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August 10, 1993

MEMORANDUM

TO: **NPR Policy Group**
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FROM: John S. Hale
Coordinator, Science & Technology Team

SUBJECT: Draft NPR Chapter on OSTP and NSF

Attached is a draft chapter on science policy and administration affecting the Office of Science and Technology Policy and the National Science Foundation for the NPR final report. This chapter is to be completed by Augtust 18, 1993. Therefore, we would appreciate receiving your comments by August 16, 1993 at the above address so that we can incorporate them into the final report.

Please feel free to call me on 632-0150, ext. 159 if you have any questions. Thank you.

Attachment

OFFICE OF SCIENCE AND TECHNOLOGY POLICY

NATIONAL SCIENCE FOUNDATION

AGENCY TEAM REPORT

NATIONAL PERFORMANCE REVIEW

INTERNAL WORKING DOCUMENT--NOT FOR DISTRIBUTION
SCIENCE AND TECHNOLOGY TEAM
August 10, 1993

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Section I

Introduction

INTRODUCTION

Background

Advancement in science and technology is viewed as a key element for national economic success. President Clinton's *Vision of Change for America* makes reference to studies showing that "investments in research and development (R&D) tend to be the strongest and most consistent positive influence on productivity growth."[1] New developments in fields such as telecommunications and information technology are expected to affect the way we work and the way our children learn. New materials and manufacturing processes can make the U.S. more competitive in world markets. Investments in basic science ensure the availability of scientists who can forge new understandings of mechanisms that effect our health and our environment. Determining how best to invest federal research dollars to meet national goals is an important element of federal policy. Delivery of resulting technological advances to business and industry is a major challenge for the Federal Government.

A look at agencies with major responsibilities in science and technology research reveals that there are many issues in common. An exhaustive presentation of those crosscutting issues is beyond the scope of this report. The report, however, does suggest mechanisms for addressing R&D priorities as well as research administration relevant to the wider federal R&D community.

The Office of Science and Technology Policy (OSTP) was created by the National Science and Technology Policy, Organization, and Priorities Act of 1976 to provide advice to the President on issues relating to science and to coordinate federal efforts in science and technology. The Act also established the Federal Coordinating Council for Science, Engineering and Technology (FCCSET). FCCSET is chaired by the Director of OSTP and includes Cabinet members or their deputies from 12 departments, heads of other agencies involved in science and technology, and representatives from the Office of Management and Budget (OMB). It is charged by the legislation with: (1) providing more effective planning and administration for federal science, engineering and technology; (2) identifying research needs; (3) using the resources and facilities of the federal agencies more effectively including eliminating unwarranted duplication; and (4) furthering international cooperation.

Many agencies have significant roles in federal R&D, but the focus and coordination of the federal R&D effort are of particular importance to the NSF with its mandate to strengthen the nation's overall potential in science and engineering. Because of its prominent role in funding university research, an increased investment in the science and engineering research administered by the NSF has been proposed by the administration. NSF has been instrumental in developing streamlined methods for research administration and has been a major participant in efforts to coordinate interagency research activities. Issues to be discussed here emphasize focus and efficiency in research administration and seek to eliminate activities that distract from research efforts.

The National Science Foundation, a relatively small, independent agency, was created by the National Foundation Act of 1950. It funds research and education in most fields of science and engineering through grants, contracts and cooperative agreements to colleges, universities and other institutions across the U.S. Each year, NSF receives approximately 30,000 proposals for new or renewed support for research, graduate fellowships and science and engineering activities and awards approximately 10,000 new awards.

Of NSF's approximately 1,200 staff members, about one-third are Ph.D. scientists, engineers or educators who are familiar with functioning in a technologically sophisticated environment. With a budget of approximately $3 billion, the agency supports research and education in all fields of the natural and social sciences, mathematics and engineering. NSF provides research funding in computers, information science, and the national information infrastructure. It has committed to using technology to improve the effectiveness of its operations and services, and it has very close ties with the university research community.

With the exception of its Directorate for Education and Human Resources (EHR) , NSF is, in general, structured according to academic disciplines. EHR sponsors activities that cross traditional disciplines. NSF staff is assisted by advisors, primarily from the scientific and engineering communities, who assist in review of proposals. However, NSF staff with appropriate expertise always make the final award decision.

NSF is a major participant in FCCSET. FCCSET, with representation from all agencies with significant scientific research activities, coordinates selected interagency research initiatives. NSF participates in all of the current initiatives. NSF also participates in the Federal Demonstration Project (FDP), a group formed by government agencies and universities interested in streamlining research administration.

Issues

Because of the importance of R&D to the nation's progress, using funds allocated for R&D productively is critical. That requires setting up management mechanisms that will focus agencies' effort on important national priorities as well as management systems that will reduce administrative overhead. To enhance policy development and implementation, a national policy council derived from the current FCCSET is proposed. This council not only can facilitate formulation of a coherent national science and technology policy but also provides a mechanism to address important issues as they emerge. Developing and articulating a clear policy to guide R&D activities is a primary component of any move toward quality management.

Making use of technological advances to streamline the management of research is another important aspect of bringing quality systems to the R&D endeavor. The NSF efforts at automating their grant management activities are presented as an example of an effective way to save money and handle program administration more efficiently.

Removing red tape that distracts from research activity is an important way to insure that more research funds are directed to productive research. The FDP has found examples of administrative requirements placed on universities that can be eliminated without compromising financial accountability. A more formal relationship between FDP and the federal government is proposed so that its documented findings can be brought to bear on government regulations. A modification of the Federal Advisory Committee Act requirements for NSF merit review panels is proposed so that NSF is relieved of the cost of advertising meetings that are closed by law.

The issues presented in this report do not exhaust the possibilities for improving management of federal R&D. Rather, along with some examples, they provide for organizational structures that can continue the effort over the long term.

1. Executive Office of the President, Office of Management and Budget, *Vision of Change for America, (Washington, D.C., February, 1993), p 52.*

OFFICE OF SCIENCE AND TECHNOLOGY POLICY

Section II

OSTP
Issue Papers and Recommendations

II. A. Creating a Quality Management Culture

STRENGTHEN COORDINATION OF SCIENCE POLICY

Background

The federal government will spend $76 billion in fiscal 1994 for scientific research and development (R&D). At least a dozen separate federal departments and agencies have significant research initiatives covering basic and applied fields of science and technology. The President and Vice President have repeatedly cited technological innovation as a key to economic growth and the creation of new markets and high-wage jobs. Because scientific research is so essential to these national goals, efficient use of federal resources for R&D is vital. Current organizational structures do not provide for the necessary coordination.

