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112TH CONGRESS
2d Session
HOUSE OF REPRESENTATIVES
REPORT
112–724

SMALL BUSINESS PROTECTION ACT OF 2012

DECEMBER 21, 2012.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. GRAVES of Missouri, from the Committee on Small Business, submitted the following

R E P O R T

[To accompany H.R. 3987]

[Including cost estimate of the Congressional Budget Office]

The Committee on Small Business, to whom was referred the bill (H.R. 3987) to amend the Small Business Act with respect to small business concern size standards, and for other purposes, having considered the same, report favorably thereon with amendment and recommend that the bill, as amended, do pass.

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I. AMENDMENT

The amendment is as follows:

The amendments (stated in terms of the page and line numbers of the introduced bill) are as follows:

Page 1, strike lines 9 through 10 and insert the following:

"(1) by striking 'SEC. 3.' and inserting the following:

"'SEC. 3. DEFINITIONS.'; and'".

Page 3, line 1, strike "In conducting" and all that follows through "the following" on line 4, and insert the following: "In conducting rulemaking to revise, modify or establish size standards pursuant to this section, the Administrator shall consider, and address, and make publicly available as part of the notice of proposed rule making and notice of final rule each of the following".

Page 3, line 20, strike the closing quotation marks and the period and insert the following:

> "'(8) NUMBER OF SIZE STANDARDS.—The Administrator shall not limit the number of size standards it creates pursuant to paragraph (2), and shall assign the appropriate size standard to each North American Industrial Classification System Code.'.".

II. PURPOSE AND BILL SUMMARY

The purpose of H.R. 3987, the "Small Business Protection Act of 2012," is to amend the Small Business Act (the Act) [1] to impose additional constraints on the ability of the Administrator of the Small Business Administration (SBA) to create size standards for small business concerns. Specifically, the legislation requires the Administrator to justify the rationale for adopting a common size standard for a group of industries, requires such size standards to be adopted after notice and comment rulemaking, and prohibits the Administrator from artificially limiting the number of size standards needed to define a small business concern for each of the industries enumerated in the North American Industrial Classification System (NAICS).

III. NEED FOR LEGISLATION

Under the Small Business Jobs Act of 2010 (Jobs Act), SBA was tasked with reviewing all size standards for each NAICS code set forth in the agency's regulations, 13 C.F.R. § 121.201, within the next 5 years.[2] Specifically, a third of the standards must be reviewed every 18 months. When reviewing and setting size standards, Section 3(a)(1) of the Small Business Act provides, in pertinent part:

> [a] small business concern . . . shall be deemed to be one that is independently owned and operated and which is not dominant in its field of operation.[3]

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[1] Originally, title II of the Act of July 30, 1953, c. 282, 67 Stat. 232 was designated as the Small Business Act of 1953. A plethora of amendments in subsequent Congresses led to a rewrite in 1958. Pub. L. No. 85–536, § 1, 72m Stat, 384 (1958). The Act is codified at 15 U.S.C. §§ 631–657q.

[2] Small Business Jobs Act of 2010, Pub. L. No. 111–240, § 1344, 124 Stat. 2504, 2545–46 (2010).

[3] 15 U.S.C. § 632(a)(1).

The Act does not define the terms "independently owned and operated" or "dominant in its field of operation." Instead, the Administrator is authorized to:

> specify detailed definitions or standards by which a business concern may be determined to be small for purposes of this Act or any other Act.[4]

The Administrator is authorized to consider number of employees, dollar volume of business,[5] net worth,[6] net income, other factors, or any combination of those factors. In short, Congress has granted the Administrator substantial discretion in the factors that will be utilized in calculating the size of a small business. The SBA's discretion is tempered by the fact that any size standard determined by the factors set forth in 3(a)(2) of the Small Business Act must meet the overarching principles—that the business must be independently owned and operated and not dominant in its field.

