes to complete a competitive HUBZone contract, the agency can issue a direct-award to an 8(a)/SDB. The agency will avoid the time constraint of a price competition and be completely immune from vendor protests, as such awards are only reviewed by the Government Accountability Office (GAO) in very narrow circumstances, such as bad faith or violation of procurement rules.<sup>10</sup>

Under the SBA’s 8(a) direct award authority, a Government agency may award contracts without providing for the competition otherwise required by the Competition in Contracting Act.<sup>11</sup> Provided that Agency procurement officials establish a firm’s eligibility and reasonable price, they can award a contract to meet Agency needs in a fraction of the time it takes to procure the same good or service from a HUBZone firm.<sup>12</sup> Before a contracting officer can issue a direct award to a HUBZone firm, that contracting officer must establish that only one HUBZone is likely to be capable of contract performance – something almost never true given the field of HUBZone firms that compete for these contracts.

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<sup>10</sup> See, e.g., Matter of MCB Lighting & Electrical, B-406703 (July 13, 2012).

<sup>11</sup> 41 U.S.C. 3301 (2020).

<sup>12</sup> 48 C.F.R. § 19.800 (2020).

GovSmart was also an SDB under the SBA's 8(a) Business Development Program during our first years. During our years as an 8(a) SDB, we benefitted from this program and received many direct awards. We were nevertheless aware that the HUBZone status that we concurrently held was a distant second in terms of business growth and development. When we graduated early from the 8(a) program in 2019, we had already transitioned to lean primarily on our HUBZone status, and we survived the loss of the direct awards. Now we struggle to make the case to Government agencies for why they ought to set a given procurement aside for HUBZones. They know, as we do, that the lack of direct award authority means a lack of efficiency.

This explains one major component of the disparity between the abundance of contract dollars awarded to SDBs and the annual failure of the Government to even reach the HUBZone minimums. To correct this disparity, I respectfully request that this Committee consider advocating for parity amongst the programs. The direct-award authority now benefiting only SDBs should be extended to all of the other programs or ended all together. Another option would be for the direct-award authority to only be granted when an agency is behind on their goals in a certain area. This change could be made by adjusting the language in the current HUBZone direct award authority to remove the requirement that procurement officials compete any requirement when more than one HUBZone is likely to supply a bid.<sup>13</sup>

## **V. The Need for a Dedicated Industry Code**

GovSmart is a reseller of information technology goods and services. We perform a critical function for the Government as an interface with the expertise and connections to assess a Government technology requirement and match that need to quality products or services offered by literally thousands of manufacturers. With our help, the agencies do not need to directly survey the universe of available solutions to a given tech problem – they can instead pose the requirement to us and our competitors, and with our amassed knowledge and experience, we can compete to recommend the best technology solution.

Resellers are not manufacturers, or, under most circumstances, direct service providers. We are more analogous to wholesalers, leveraging the benefits of volume and supplier relationships to provide prices to the government that are well below the manufacturer's suggested retail price (MSRP). We are also full-spectrum prime contractors with project management capability, ongoing customer support obligations, and expertise in architecting solutions that will meet our customer agency's needs.

The SBA currently prohibits the use of industry codes that are the most descriptive of our industry. For various reasons, including the need to track categories of government spending, the SBA requires us to classify ourselves as either manufacturers or service providers under the North American Industry Classification System, or NAICS, codes appropriate for those industries. For example, computer manufacturers are generally classified under NAICS code 334111, *Computer Device Manufacturing*. Computer service providers are generally classified under NAICS code

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<sup>13</sup> 48 C.F.R. § 19.1306(a) currently reads in relevant part, "A contracting officer shall consider a contract award to a HUBZone small business concern on a sole source basis ... provided that . . . (1) The contracting officer does not have a reasonable expectation that offers would be received from two or more HUBZone small business concerns." Removing this requirement would place HUBZone small businesses on parity with 8(a) SDBs for direct awards.