The Office of Science and Technology Policy (OSTP) was created by the National Science and Technology Policy, Organization, and Priorities Act of 1976 to provide advice to the President on issues relating to science and to coordinate federal efforts in science and technology. The Act also established the Federal Coordinating Council for Science, Engineering and Technology (FCCSET). FCCSET is chaired by the Director of OSTP and includes Cabinet members or their deputies from 12 departments, heads of other agencies involved in science and technology, and representatives from the Office of Management and Budget (OMB). It is charged by the legislation with: (1) providing more effective planning and administration for federal science, engineering and technology; (2) identifying research needs; (3) using the resources and facilities of the federal agencies more effectively including eliminating unwarranted duplication; and (4) furthering international cooperation. In the Reorganization Plan #1 of 1977, President Carter abolished FCCSET and reconstituted it by Executive Order 12039 to advise and assist the Director of OSTP.

FCCSET operates through committees, subcommittees and working groups and is currently focusing on six budget initiatives.[1] The initiatives have evolved over time in response to administration priorities, outside interests, and Council interests.

Participation in FCCSET initiatives is voluntary. Agencies that are interested in a particular initiative may commit agency funds to that initiative. The way the funds are used is also ultimately the decision of the participating agency. According to the FCCSET procedures, once an agency commits funds it is not expected to reduce or withdraw them regardless of how appropriations change. However, FCCSET itself has no authority to redirect funds or to withhold funds for any reason. Each initiative includes one or two OMB budget examiners who provide advice, but authority for budget decisions rests with the agency budget examiner. There is agreement among experts in OMB, the General Accounting Office (GAO), and OSTP that FCCSET does not have the teeth to establish priorities, direct policy and participate fully in the budget process.

The need for "one-stop shopping" for federal science and technology policy has been broadly recognized. For example, a report from the National Science Board Commission on the Future of National Science Foundation has as its first recommendation: "The United States should have a stronger and more coherent policy wherein science and engineering can contribute more fully to America's strength."[2] As well, a 1992 report of the Carnegie Commission on Science, Technology, and Government concluded, "With OSTP leadership the Federal Coordinating Council on Science, Engineering, and Technology (FCCSET) should extend its promising efforts in shaping long-term S&T goals involving more than one federal agency and emphasize the articulation of specific long-term goals through a more explicit planning process.[3]

Other evidence of concern about policy coordination comes from the Congress and GAO. Recognition by some members of the Congress that there is inadequate coordination of federal activities in science and technology has led to a proposal for a separate cabinet-level Department of Science, Space, Energy and Technology.[4] GAO, in a May 1993 report, states that the Advanced Research Projects Agency, a principal participant in the High Performance Computing Initiative (a FCCSET initiative), needs to improve dissemination of its research information to the other agencies involved.[5] This finding in conjunction with concern from the Congress, has instigated further investigation by GAO.

In addition to FCCSET, there are two other councils established by legislation to deal with specific aspects of science policy. The National Space Council is currently headed by the Director of OSTP and no longer functions separately. The National Critical Materials Council, whose charge to coordinate matters relating to materials policy and research overlaps with a FCCSET initiative, has had a 1993 appropriation even though its authorization has expired.

The current Director of OSTP is attempting to increase policy coordination through a Science and Technology Deputies Group composed of individuals from each agency who have access to the Secretary and can make commitments for the agency. The members are the points of contact in each agency responsible for implementation of initiatives in science and technology.

Under the current structure, FCCSET does not have the authority to bind agencies to policy decisions or budget allocations.

FCCSET does not currently encompass most of the federal effort in science and technology. The six FCCSET initiatives account for approximately 16 percent of the fiscal 1994 federal R&D budget.

FCCSET has generated an elaborate structure of committees, subcommittees and working groups (three established by legislation). There are 54 named on a list that is still being updated. A review of membership lists in the FCCSET publications shows group sizes ranging from eight to 39 members, with most having between 12 and 20 members. A June 1993 list of the committee and working group meetings already scheduled for the period between June 23 and Christmas contained 76 meetings and certainly more will be scheduled for the latter months.

According to its procedures manual, the process of selecting FCCSET initiatives involves four stages of review by the full FCCSET and three referrals to committee for information or planning.[6]

Despite its complex structure, FCCSET has fostered valuable communication among participants. Coordination and information exchange are occurring around the initiatives. Professional staff have formed subgroups to share technical information. Many of the FCCSET meetings do result in constructive communication and coordination among agency representatives. However, an effective policy council must do more than promote exchange of technical information.

In this time of declining federal resources, it is imperative that goals and priorities for science and technology be well-defined and that available resources be directed to meeting those goals. To achieve the necessary focus, the responsibility for science and technology policy in the Executive Branch must rest in a single organization. The responsibility must be accompanied by the authority to assure that policies are implemented and to work with OMB, OSTP and the federal agencies to develop budgets that reflect those policy initiatives.

Recommendations

Modify the current FCCSET structure and reconstitute the organization as the National Science and Technology Council (NSTC), which should coordinate development and implementation of science and technology policy.

1. **A senior policy council should be constituted and named the National Science and Technology Council. The President and/or the Vice President, Assistant to the President for Science and Technology Policy, Cabinet Secretaries and agency heads from departments and agencies having major roles in either development or use of science and technology, as well as the heads of the National Economic Council, National Security Council, Council of Economic Advisors and OMB would be members.** The NSTC would be charged with assuring that the President's goals are implemented effectively as well as with performing the functions assigned to FCCSET in its enabling legislation. The NSTC would coordinate science and technology policies for all agencies. The group would be chaired by the President or Vice President.

2. **The NSTC must have the authority to initiate Presidential Review Directives and Presidential Decision Directives in order to assure that policy decisions are implemented and to compel participation by all agencies.**

3. **The current S&T Deputies Group would function as the deputies for NSTC and would oversee working groups.**

4. **All current FCCSET standing committees would be dissolved or rechartered to meet current needs.** The NSTC or Deputies Group would establish technical

working groups as needed. The working groups would provide technical information in support of NSTC goals and would develop detailed implementation plans including milestones and metrics for evaluation of progress toward stated goals. Working groups would be composed of senior technical staff from participating agencies. A working group would exist only as long as the NSTC needed its assistance.

5. **Advisory groups representing the private sector would be established to provide information for NSTC deliberations on policy and priorities.** In addition working groups would communicate with appropriate private sector organizations or small technical advisory groups composed of private sector representatives in order to receive input from stakeholders. These advisors would assure that the government used the most current and relevant information in developing its plans.

6. **The Council and the Deputies Group should work closely with OMB in formulating budgets.**

7. **Whenever possible, exchange of information should occur electronically in order to minimize the number of meetings and the exchange of paper.** Initially all members of the Deputies group should be connected to the Internet, a widely available worldwide computer network, or other network that will allow electronic communication.