The SBA took the authority granted by Congress and developed size standards for individual categories of small businesses. Originally, the size standards were developed based on four-digit classifications of each type of business using Standard Industrial Classifications or SIC codes. When the Federal government moved to the more exact NAICS for data collection, the SBA modified its size standards to fit the new NAICS codes.

Historically, the SBA utilized two distinct standards for determining whether a business was not dominant in its field. Manufacturers, distributors, and certain utilities were measured by the number of employees. All other businesses, both services and retail establishments, were calculated by the gross revenue of the firm. The two standards never overlapped. If the SBA determined that a particular industry was measured by gross revenue, the SBA also did not impose an employee threshold. Thus, the SBA created a bright line standard in which a business either was required to enumerate employees or tabulate gross revenue.

SBA formalized its process for establishing size standards when it published a white paper entitled "Size Standards Methodology" detailing the five primary industry factors considered when establishing size standards.[7] The five factor analysis begins by examining four economic characteristics of the industry: average firm size, startup costs and entry barriers, industry competition, and distribution of firms by size.[8] SBA's fifth factor examines the impact of an existing size standard as well as the potential impact of a size standard revision on SBA's Federal contract assistance to small businesses. After considering the primary evaluation factors, SBA then will assess any industry specific factors, such as technological changes and industry growth trends. This methodology supports the Committee's longstanding view of how size standards should be developed: granular analysis of specific industry characteristics.

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[4] 15 U.S.C. § 632(a)(2)(A).

[5] Current SBA size standards use gross revenue as a measure of dollar volume. Nothing in the Act requires reliance on dollar volume and other measures could be used.

[6] The net worth standard is used, for among other purposes, to determine eligibility for investments made by small business investment companies, loans made pursuant to Title V of the Small Business Investment Act of 1958, and for participation in the program established by 8(a) of the Small Business Act.

[7] 74 Fed. Reg. 53940 (October 21, 2009).

[8] 13 C.F.R § 121.102(a))

In some cases where industries are closely related, SBA will consider a common size standard, even if the underlying analysis would otherwise support different size standards. This will most often occur when many of the same businesses operate in the same two or more industries, so SBA believes that the common size standard will better reflect the industry marketplace. Data for this analysis is drawn from the Economic Census, and County Business Patterns, each published by the United States Census Bureau, as well as the United States Bureau of Labor Statistics' Quarterly Census of Employment and Wages and Business Employment Dynamics, the Risk Management Association's Annual Statement Studies, the Federal Procurement Data System, and SBA's own lending data. After the analysis is complete, SBA then proposes what it believes to be the correct size standard. Final size standards are selected after input from the public through notice and comment rulemaking.

Currently, there are roughly 1100 industrial classifications for which the SBA has implemented 38 size separate size standards. These standards are based on either the number of employees, gross revenue, or other factors[9] that the SBA believes reflect the correct size of the business. However, to simplify the size standards, SBA has proposed selecting future size standards from a limited number of fixed size standards. The eight revenue based standards will be $5.0 million, $7.0 million, $10.0 million, $14.0 million, $19.0 million, $25.5 million, $30.0 million, and $35.5 million, and the eight employee based standards will be 50 employees, 100 employees, 150 employees, 200 employees, 250 employees, 500 employees, 750 employees, and 1,000 employees. The SBA will transition to these size standards over the course of five years, as it conducts a systematic review of all its size standards required by § 1344 of the Jobs Act.

As SBA has begun implementing this approach, several industries have expressed concerns regarding the impact this will have and SBA's failure to properly follow its own methodology. Due to this, H.R. 3897 prevents the SBA from creating common size standards or condensing the roughly 1100 industries into 16 size standards for the sake of convenience. Instead, this legislation will require the SBA to ensure that the size standards accurately and legitimately represent small businesses. Additionally, this legislation enhances small businesses' awareness of the size standard process during proposed rulemaking which is essential as the SBA continues reviewing its size standards. To ensure complete transparency, this bill requires all information regarding analysis and rationale to be made publicly available.