541519, *Other Computer-Related Services*. By forcing resellers to classify themselves falsely as either manufacturers or service providers, all procurement dollars awarded to resellers can be used to capture overall government spending on supplies and services. However important the benefit of such data, or however difficult it may be to acquire otherwise, this system results in very serious harm to the very small businesses the SBA is chartered to shepherd.

If a reseller classifies itself as a manufacturer, it falls under the rules applicable to manufacturers, including size standards that are formulated to be relevant to companies engaged in manufacturing, not resale. These are generally employee-based size standards. For services companies, small businesses must not exceed a specified amount of annual revenue. As a reseller is not a manufacturer or a service provider, neither yardstick properly measures companies in our industry. The SBA has attempted to fix this issue by creating an exception within the 541519 NAICS code for Information Technology Value-Added Resellers (ITVARs), but this exception falls drastically short of an actual solution as it continues to deny the reality that resellers are primarily wholesalers and not service providers or manufacturers.

With an information technology reseller industry in the billions of dollars annually, this harm affects many companies and their employees. I respectfully request that this Committee consider taking steps to establish an industry-specific NAICS Code focused on information technology resellers that results from an honest evaluation of our industry. I would welcome the chance to discuss this issue more fully in a hearing focused on these NAICS codes, as I believe that is the only way to fully explore the complex consequences that follow from forcing the use of inaccurate codes.

## **VI. Need to Re-Assess the Non-Manufacturer Rule**

The most troubling rule inherited from the misclassification of information technology resellers is known as the “Non-Manufacturer Rule” (NMR), which requires among other things that any small business reseller bidding on a contract set aside for small business be either the manufacturer of the goods it offers, or to supply only goods made by another small business.<sup>14</sup> At first glance, this statutory rule is important to support small business manufacturers against the encroachment of large businesses that could offer lower prices based on lower production costs, etc. As applied to resellers of normal commodities such as office chairs or military uniforms, this requirement makes intuitive sense – as does the possible penalties for violation. A violation of this rule carries with it a minimum fine of \$500,000 and potential debarment. One infraction could therefore be insurmountable for a small business. As applied to the information technology value-added reseller industry, the NMR has become increasingly irrelevant and problematic to companies like GovSmart.

Information technology presents the greatest advantage – and the greatest risk – to government operations, and not just any product can be used on Government networks and to store or process Government data. Only the most well-built, heavily tested, and highly certified products meet current government standards. Accordingly, Government agencies can only buy these industry-leading products – nearly all of which are manufactured by large businesses. Few small business

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<sup>14</sup> 15 U.S.C. 637(a)(17) (2020).

products can qualify under the ever-more-stringent cybersecurity and supply chain risk management regulations applicable to these products.

This leaves GovSmart in a lurch. Being subject to the nonmanufacturer rule, we must either manufacture the computers we sell or offer to sell computers manufactured by another small business. However, our customer can only purchase computers made by large businesses that can ensure their products are tested and certified as safe. The same concern applies to software manufactured by large businesses. Increasingly, small business resellers cannot comply with the nonmanufacturer rule and still provide the products the Government needs.

This issue has now been recognized by many Government agencies that are moving to address the problem. For example, the SBA itself issued in 2019 a waiver of the NMR with respect to laptop and tablet computers after research amassed by GovEvolve and Madison Services Group demonstrated conclusively that no small businesses make laptops and tablets in quality and quantities sufficient to supply the Federal market.<sup>15</sup> Two large Government Departments have now also recognized the inherent problems with enforcing the NMR against IT resellers. These agencies sought and obtained from the SBA waivers of the NMR for their upcoming information technology government-wide acquisition contracts (GWACs) known as First Source III (DHS)<sup>16</sup> and Information Technology Enterprise Solutions – 4 Hardware (ITES-4H, Department of the Army).<sup>17</sup> Together, resellers like GovSmart will sell close to \$20 billion in products to these agencies, but without the unnecessary threat of heavy fines and company-ending debarment.