The proposed policy council should be created immediately by Executive Order. Consistent with the goal of coordinating all scientific R&D in one organization, formal action should be taken to deal with related groups that are no longer needed. Legislation is needed to reassign the functions of the National Space Council, the National Critical Materials Council and the three FCCSET standing committees established by legislation.

Implications

The proposed NSTC does not create a new federal organization. It streamlines the existing structure by combining three councils into one and by giving the remaining council the authority needed to function effectively.

The primary benefit of the proposed council is to focus scarce resources on national priorities which have been agreed upon in open discussion among agencies involved in science and technology. Agencies are likely to receive some benefits from expanded cooperation but will also relinquish some independence as a result of the council's expanded authority. Applying formal evaluation criteria to the collaborative efforts is likely to improve the end products and benefit all participants.

This new organization, composed of people versed in science and technology, provides an excellent opportunity to test the application of information technology to coordination, planning, and review functions. Since no operating procedures will exist, the Council can, from the start, use current technology to reduce meetings, reports and paper exchange. Over time, a strong representative group can also make great progress toward developing standard terminology and formats for shared databases pertaining to federal R&D activities.

Fiscal Impact

Because this proposal makes use of existing agency and OSTP personnel, there would be no estimable fiscal impact. In the long run, there is potential to use federal R&D funds more efficiently through focusing agencies' efforts on well-defined goals.

A less complex operating structure should reduce operating costs slightly. For example, assuming that each of the 76 meetings cited earlier takes 3 hours including travel and preparation time and that each one involves 15 people, six months of FCCSET meetings consume 3,420 hours of agency personnel's time. Some of these hours spent in meetings might become available for other activities in support of interagency science and technology efforts.

Endnotes

1.The six FCCSET initiatives (program areas) for fiscal 1994 are (1) Advanced Manufacturing Technology, (2) High Performance Computing and Communications, (3) U. S. Global Change Research, (4) Advanced Materials and Processing, (5) Biotechnology Research and (6) Science Mathematics, Engineering and Technology Education.

2. National Science Board Commission on the Future of the National Science Foundation, *A Foundation for the 21st Century: A Progressive Framework for the National Science Foundation*, (Washington, D.C., November 20, 1992), p.4.

3. Carnegie Commission on Science, Technology, and Government, *Enabling the Future: Linking Science and Technology to Societal Goals*, (New York, N.Y., September 1992), p. 16.

4.U.S. Congress, House, *A Bill to Establish a Department of Science, Space, Energy, and Technology,* 103rd Cong., 1st sess., 1993, H.R. 1300.

5. U. S. General Accounting Office, *High Performance Computing Advanced Research Projects Agency Should Do More to Foster Program Goals*, (Washington, D.C., May 1993)

6. Federal Coordinating Council for Science Engineering and Technology, *Policies and Procedures Manual,* (Washington, D.C.: Executive Office of the President, Office of Science and Technology Policy, October 30, 1992), pp 11-13.

NATIONAL SCIENCE FOUNDATION

Section III

NSF
Issue Papers and Recommendations

III. A. Shifting From Red Tape to Results

USE THE FEDERAL DEMONSTRATION PROJECT TO INCREASE RESEARCH PRODUCTIVITY

Background

In the mid-1980s, the nine campuses of the Florida State University System plus the University of Miami joined with five federal agencies (National Science Foundation, Department of Energy, National Institutes of Health, U.S. Department of Agriculture and the Office of Naval Research) to experiment with reducing administrative overhead on research grants. They wanted to simplify administrative procedures without compromising financial accountability so that Principal Investigators (PIs) would have more time for research activities. The Florida demonstration was so successful that in 1988, the demonstration was broadened to 50 universities and ten federal agencies as the Federal Demonstration Project (FDP). The participating universities were selected by a competitive process managed by the National Academy of Sciences.

The FDP has developed from the cooperative effort of government and researchers. Interested agencies and universities have joined together to find ways to make grant award and administration work better. The FDP has no formal status and no operating budget. The FDP is organized into a Committee of the Whole which meets once a year to exchange information and set the future agenda. A steering committee that meets four times a year provides coordination. Several task groups design demonstrations. A Federal Interagency Assessment Committee (IAC) created by the Office of Management and Budget (OMB) oversees the project. The Government-University-Industry Research Roundtable of the National Academies of Science and Engineering and Institute of Medicine serves as a neutral convener for discussion of issues relating to FDP.[1] FDP demonstrations include formal evaluation that allow OMB to determine the value of recommended changes. The FDP is planning a one-day meeting in the Fall of 1993 to identify critical issues of research administration to be addressed in the next several years.

Four demonstrations were included in the Florida phase. The first demonstration gave institutions the authority to manage project budgets without getting prior approval for rebudgeting. The second demonstration allowed grantees to incur costs at their own risk up to 90 days before formal issuance of the grant without prior approval. A third allowed no-cost extensions of up to 12 months, and the fourth and final demonstration allowed grantees to carry forward unobligated grant funds to the next funding period.

On the basis of the experience in Florida, the Office of Management and Budget (OMB) authorized all federal agencies, on an optional basis, to use the streamlined procedures. The impact of the four experimental procedures also was formally evaluated in 28 universities in addition to those in Florida.[2] Response from 2,501 PIs indicated that the streamlined procedures saved an average of 5.2 days per year. That represented 38.5 person years of effort for the 2,501 investigators. Eighty-nine percent of that time was reinvested in scholarly activity and 73 percent in research. The study's authors assert that if these findings were extrapolated to all federally funded PIs, this reinvestment in research as a result of using the simplified procedures would increase sixfold.

The next demonstration evaluated the effectiveness of equipment screening regulations. OMB Circular No. A-110 requires procurement procedures "to assure the avoidance of purchasing unnecessary or duplicative items."[3] Subsequent A-110 audits prescribed a two-level screening process based on cost of equipment as well as a requirement for centralized inventories and for proof of screening.

The FDP studied the value of the formal equipment screening process for meeting the objective stated in A-110.[4] In a one year period, the 31 participating institutions performed over 4,900 separate screens involving almost $83 million worth of equipment. Two screens resulted in matches, avoiding the purchase of $18,881 worth of equipment. The study concluded that the cost of the time spent by PIs and administrators (estimated at $195,413) was more than ten times the savings accrued as a result of equipment screening. That estimate did not include the cost of developing and maintaining the screening systems. The study also found that PIs, independent of screening requirements, used university systems and informal networking to find opportunities to share equipment when it benefited their research and that such inquiries were made before a procurement request was ever submitted for screening.

The Commonwealth of Virginia performed a study of administrative decentralization in higher education.[5] The purpose of the study was to identify administrative functions that could be delegated to the universities. Universities that met standards for financial management and management efficiency were relieved from following selected procedures. Given a positive incentive, all universities in the state improved their financial management and all but one qualified. An additional, unexpected success was the qualification of the two major teaching hospitals. In response to the incentives, they brought very complex financial systems into compliance with the standards.