IV. HEARINGS

The procedures used by the Administrator to create size standards was fully ventilated in a hearing conducted by the Subcommittee on Economic Growth, Capital Access and Tax entitled "Professional Services: Proposed Changes to the Small Business Size Standards" on May 5, 2011. This hearing reviewed the Small Business Administration (SBA) proposed rule increasing the small business size standards for 35 industries and one sub-industry. At

[9] For example, asset size is used to determine whether a bank is small.

the hearing, all witnesses agreed growth in the size standards is necessary to reflect economic conditions, but each disagreed with the changes proposed by SBA.

V. COMMITTEE CONSIDERATION

The Committee on Small Business met in open session, with a quorum being present, on March 22, 2012, and ordered H.R. 3987 reported, as amended, to the House by a voice vote at 10:24 am. During the markup, one amendment was offered and adopted. Disposition of the amendment is addressed below.

Amendment Number One filed by Mr. Walsh (R–IL) clarifies that SBA must make the basis of its rulemakings publicly available, and prohibits SBA from artificially limiting the number of size standards. Amendment Number One was adopted by a voice vote at 10:24 am.

VI. COMMITTEE VOTES

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the recorded votes on the motion to report the legislation and amendments thereto. No recorded votes were taken in consideration of H.R. 3987.

AMENDMENT TO H.R. 3987 OFFERED BY MR. WALSH OF ILLINOIS

Beginning on page 3, line 1, strike "In conducting" and all that follows through "the following" on line 4, and insert the following: "In conducting rulemaking to revise, modify or establish size standards pursuant to this section, the Administrator shall consider, and address, and make publicly available as part of the notice of proposed rule making and notice of final rule each of the following".

Page 3, line 20, insert before the period at the end the following:

> "(8) NUMBER OF SIZE STANDARDS.—The Administrator shall not limit the number of size standards it creates pursuant to paragraph (2), and shall assign the appropriate size standard to each North American Industrial Classification System Code.".

VII. SECTION-BY-SECTION ANALYSIS OF H.R. 3987

SECTION-BY-SECTION ANALYSIS OF H.R. 3987 AS AMENDED

Section 1—Short title

This section provides that the bill may be cited as the "Small Business Protection Act of 2012."

Section 2—Small business concern size standards

This section amends section 3 of the Small Business Act to require that the Administrator of the SBA provide and make publicly available justifications prior to grouping NAICS codes into a single size standard in order to demonstrate that the size standards are appropriate for each industry placed in the grouping. This section also specifies items that the Administrator must consider and address prior to altering or establishing size standards. These items include a detailed description of the industry, an analysis of the competitive environment for the industry, the approach and source

of all data used by the Administrator to develop the standard, and anticipated effects of the proposed rule on the industry. Further, this section indicates that the number of size standards should not be limited and rather that all NAICS codes should be given an appropriate size standard.

VIII. CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, May 8, 2012.

Hon. SAM GRAVES,
Chairman, Committee on Small Business,
House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 3987, the Small Business Protection Act of 2012.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Susan Willie.

Sincerely,

DOUGLAS W. ELMENDORF.

Enclosure.

H.R. 3987—Small Business Protection Act of 2012

Summary: H.R. 3987 would limit the authority of the Small Business Administration (SBA) to set certain size standards for the purpose of establishing eligibility for various federal assistance programs. The bill also would broaden the amount of information provided to the public when the SBA proposes or modifies a size standard.

Based on information from the SBA, CBO estimates that implementing H.R. 3987 would cost $12 million over the 2013–2017 period, assuming appropriation of the necessary amounts. CBO estimates that enacting H.R. 3987 would not affect direct spending or revenues; therefore, pay-as-you-go procedures do not apply.

H.R. 3987 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would not affect the budgets of state, local, or tribal governments.

Estimated cost to the Federal Government: The estimated budgetary impact of H.R. 3987 is shown in the following table. The costs of this legislation fall within budget function 370 (commerce and housing credit).