IT resellers face a unique problem with respect to the NMR, and these organizations have recognized these challenges. I therefore respectfully request that this Committee examine the use and need of the NMR for all information technology procurements, especially those impacting IT resellers, across government. This would allow us to fulfill both our customer's needs and our duty to comply with all procurement laws and would be a welcome change across the IT reseller industry. With respect to other industries, there are two additional improvements to the NMR that would help other industries when it comes to compliance. First, the SBA should be required to provide justification if an NMR waiver is not granted. Second, the SBA should provide a list of elements to agencies that must be included in the waiver so that all parties are clear on the application of the waiver.

## **Conclusion.**

The HUBZone program is a valuable way to inject Federal procurement dollars into underserved communities. However, the program would benefit greatly from the changes recommended during today's testimony. These changes will help our company further benefit this community and its underserved areas. The addition of a new industry code focused on information technology resellers like GovSmart, and the removal of the Non-Manufacturer Rule will also help our company tremendously.

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<sup>15</sup> 85 Fed. Reg. 13692 (Mar. 9, 2020).

<sup>16</sup> DHS Solicitation # 70RTAC21R00000003, available at [www.sam.gov](http://www.sam.gov).

<sup>17</sup> Solicitation # W52P1J-20-R-0082, available at [www.sam.gov](http://www.sam.gov).



I have also attached a brief outline of additional issues important to us as a Small Business. Thank you for the opportunity to testify today, and I look forward to answering your questions.

**Supplement:**  
**Challenges of being HUBZone Certified**

1.) Difficult to scale with the 35%/50%+ eligibility requirement

**i. Difficult to hire inside of HUBZone because of the lack of available skilled labor**

1. When people become skilled, they make more money and move out of the HUBZone. This leaves mostly unskilled workers in the areas we must hire 35% of our workforce from.
2. Some potential employees are homeless or couch surfing to survive, and although they are below the poverty level, they do not qualify for HUBZone employment or possess the skills necessary to occupy one of the available job positions that do not require HUBZone residency.

**ii. Difficult to hire because potential employees lose government assistance**

1. New hires will potentially lose public assistance in the form of:
  - a. Unemployment
  - b. Supplemental Nutrition Assistance Program (formerly known as Food Stamps)
  - c. Access to Affordable Housing (section 8)
  - d. Child Care Services
  - e. Energy Assistance
  - f. Medicaid
  - g. Temporary Assistance for Needy Families
2. We have countless examples of people voluntarily terminating their employment when they realize that they must work full-time to pay the bills, and that so many of their government assistance programs end because of their employment.

**iii. Difficult to invest in building infrastructure**

1. HUBZone maps can change with the census at any time, without adequate warning, after a major long-term investment is already made in a property
  - a. This forces HUBZone companies to always rent their office space (usually at a higher rate than the mortgage) or take massive financial risks by purchasing a property that may not be useful to them in the near future.

- b. This disincentivizes HUBZone employers to help transform the HUBZone into a zone with higher-opportunity and poverty rates below 25%.
- c. Being truly successful in the program is corporate suicide. The rules force the companies to move into a new HUBZone, leaving all of those gained jobs behind.

2.) Preference is given to 8(a) companies because of the Direct-Award rules

**i. Standard 8(a) companies receive direct-award contracts up to \$8M for hardware contracts, and Native 8(a) companies can receive direct-award contracts up to \$22M (Civilian) and \$100M (DOD) with no competition.**

- 1. 8(a) direct-award contracts cannot be protested. In most cases, HUBZone companies can't even see them. We are not considered an "interested party" by the Agency, GAO or CFC, and so we cannot successfully protest a solicitation or subsequent award to a competitor with an inferior solution or value.
- 2. 8(a) direct-award contracts are much faster to award because there is no competitive process.
- 3. 8(a) direct-award contracts can allow contracting personnel to effectively choose their brand of manufacturer while avoiding the standard process of having to write a "Justification and Approval" for that brand, and then having to get it approved by a Senior Procurement Executive, or higher.