The FDP has been able to recommend regulatory changes that simplify administration of research grants and allow university researchers to spend more of their time on productive research. There is no set place in the federal government to receive FDP recommendations although OMB has modified Circular A-21 and is in the process of modifying A-110 as a result of the initial demonstrations. This process of developing procedures that simplify research administration without reducing accountability should be continued.

Recommendations

1. The Federal Demonstration Project in cooperation with the Office of Management and Budget should define a systematic means to select participants and to introduce those procedures that are shown to be effective into federal regulations.

A formal certification process for including organizations in the FDP should be established. Certification criteria should be based on official audits of: 1) university financial statements and 2) internal controls based on audits conducted in accordance with OMB Circular A-133 and cognizant audit agencies as necessary. The focus should be on operating procedures that prevent misuse of funds. Those universities whose procedures provide a reasonable assurance of accountability and control of financial expenditures for federal activities would be allowed to participate. Periodic recertification would be required. The process of applying for certification should be formalized and perpetuated in OMB Circular A-110.

The Federal Interagency Assessment Committee should define the certification criteria. The criteria should be included in OMB Circular A-110. Examples of standards are an unqualified audit opinion from the designated auditor and no significant audit deficiencies including compliance findings to the university as a whole and relative to federally assisted activities.

The current structure of the FDP should be used to approve and evaluate demonstrations and to present results to OMB. A central point within OMB should be designated to receive suggestions.

The FDP should be used as a model for testing new procedures. The FDP is currently serving as an effective interagency reinvention lab for administration of research grants. It is a model for an approach that could be used for testing and evaluating other changes to government procedures. Interested parties organize to suggest changes and to implement them on a limited basis so that risk can be controlled and results studied. The new procedures are subjected to a formal evaluation and implemented more widely only if they prove beneficial.

Implications

FDP provides a model for simplifying administrative procedures without eliminating accountability. Because administrative costs are reduced, more federal grant money can be spent on research. The certification process will help assure qualified participants and the IAC provides the necessary oversight.

Fiscal Impact

Using streamlined procedures allows the government to buy research instead of paperwork with its grant money. Implementation of the procedures in the four initial demonstrations has been estimated to add 158 years of research activity per year at no cost.[6]

Endnotes

1. Research Roundtable, *What is the Federal Demonstration Project?* (Washington, D.C., August 1991).

2. Productivity/Assessment Task Group of the Federal Demonstration Project (PATG), *The Impact of the Use of Expanded Authorities within the Federal Demonstration Project* (February 1991).

3. Office of Management and Budget, *Circular No. A-110 Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Nonprofit Organizations* (Washington, 1976) attachment O, paragraph 3.c.

4. Federal Demonstration Project, *Report of Task Group Five on Equipment Screening Study,* (Washington, D.C., December 1991).

5.Finley, Donald J., *Administrative Decentralization in Higher Education, (*Commonwealth of Virginia, May 1988)

6.*The Impact of the Use of Expanded Authorities,* p. 3.

MODIFY FEDERAL ADVISORY COMMITTEE ACT REQUIREMENTS FOR MERIT REVIEW PANELS

Background

Each year, the National Science Foundation receives about 30,000 proposals requesting new or renewed support for research, graduate fellowships and science and engineering activity. These proposals are reviewed by merit review panels and the best are chosen for funding. The NSF model for merit review has been validated in numerous studies and reports, and aspects of its process for ensuring objective reviews has been both praised and emulated.[1] [2] NSF's merit review panels, which exist only to review grant proposals, are currently subject to procedural and reporting requirements specified in the Federal Advisory Committee Act (FACA).[3] The value of applying FACA to merit review panels has been questioned.

FACA was enacted in 1972 to establish a system to govern the creation and operation of advisory committees in the executive branch. The bill establishes procedures to review the need for committees periodically. It attempts to limit the number of committees by assuring that only essential committees are created and that they are terminated when their task has been completed. FACA also requires that Congress and the public be kept informed of advisory committee activities and that meetings be open unless exempted by other legislation. NSF panel meetings are exempt from the open meeting requirement under the Sunshine in Government Act but the merit review panels themselves are subject to all other requirements of FACA.

FACA requires that agencies maintain systematic information on the nature, function, and operation of each advisory committee. A committee cannot meet or take action until a committee charter has been filed with the agency head and with the standing committees of the House and Senate which have legislative jurisdiction of the agency. FACA lists nine items to be included in the charter, for example: scope and objectives, description of duties, term, operating costs, and number and frequency of meetings. Obtaining a charter takes 60 to 90 days and panels must be rechartered every two years. A copy of the charter and of any reports that are prepared go to the Library of Congress.

Meetings must be announced in the *Federal Register*. Further, each of the panels must be addressed in an annual report by the agency to GSA which is used for the President's annual report to Congress on advisory committee activities. The annual report details number of meetings, costs, members, and a justification for the panel's continued existence. Lists of all persons serving during the fiscal year are included in the report.

Because NSF's merit review panels meet the definition of an advisory committee under FACA, the number of advisory committees NSF must track under FACA is nearly tripled; 66 of the 95 NSF advisory committees are for merit review. After advisory committees are reduced in accord with a recent Executive Order, at least 85 percent of NSF's advisory committees will be merit review panels. This results in many hours of effort that neither enhance the grant review process nor result in better use of advisory committees by NSF. As well, meeting the requirement to announce meetings in the *Federal Register* costs approximately $60 thousand per year.

It can be argued that removing FACA requirements from merit review panels will further decrease access to a process that has already been criticized as too secretive. However, FACA recognizes the exemption of NSF merit review panels from the open meeting requirement to protect the privacy of proposers and their confidential business. The minutes that are prepared and made available on request are cursory for the same reason. Reviewers for individual proposals also cannot be revealed but copies of the reviews with reviewer's name removed and summaries of panel deliberations are automatically mailed to the applicant when review is complete. Further the merit review panels exist solely for the purpose of reviewing proposals and convene only for that purpose. Use of merit review panels is a basic element of NSF operations and information about their use is readily available in NSF publications including the grant application kit.

In 1991, GAO studied adherence to FACA in peer review by six agencies.[4] Ninety percent of the 469 peer review panels in the six agencies were chartered, including all NSF panels. Agencies that did not charter argued that the ad hoc nature of the panels, which often were convened quickly and met only once, made it impractical and that these panels were exempt because they did not provide consensus advice as is stated in the FACA definition. GAO did not evaluate the specific committees but did state that there was benefit in announcing the existence of panels and when and where they meet. In the case of NSF, the method of evaluation is part of the grant announcements and information about panels is easily obtained.