	By fiscal year, in millions of dollars—					
	2013	2014	2015	2016	2017	2013–2017
CHANGES IN SPENDING SUBJECT TO APPROPRIATION						
Estimated Authorization Level	1	3	3	3	3	13
Estimated Outlays	1	2	3	3	3	12

Basis of estimate: Under current law, the SBA sets out specific criteria, referred to as size standards, that a business must meet to be considered a small business that is eligible for certain federal assistance programs. The agency has established 41 different size

standards covering more than 1,100 industries classified in the North American Industry Classification System (NAICS).

H.R. 3987 would limit the SBA's authority to set size standards for groups of industries unless the agency can justify that the size standard is appropriate for every individual industry included in the grouping. The bill also would require the SBA to make certain information available, including an analysis of the competitive environment and the effect of the standard on the industry in question when proposing or modifying a size standard.

The SBA currently has a staff of four to review and update the 41 established size standards. Based on information from the SBA, CBO expects that the agency would need to add 16 staff positions over time to develop size standards for more than 1,100 individual industries in the NAICS or to provide justification for size standards that would apply to groups of industries. CBO estimates that implementing H.R. 3987 would cost $12 million over the 2013–2017 period, assuming appropriation of the necessary amounts.

Pay-As-You-Go considerations: None.

Intergovernmental and Private-sector impact: H.R. 3987 contains no intergovernmental or private-sector mandates as defined in the UMRA and would not affect the budgets of state, local, or tribal governments.

Estimate prepared by: Federal Costs: Susan Willie; Impact on State, Local, and Tribal Governments: Elizabeth Cove Delisle; Impact on the Private Sector: Vi Nguyen.

Estimate approved by: Theresa Gullo; Deputy Assistant Director for Budget Analysis.

IX. UNFUNDED MANDATES

H.R. 3987 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act, Pub. L. No. 104–4, and would impose no costs on state, local or tribal governments.

X. NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY AND TAX EXPENDITURES

In compliance with clause 3(c)(2) of rule XIII of the Rules of the House, the Committee provides the following opinion and estimate with respect to new budget authority, entitlement authority and tax expenditures.

The Committee does adopt as its own the estimate of new budget authority contained in the cost estimate prepared by the Director of the Congressional Budget Office pursuant to § 402 of the Congressional Budget Act of 1974. While the Congressional Budget Office estimates a cost of $12 million over 5 years to implement H.R. 3987, the Committee estimates that SBA's current costs will decrease. Under SBA's current size standard process, SBA already calculates all the information required under this provision. SBA then takes that information, applies filters to force the size standard into one of SBA's preapproved size standards, and then is required to undertake calculations to blend related industries into a single size standard. It is the height of illogic to assume that a process the SBA currently undertakes to develop individual size standards will cost the agency an additional $2.5 million per year.

H.R. 3987 will no longer require SBA to undertake these additional steps, which will therefore save SBA resources. Furthermore, H.R. 3987's requirement that SBA publish justifications for its size standards as part of the rulemaking process will not add any additional costs, as SBA already publishes these justifications under its current process and is required to do so pursuant to federal law.

XI. Oversight Findings

In accordance with clause (2)(b)(1) of rule X of the Rules of the House, the oversight findings and recommendations of the Committee on Small Business with respect to the subject matter contained in H.R. 3987 are incorporated into the descriptive portions of this report.

XII. Statement of Constitutional Authority

Pursuant to clause 3(d)(1) of rule XIII of the Rules of the House of Representatives, the Committee finds that the authority for this legislation in Art. I, § 8, cls. 1, 3, and 18 and Art. IV, § 3, cl. 2 of the Constitution of the United States.

XIII. Congressional Accountability Act

H.R. 3987 does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of § 102(b)(3) of Pub. L. No. 104–1.