**ii. Agency procurement scorecards allow up to 200% extra-credit for doubling the 8(a) goal, effectively raising the weighted performance to 20%.**

- 1. Agencies contracting shops have all figured out that they can use the other socio-economic programs and particularly the 8(a) program, which is easier/faster/less stressful, to meet and far exceed their shortfall of the HUBZone goal. See chart below:

## Calculating Prime Contracting Score

Category	Category Component Achievement	/	Goal	=	Achievement Score	X	Component Weight	=	Weighted Performance
Small Business	21.00%	/	23%	=	91.3%	x	60.00%	=	54.78%
SDB	10.50%	/	5%	=	200.00%*	x	10.00%	=	20.00%
WOSB	4.00%	/	5%	=	80.00%	x	10.00%	=	8.00%
SDVODB	3.50%	/	3%	=	116.67%	x	10.00%	=	11.67%
HUBZone	1.50%	/	3%	=	50%	x	10.00%	=	5.00%
<b>Total Prime Contracting Weighted Performance (Prime Score)</b>									<b>99.45%</b>

\*achievement score capped at 200.00%

- 3.) NAICS-related size-standards and FAR Non-Manufacturer-Rule are not being applied properly, and have a high potential and great financial incentive for abuse
- i. **Class-waivers/Individual Waivers to the NMR only recently applied to the HUBZone program at all.**
    1. This is one of the changes that positively impacted the goal achievement this year
  - ii. **Hybrid NAICS 541519 with VAR Exception is widely used incorrectly**
    1. The largest Government-Wide-Acquisition-Contract for IT products/services (SEWP V) received an exception for accidentally ignoring the Non-Manufacturer-Rule in the contract competition stage, making it possible for the industry to “get around” the requirements to provide items manufactured by a similarly situated entity.
  - iii. **Manufacturing NAICS 334111 and other 3-series NAICS codes are widely used incorrectly**
    1. There is no class-waiver for Desktop computers or Servers (and the laptops/tablets waiver only created very recently with the help of GovEvolve).
  - iv. **NAICS 423430 perfectly describes our industry but is not used anymore due to problems with classification of items purchased.**
    1. The “work-around” (using 541519) which is widely used, has the same problem attached to it, while creating even more problems along the way.

- 4.) Government-incentivized predatory bidding strategies benefit the largest “in the know” contractors, while leaving honest contractors (often small HUBZone companies) out in the cold
- i. We created an animated video to explain the problem.  
<https://www.youtube.com/watch?v=WkMMvTnYxfM>
  - ii. Summary: Companies are highly incentivized to lie about their prices to score huge multi-billion-dollar Government-Wide-Acquisition-Contracts for commercial-off-the-shelf IT products, knowing full-well that they will never have to honor those prices. This is due to the length of the price competition and the inevitable release of new items that will replace the old ones by the time the contract goes live. This strategy is known by all the big players in the industry, and despite our best efforts to educate the contracting officers away from this by only evaluating pricing at the task-order-level, we are failing to get through. Even high-level Federal procurement attorneys have suggested that we do what everyone else does since there is no clearly defined rule against it, or metrics to evaluate it.
- 5.) Deal Registrations cause large businesses to profit more at the expense of Small Businesses
- i. Most major manufacturers have “Deal Registration” programs in place to incentivize being first to bring an opportunity to the manufacturer. The “registered” partner receives major discounts from ~15-90% off the standard reseller cost, causing a completely uneven playing field.
  - ii. Large business resellers are usually the ones that the end users come to when deciding what to buy. By the time it gets to contracting and gets set-aside for a socio-economic program, the deal is already “registered.” This means that the small business prime contractor must now buy the products from the large business who is registered, or else pay a lot more for those products to go direct to the manufacturer. This almost always leads to the large business middle-man controlling all of the pricing, and keeping the lion’s share of the margin for themselves. It is more common than not for the small businesses to receive an RFQ directly from contracting, only to find out that a large business partner is registered. Common practice is for the small business to mark-up the products by 1%-3% when the large business has significantly higher margin (sometimes more than 10 times more margin than the small business). The chain usually looks like this:

**Manufacturer → Distributor → “Registered” Large Business → Small HUBZone Business → Government**

*\*Every tier has its own markup added on\**

## **Suggestions to help the HUBZone program achieve its goal:**

- 1.) Create parity in all socio-economic programs
  - a. Activate the SBA direct-award program in all socio-economic areas where the goal has not yet been met by the agency.
  - b. Require the same 5% of contracting dollars to go towards HUBZone and SDVOSB companies (just like SDB companies).
  - c. Do not allow extra-credit for using easier programs like the 8(a)/SDB program.
- 2.) Create more incentive for HUBZone residents to become gainfully employed
  - a. Slowly scale back on incentives to stay at home. Instead, funnel that money to the disadvantaged workers directly through their employers. This would supplement their income to offset their much higher training costs and would incentivize gainful, taxable, long-term employment.
- 3.) Grandfather the HUBZone principal office permanently
  - a. Helping to make the HUBZone prosperous should not be a corporate death sentence.
  - b. Moving to another HUBZone would leave a hole in opportunity. Corporate displacement is the downfall of many impoverished areas (Detroit, East St. Louis, etc.).
  - c. This will allow HUBZone companies to save money and invest in their community by purchasing building infrastructure without taking on a massive financial risk that they cannot control.
- 4.) Allow all potential employees under the poverty level to count as HUBZone
  - a. Homeless/Couch surfing candidates who cannot afford to pay for a house/room in the HUBZone should not be ineligible for this type of Federal help.
  - b. Grandfather them in so that employers are incentivized to permanently transform them into skilled workers.
- 5.) Permanently and retroactively grandfather employees who lived and worked in the HUBZone for a long period of time before the “Legacy” changes were made
  - a. The addition of the new rule for “legacy” employees was having a very positive impact on the way that HUBZone companies operate. It creates incentive to create skilled workers who eventually earn more money and can afford to live in a nicer home outside of the HUBZone. This policy should be completely retroactive, to not unfairly punish companies who created prosperity amongst the HUBZone employees in the past. In our case, we have opened a case and received a letter from the Deputy Director of the HUBZone Program, stating that we were in compliance and that our old “legacy” employees count as HUBZone. Then without warning, the FAQ was updated to discontinue the retroactive nature of the rule. We only now discovered this while preparing this testimony and now our

entire company is at risk.

6.) Bring back the NAICS code for IT Product Resellers (423430) and have a size standard of 150 employees

- a. The 423430 NAICS accurately describes the type of companies that receive these awards. Manufacturing NAICS codes are not appropriate because we are not manufactures and the size standards (1250 employees) make no sense for resellers. Services NAICS codes have revenue-based size standards that make no sense if you also sell IT-hardware in bulk at very slim margins.
- b. Currently the “work around” is to use NAICS 541519, which is a catch-all and has a 150-person size standard when using the VAR exception. The problem with this NAICS is that it requires 15%-50% services and this is usually fudged.
- c. This would solve the size standard issues and allow small businesses and socio-economic companies to compete.

7.) End predatory pricing strategies by changing the way the proposals are evaluated

- a. Force agencies to do all price competitions at the task order level where the order will have to come to fruition. Outlaw arbitrary price competitions where bidders make up their price out of thin air to secure lucrative contracts over long periods of time.
- b. Provide active on-ramps for all multi-year-multiple-award Agency and Government-Wide-Acquisition-Contracts. This will allow smaller HUBZone companies to compete.

8.) Educate Contracting Personnel about “Deal Registrations”

- a. Contracting Officers need to understand Deal Registrations and how they negatively impact the companies who do not hear about the opportunity first.
- b. One solution is for the “market research” to be completed by a small HUBZone business/socio-economic potential awardee, so that they have an opportunity to hold the registration without having to “multi-tier it” by buying from a large business who buys it from the manufacturer directly.