Recommendation

Congress should modify some provisions of the Federal Advisory Committee Act for NSF merit review panels. The legislative amendments will apply to those committees that are established to provide peer review for technical research proposals and projects. To avoid circumventing the original intent of the legislation, only those committees whose deliberations are already exempt from open meeting requirements would be eligible. Merit review panelists would continue to be subject to all ethics regulations.

Accordingly, Section 4(b) of FACA might be amended to add a new exemption as follows:

"(3) any committee or panel of experts whose sole purpose is to provide expertise and evaluation for use by an agency in selecting among competing applications or proposals for research grants, fellowships, or other assistance awards."

An alternative approach is to continue to cover panels but modify the procedural requirements for highly technical grant review panels that meet only in closed session. Examples of procedural changes are: 1) substituting a requirement to publicize meeting schedules, panel membership and other relevant information not excluded by the Sunshine in Government Act for the requirements for announcements in the Federal Register and 2) lengthening the life of a charter so panels are chartered less frequently.

Implications

Any change in legislation that can be construed as an attempt to hide information from the Congress or the public is sensitive. The changes recommended here are not for the purpose of determining what can be made public: that has been done in legislation and will continue to be litigated. The primary purpose of the proposed exemption of NSF merit review panels from certain FACA requirements is to avoid the cost and burden of publishing numerous announcements of closed meetings, information of questionable value that interested researchers can easily obtain directly from NSF. Further, NSF could at nominal cost post a meeting schedule on its Internet network service which is far more accessible to its research community than the *Federal Register*.

The Congress is concerned as well with the composition and the cost of merit review panels. Again, NSF publishes such information in annual reports and budget documents. If that were not satisfactory, maintaining the requirement for an annual report would cancel only a small part of the savings. As well, OMB as part of its budget reviews could assure that NSF was properly managing its grant review panels. The key is to carefully define the information that Congress and others need and assure that it is made available efficiently.

A stated goal of NPR is to give managers the authority to determine how to fulfill agency requirements. This is an example where agency management can be charged with and evaluated on keeping the scientific community and others informed of the merit review process. Methods for disseminating information have changed since FACA was enacted in 1972. NSF should be given the freedom to incorporate the processing and dissemination of merit review panel information with its other information processing activities.

Fiscal Impact

Cost savings would accrue from reduced reporting efforts, particularly by removing the requirement to publish notices in the *Federal Register*. During fiscal year 1992, NSF announced approximately 470 meetings devoted to merit review in the *Federal Register*. In addition to meeting notices, FACA requires that a notice announcing the establishment and renewal of all committees be announced. Each meeting notice costs approximately $130, in addition to the staff time required for preparation. In fiscal year 1992 these costs amounted to over $60,000, plus staff time.

FACA requires agencies to have a Committee Management Officer. The majority of that person's effort is in meeting FACA requirements for merit review panels. Additionally, the officer has clerical assistance and assistance from the program areas. If FACA requirements for merit panels were eliminated the cost of one FTE ($75,000) could be eliminated.

Although the savings in all agencies has not been studied, it is worth noting that NSF had only 15 percent of the panels GAO studied and that in fiscal year 1992, grant review committees accounted for 22 percent of all federal advisory committees.[5] Thus, there is potential for greater savings throughout the government.

Fiscal Impact Table

Net Savings/Changes to Baseline

In Millions of Dollars

	1994	1995	1996	1997	1998	Total
Budget Authority	0.135	0.135	0.135	0.135	0.135	0.675
Outlay	0.135	0.135	0.135	0.135	0.135	0.675
Change in FTEs	(1)	(1)	(1)	(1)	(1)	

Endnotes

1.McGarity, Thomas O., *Peer Review in Awarding Discretionary Grants in the Arts and Sciences* (Administrative Conference of the U.S, December 1992).

2. National Science Foundation, *Report of the Merit Review Task Force* (Washington, D.C., August 1990)

3. *Federal Advisory Committee Act,* Public Law 92-463 (1972).

4.General Accounting Office, *Peer Review: Compliance with Privacy Act and Federal Advisory Committee Act,* GAO/GGD 91-48 (Washington, D.C. , April 1991)

5. *Twenty First Annual Report of the President on Federal Advisory Committees: Fiscal Year 1992* (Washington, D.C. 1993), p. 2.

III. B. Creating a Quality Management Culture

CONTINUE AUTOMATION OF NSF RESEARCH SUPPORT FUNCTIONS AND SHARE RESULTS WITH OTHER AGENCIES

Background

In the last several years, NSF has re-engineered many of its business practices in order to handle an increase in workload without a concurrent increase in staff. Five years ago, NSF's interactions with the research community were paper-intensive. NSF would mail thousands of copies of program announcements to researchers throughout the country. Research institutions would respond with ten to fifteen copies of over 30,000 proposals that averaged over 50 pages. Appropriate peer reviewers were selected by NSF scientific staff and eight to twelve copies of the proposal would be sent to the reviewers. The peer reviewers would mail back their written review of the proposal. Copies of the reviews of proposal would be made for panel reviewers. After a funding decision is made an award letter is sent to the research institution and to the principal investigator. In short, NSF was beginning to drown in its paper processes.

The agency committed itself to implementing new technological strategies to attack the paperwork problem and reduce workload burdens for the NSF staff and the research community. NSF initiated a research program to address the technological and behavioral issues involved in the design and implementation of a totally electronic proposal, review and award process. In 1987, this program, known as EXPRES (Experimental Research in Electronic Submission), began as a cooperative agreement with university and industry partners to explore the research issues involved in implementing a full-scale interoperable system. The goal was to build on the diversity of technology in the university environment rather than to mandate limited standards for interacting with the NSF.

EXPRES researchers discovered that major breakthroughs in technology related to the exchange of compound documents across dissimilar hardware and software platforms were necessary before the basic concepts of EXPRES could be achieved. In 1987 the technology was not mature enough to meet the objectives of the research program. Additionally, the university information technology infrastructure was uneven; the variance of quality even on one campus was significant. The EXPRES program, however, did validate the NSF goals of electronic document exchange. Although full-scale implementation of NSF's concept was not possible, NSF committed to the pursuit of achievable components of the overall program. The following examples illustrate some of the progress the Foundation has made in these areas:

1) *Automation of external information dissemination.* Several years ago, NSF implemented the Scientific and Technical Information System (STIS)[1] to provide information about NSF and its research programs to its customers. This system, which is accessible in a variety of ways, including Internet access and dial-in access, has grown over the years. Today, there are over two thousand requests for information each day across the U.S. People in over 60 countries have obtained information from the STIS system. The system now provides immediate access to all NSF program announcements, NSF guidelines for the submission of proposals, information about the research being performed by NSF grantees, personnel vacancy announcements, and numerous informational publications.