XIV. Federal Advisory Committee Act Statement

H.R. 3987 does not establish or authorize the establishment of any new advisory committees as that term is defined in the Federal Advisory Committee Act, 5 U.S.C. App. 2.

XV. Statement of No Earmarks

Pursuant to clause 9 of rule XXI, H.R. 3987 does not contain any congressional earmarks, limited tax benefits or limited tariff benefits as defined in subsections (d), (e) or (f) of clause 9 of rule XXI of the Rules of the House.

XVI. Performance Goals and Objectives

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House, the Committee establishes the following performance-related goals and objectives for this legislation:

H.R. 3987 includes provisions to impose additional constraints on the ability of the Administrator of the Small Business Administration to create and revise size standards for small business concerns to ensure transparency and accuracy.

XVII. Changes in Existing Law Made by the Bill, as Reported

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

SMALL BUSINESS ACT

* * * * * * *

[SEC. 3. (a)(1) For the purposes]

SEC. 3. DEFINITIONS.

(a) SMALL BUSINESS CONCERNS.—

(1) IN GENERAL.—For the purposes of this Act, a small-business concern, including but not limited to enterprises that are engaged in the business of production of food and fiber, ranching and raising of livestock, aquaculture, and all other farming and agricultural related industries, shall be deemed to be one which is independently owned and operated and which is not dominant in its field of operation: *Provided,* That notwithstanding any other provision of law, an agricultural enterprise shall be deemed to be a small business concern if it (including its affiliates) has annual receipts not in excess of $750,000.

* * * * * * *

[(3) When establishing]

(3) VARIATION BY INDUSTRY AND CONSIDERATION OF OTHER FACTORS.—When establishing or approving any size standard pursuant to paragraph (2), the Administrator shall ensure that the size standard varies from industry to industry to the extent necessary to reflect the differing characteristics of the various industries and consider other factors deemed to be relevant by the Administrator.

* * * * * * *

(5) ALTERNATIVE SIZE STANDARD.—

(A) IN GENERAL.—The Administrator shall establish an alternative size standard for applicants for business loans under section 7(a) and applicants for development company loans under title V of the Small Business Investment Act of 1958 (15 U.S.C. 695 et seq.), that uses maximum tangible net worth and average net income as an alternative to the use of industry standards.

(B) INTERIM RULE.—Until the date on which the alternative size standard established under subparagraph (A) is in effect, an applicant for a business loan under section 7(a) or an applicant for a development company loan under title V of the Small Business Investment Act of 1958 may be eligible for such a loan if—

(i) the maximum tangible net worth of the applicant is not more than $15,000,000; and

(ii) the average net income after Federal income taxes (excluding any carry-over losses) of the applicant for the 2 full fiscal years before the date of the application is not more than $5,000,000.

(6) COMMON SIZE STANDARDS.—In carrying out this subsection, the Administrator may establish or approve a single size standard for a grouping of four digit North American Industrial Classification codes only if the Administrator makes publicly available, not later than the date on which such size standard is established or approved, a justification demonstrating that such size standard is appropriate for each individual industry classification included in the grouping.

(7) PROPOSED RULE MAKING.—In conducting rulemaking to revise, modify or establish size standards pursuant to this section, the Administrator shall consider, and address, and make publicly available as part of the notice of proposed rule making and notice of final rule each of the following:

(A) a detailed description of the industry for which the new size standard is proposed;

(B) an analysis of the competitive environment for that industry;

(C) the approach the Administrator used to develop the proposed standard including the source of all data used to develop the proposed rulemaking; and

(D) the anticipated effect of the proposed rulemaking on the industry, including the number of concerns not currently considered small that would be considered small under the proposed rulemaking and the number of concerns currently considered small that would be deemed other than small under the proposed rulemaking.

(8) NUMBER OF SIZE STANDARDS.—The Administrator shall not limit the number of size standards it creates pursuant to paragraph (2), and shall assign the appropriate size standard to each North American Industrial Classification System Code.

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