2) *Standardization of proposal package.* In coordination with other research agencies, NSF has identified data elements commonly required by each agency and has developed proposal submission standards in a package that may be used by all research institutions to submit proposals. This package is available electronically and is intended to facilitate electronic proposal submission.[2] [3]

3) *Electronic receipt of proposal reviews.* After careful consideration and coordination with the research community, NSF allows reviewers to send their reviews to NSF by electronic mail. Several technical and legal issues needed to be addressed and resolved, such as the question of electronic signatures. With the cooperation of the research community, many proposal reviews are now received electronically.

4) *Electronic transmission and receipt of financial information.* Beginning in 1992, NSF implemented a program to electronically mail Federal Cash Transaction Reports to many of the major research institutions receiving NSF funding. This process greatly facilitates the institution's ability to account for expenditures made under NSF grants and expedites posting to the NSF financial accounting system.

5) *Significant reduction of internal paper processes.* While the agency still receives

much of its external correspondence by paper, the agency has sharply reduced the majority of paper intensive processes that existed five years ago. This was accomplished with state-of-the-art information systems to support mission requirements, the use of bulletin boards and electronic mail to support internal communications requirements, and the re-engineering of proposal processing to make them suitable for automation.

A sign of the success of these initiatives is the increased efficiency in the work processes of the agency. In the last ten years, the number of proposals received by the agency has more than doubled and the budget for science, engineering and education research has tripled. While this represents a significant increase in workload and accountability, the staffing at NSF has remained virtually constant. The re-engineering of business practices using information systems is credited with NSF's ability to do more with less.

NSF continues to re-engineer. However, its primary "production" process, programmatic reviews of unsolicited proposals, is still too paper intensive, and inflexible with regard to the way information is exchanged among proposers, reviewers, NSF staff, and the systems which support their work. Pilot studies testing new processes based on empowering professional staff with an advanced information technology are needed. For full value, a major study of system re-engineering to explore ways to tie together processes, program design, proposal acquisition, and review, selection decision making and award administration will be required. If the workload continues to increase at the current rate, increasing efficiency through automation will be the only way to handle it.

Recommendations

1. NSF should continue its efforts to implement advanced information technology in the proposal submission, review, award, and information dissemination process. It should continue, as it has done with STIS, to make use of commonly available low-cost technologies. Advances in commercial word processing, forms applications and mail-enabled applications will provide many of the tools needed to prepare and submit grant applications electronically and to distribute them for review and comment. Public domain search and retrieval software, like that used in STIS, is continuing to improve and to be adopted by university researchers. NSF already has responsibility for much of the work in development of the high-speed network that will be needed. Because of its responsibility in the area of computer science, NSF will continue to stay abreast of industry advances in encryption, network security and digital signature standards. These are necessary for widespread acceptance of electronic grant processing. Researchers must be assured that the technology will protect their proposals against unauthorized access and electronic theft, and universities must be confident that proposals cannot be submitted without proper authorization by designated officials.

2. A formal means for NSF to share developments with other research agencies should be defined. NSF's achievements in automation should be shared more widely with other agencies. Because of its expertise and experience, in consultation with the Office of Science and Technology Policy, NSF should be designated as the lead agency for automation of grants processing. NSF should use interagency coordinating groups such as the Working Group on Government Information Infrastructure suggested in the Information Technology report to interact and form alliances with agencies who have similar needs. In addition, it should use the informal contacts forged over the years on other cooperative efforts to identify agencies who could both contribute and benefit from participation in collaborative efforts.

Through the lead agency mechanism, NSF could be identified as a test-bed for projects that will demonstrate the efficiencies that can be realized through full-scale utilization of information technology in grant-making agencies. These pilot projects could focus on all aspects of the process from proposal receipt, review and award, to financial management and dissemination of research results.

3. NSF should be able to compete for funds to accelerate automation of grants processing. The NPR Information Technology report has proposed that a government-wide "venture capital" fund be available to federal agencies for innovative research and/or that agencies be allowed to keep some of the funds saved as a result of reengineering their business processes. If these suggestions are enacted, NSF should seek such "venture capital" to accelerate its efforts. NSF should also explore the possibility of entering into Interagency Agreements with other agencies that might benefit from its work. Cost of development could be shared and more funding would be available to NSF for its development efforts.

Implications

Considerable savings in materials, mailing and storage can be realized by moving to paperless grant processing and information dissemination. However, the government cannot set up a system that would have the effect of excluding any potential user. Therefore, NSF must make provision for those universities who do not have the latest technology available. They must also be sensitive to the various groups within the university community who participate in grant preparation. Whereas scientific researchers may have the necessary hardware and software, the administrative side of the university which must approve budgets and prepare the institutional sections of the proposal may not.

NSF must balance the need to serve all with the need to take advantage of the best technology. With rapidly changing technology, using the least common denominator means building in obsolescence. NSF's approach in STIS was to provide several alternative methods. Other new systems must, like STIS, attempt to achieve the advantages of the most advanced approach while making allowance for those who cannot afford to acquire the latest.

The concern for security cannot be ignored. Stories of computer fraud and break-ins are becoming routine. Advances in data encryption and network security will alleviate some concern. Widespread acceptance of electronic processing may not occur until security improvements are available.

Universities may have to change their internal processing so that the electronic grant proposals can flow through their offices and be properly signed and approved before submission. The need for change within the university may be the most difficult barrier to automating grant processing.

Whereas, there are economies for the government in developing a single method for processing all grant proposals and for the university in processing all grants the same way, all agencies may not be satisfied with a generic grant proposal kit. Several research offices joined with NSF in developing their current kit but at least one preferred to develop a kit to meet its own unique requirements.

Fiscal Impact

While cost savings are difficult to quantify, in the case of the STIS system cited above, savings in postage are amounting to as much as $1 million per year in addition to the cost of preparing thousands of mailings.

After full implementation, the electronic receipt and review of proposals could result in savings of $1 million or more annually. Currently approximately $1.2 million is spent to mail 10 copies of the 30 thousand proposals that are sent out to reviewers. Some initial investment to purchase equipment may be required over and above NSF's current plans for spending in "Salaries and Expenses."

Savings will also accrue to the universities who collectively spend a minimum of $1.2 million to mail proposals to NSF.

These economies, combined with the introduction of information technologies in the process for dissemination and utilization of research results would yield substantial benefit to the Government and the research community of the United States. As proposal volumes increase over the next decade as they have in the past, only intensive use of information technology will permit NSF and other agencies to maintain control over rapidly expanding program administrative costs.

Fiscal Impact Table

Net Savings/Changes to Baseline
In Millions of Dollars

	1994	1995	1996	1997	1998	Total
Budget Authority	0.0	0.25	0.50	0.75	1.0	2.5
Outlay	0.0	0.25	0.50	0.75	1.0	2.5

Endnotes

1.National Science Foundation, *STIS User's Guide,* NSF 91-19(rev.), version 2.1(Washington, D.C., September,1992)

2.National Science Foundation, *Grants for Research and Education in Science and Engineering: A Proposal Guide and Forms Kit*, Draft, June 5,1993, Appendix H

3.National Science Foundation, "The NSF Electronic Proposal Submission Project", Draft, May 5,1993.

Section IV

Agency Reinvention Activities

NATIONAL SCIENCE FOUNDATION REINVENTION LABORATORY (LAB)

Getting Started and Motivating Participation

The National Science Foundation (NSF) is a small, sharply focused agency with intense interaction with the public it serves--the research and education community and the general public. It has direct communication with the academic community through temporary visiting "rotators", external advisory committees and peer reviews. In addition, the NSF has a history of partnership with industry and is at the core of federal enterprises of computing and networking research and applications programs. Thus, the NSF proposed to serve as a model agency and as a reinvention lab.

Reinvention Lab

In response to the Vice President's invitation to collaborate on reinventing government, six employees have been designated to lead the reinvention effort within the NSF. This group coordinated the development of the issues for submission to the NPR team and recommended using the NSF as a reinvention lab. Using the NSF as the reinvention lab will enable the agency to accelerate its present innovation activities in a staged fashion within and across organizational units. This strategy already has yielded: (1) widespread adoption of electronic interaction in and outside of the agency; (2) an advanced computer based information infrastructure; and (3) worldwide network communications accessible on every desk.

Looking Ahead

The NSF requires only the full authority to employ its resources, including program resources in partnership with the research and education communities, to expand sharply its nascent innovations: (1) the electronic commerce, such as proposal submission and review, financial transaction, and networked information services; (2) virtual workplace (remote computer-based office operations and virtual programs across the NSF and other agencies); (3) virtual meetings such as teleconferencing; and (4) virtual laboratories (collaboratories and metacenters).

Section V

Fiscal Impact Summary

OFFICE OF SCIENCE AND TECHNOLOGY POLICY
& NATIONAL SCIENCE FOUNDATION
FISCAL IMPLICATIONS SUMMARY

CHANGE IN BUDGET AUTHORITY
Numbers in Millions

Ch. Ref.	Recommendation	Fiscal Year 1994	1995	1996	1997	1998	1999	CUM	Change in FTEs
OSTP	Strengthen Coordination of Science Policy	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0		
NSF 1	Federal Demonstration Project	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	
NSF 2	Modify Federal Advisory Committee Act	$0.0	$0.1	$0.1	$0.1	$0.2	$0.2	$0.7	(1.0)
NSF 3	Automation of NSF Research Support Functions	$0.0	$0.3	$0.5	$0.8	$1.0	$1.0	$3.6	
	Total, OSTP & NSF	$0.0	$0.4	$0.6	$0.9	$1.2	$1.2	$4.3	

CHANGE IN OUTLAYS
Numbers in Millions

Ch. Ref.	Recommendation	Fiscal Year 1994	1995	1996	1997	1998	1999	CUM	Change in FTEs
		$0.0							
OSTP	Strengthen Coordination of Science Policy	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0		
NSF 1	Federal Demonstration Project	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	
NSF 2	Modify Federal Advisory Committee Act	$0.0	$0.1	$0.1	$0.1	$0.2	$0.2	$0.7	(1.0)
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	Total, OSTP & NSF	$0.0	$0.4	$0.6	$0.9	$1.2	$1.2	$4.3	

DRAFT--INTERNAL WORKING DOCUMENT

NATIONAL PERFORMANCE REVIEW
AGENCY TEAMS
ISSUE DECISION PACKAGE

TEAM: Science & Technology

Date: August 3, 1993

Issue No.	Issue Title	5-Year Impact (Million $)	NPR Team Position	Agency Position	Action from Tollgate 4 Meeting
1	Strengthen Coordination of Science Policy	$0	The federal government will spend about $76 billion in fiscal year 1994 for scientific research and development. At least a dozen federal agencies conduct significant research that can have a major affect on the U.S. economy. The President's ' declared technology initiative has stated that the Administration will strengthen the Federal Coordinating Council on Science, Engineering and Technology (FCCSET) to improve coordination of these many efforts. It is proposed to reconstitute FCCSET as the National Science and Technology Council (NSTC) -- strengthening FCCSET, absorbing duties of two other science councils, and reducing the large number of FCCSET committees.	The Office of Science & Technology Policy (OSTP) concurs. Other agencies with major R&D activities may present a range of views -- some opposing any efforts to influence their programs via this strengthened instrument for coordinating science. White House domestic policy staff believe this charter resides to some extent in the National Economic Council. (NEC would be a member of the NSTC.)	
2	Use the Federal Demonstration Project to Increase Research Productivity	$0	In the mid-1980's a pilot undertaking began that would simplify the administrative procedures needed on research grants, so that the Principal Investigators could devote more time to actual research. This Federal Demonstration Project (FDP) has proved successful. Procedures from the original demonstration have been incorporated into Circular A-110. We recommend that formal procedures be established for increasing participation and developing new demonstrations. FDP should be used further as a model for testing new, bureacracy-reducing procedures.	NSF and OMB concur.	

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TEAM: Science & Technology

Date: August 3, 1993

Issue No.	Issue Title	5-Year Impact (Million $)	NPR Team Position	Agency Position	Action from Tollgate 4 Meeting
3	Modify Federal Advisory Committee Act Requirements for Merit Review Panels	$0.68	The Federal Advisory Committee Act (FACA) establishes procedures to review the need for advisory committees; to keep the Congress informed on committee activities; to keep meetings open where possible. By law, however, NSF panels to review grant proposals are exempt from the open meeting requirement. NSF receives about 30,000 such grant proposals requiring panel review each year. Congress should modify some provisions of FACA to exempt such panels whose sole purpose is to provide expertise and evaluation used in selecting among competing grants proposals. This or similar alternatives would remove an extensive bureaucratic burden, including costs for Federal Register announcements of meetings closed by law anyway.	NSF concurs.	
4	Continue Automation of NSF Research Support Functions and Share Results With Other Agencies	$2.50	In the last several years, NSF has re-engineered many of its business practices in order to handle an increased workload with a relatively small staff. Most of these interactions with the research community have been paper-intensive -- including hundreds of thousands of pages of grants proposals. NSF has now undertaken new efforts to automate the submission, review and eventual reporting of results for these research grants. NSF should continued these developments; establish in coordination with OSTP formal means to share	NSF concurs. Some other agencies, including the National Institutes of Health and the National Technical Information Service, may wish to take an equally active role.	

NATIONAL PERFORMANCE REVIEW
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Issue No.	Issue Title	5-Year Impact (Million $)	NPR Team Position	Agency Position	Action from Tollgate 4 Meeting
			these developments with other agencies; and seek "venture capital" (as proposed in the NPR information technology report) to support these efforts.		

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Date: August 3, 1993

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			these developments with other agencies; and seek "venture capital" (as proposed in the NPR information technology report) to support these efforts.		

Clinton Presidential Records
Digital Records Marker

This is not a presidential record. This is used as an administrative marker by the William J. Clinton Presidential Library Staff.

This marker identifies the place of a tabbed divider. Given our digitization capabilities, we are sometimes unable to adequately scan such dividers. The title from the original document is indicated below.

Divider Title: **SBA**

SMALL BUSINESS ADMINISTRATION FACT SHEET

The Small Business Administration (SBA) was established as an independent agency of the federal government in 1953 to provide asistance to the nation's small businesses. The agency employs approximately 4,000 people (excluding disaster personnel) with a fiscal year 1993 budget of approximately $760 million.

Access To Credit. The agency's primary role is as a lender of last resort for the nation's small businesses. With a total loan portfolio exceeding $20 billion, SBA's credit programs have provided some relief for borrowers unable to obtain loans without a federal guaranty. Almost 95 percent of all business credit extended through the SBA is provided in the form of loan guarantees. SBA administers a number of small direct loan programs to assist businesses owned by handicapped persons, veterans, minorities and other disadvantaged individuals. A new microloan program was established in 1992 to provide very small loans (averaging $9,700) up to $25,000 to individuals starting or expanding businesses.

Advocacy. The agency's Office of Advocacy serves as an advocate for the nation's small business and will play a key role in preparing for and coordinating the 1994 White House Conference on Small Business.

Disaster Relief. SBA's disaster loan programs provides direct loans to homeowners, renters and businesses to repair or replace damages resulting from physical disasters. A small number of economic injury loans are provided to small businesses for working capital to assist them through the recovery period.

Management and Technical Assistance. Business Development programs at SBA provide a combination of managerial and technical assistance to present and prospective business owners. Much of the agency's business development activities are provided through the Small Business Development Centers loacted in every state.

Minority Assistance. Minority small business assistance programs provide contractural, financial, technical and management assistance necessary to promote business development of small businesses owned by socially and economically disadvantaged individuals.

Procurement Assistance. Procurement assistance programs ensure that small businesses receive a fair share of government procurement and sales. SBA also administers the Certificate of Competency (COC) program which certifies the capibility of a small firm to perform a federal contract and it provides grants to states for tree planting.

Other Assistance. SBA also provides guarantees of payment and performance bonds for small contractors, promotes international trade, promotes the expansion of businesses owned by women, veterans and natove americans and administers the Small Business Innovation Research (SBIR) program which requires federal agencies to set-aside a small portion of their extramural research and development budgets for contracts with small businesses.

NATIONAL PERFORMANCE REVIEW
AGENCY TEAMS
ISSUE DECISION PACKAGE

TEAM: SMALL BUSINESS ADMINISTRATION

Date:

Issue No.	Issue Title	5-Year Impact (Million $)	NPR Team Position	Agency Position	Action from Tollgate 4 Meeting
1	Allow Judicial Review of the Regulatory Flexibility Act	$0	Rec 1. There should be judicial review of agency determinations under the Regulatory Flexibility Act of 1980.	Agency Concurs	
			Rec 2. Presidential Executive Order requiring SBA to issue governmentwide guidance for complying with the analytical requirements of RFA.	Agency Concurs	
2	Reinvent Section 8(A) Program	0	To adopt all Recommendations	Agency Originated Issue Paper	
3	Increase Small Business Loans-Adjust Review Standards	0	Rec 1. Presidential Executive Order to revise the examination guidelines of financial institutions by banking regulators so that all institutional loans may be placed in a single pool for review.	Agency Concurs	
			Rec 2. The President should direct the Treasury to require that banks' capital reserve rates for government securities be increased to 6% over a two-year period.	Agency Concurs	
4	Change Microloan Program to Increase Loans for Small Business	0.0	Rec 1. Congress should amend the Small Business Act to give SBA authority to provide 100% loan guarantees to selected SBA intermediaries.	Agency Concurs	
5	Establish User Fees for SBA Services	68	Rec 1. Congress should give SBA the authority to establish user fees for SBDC counseling services at $15.00/hour.	Agency Concurs	
6	Distribute SBA Staff Based on Administrative Efficiency and Workload	0	Rec 1. President should issue a memorandum to the SBA Administrator requesting that SBA staff be allocated on the principles of adminstrative efficiency and workload	Agency Concurs	
7	Add a question of firm size to future economic surveys	0	Rec 1. The President should issue an Executive Order that economic surveys of business should include a question on company size.	Agency Concurs	
			Rec 2. The Executive Order should also provide enforcement during the approval process.	Agency Concurs	
8	Grant SBA Independent Litigating Authority	0	Rec 1. Congress should amend the SBA Act to include litigating authority for SBA	Agency Concurs	

THE U. S. SMALL BUSINESS ADMINISTRATION

AGENCY TEAM REPORT

NATIONAL PERFORMANCE REVIEW
TOLLGATE 4

INTERNAL WORKING DOCUMENT - NOT FOR DISTRIBUTION
August 3, 1993

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SECTION I

INTRODUCTION AND EXECUTIVE SUMMARY

SMALL BUSINESS ADMINISTRATION
INTRODUCTION

The Small Business Administration (SBA) was established as an independent agency of the federal government in 1953 to provide financial, management, technical procurement and other related assistance to the nation's small businesses, giving particular attention to small minority-owned businesses. The agency employs approximately 4,000 people (excluding its disaster assistance personnel) with a fiscal year 1993 budget of approximately $760 million.

Access To Credit

The agency's primary role is as a lender of last resort for the nation's small businesses. Traditionally, small firms have faced serious problems obtaining long-term loans in the private credit marketplace. With a total loan portfolio exceeding $20 billion, SBA's credit programs have provided some relief for borrowers unable to obtain loans without a federal guaranty. Demand for the agency's credit programs are at an all time high and the agency has had to seek supplemental budget authority in fiscal years 1992 and 1993 to meet this demand.

Almost 95 percent of all business credit extended through the SBA is provided in the form of loan guarantees. In 1992, nearly $6.5 billion of SBA-backed, generally long-term credit was provided to small businesses through banks, non-bank lenders, state and local development companies, and SBA-licensed investment companies.

SBA administers a number of small direct loan programs with 1992 approvals totaling less than $0.1 billion. These programs are designed to assist businesses owned by handicapped persons, veterans, minorities and other disadvantaged individuals. A new microloan program received a little over $30 million in funding both this year and last to provide very small loans (averaging $9,7000) up to $25,000 to individuals attempting to start or expand businesses.

Advocacy

The agency's Office of Advocacy serves as advocate for the nation's small business and will play a key role in preparing for and coordinating the 1994 White House Conference on Small Business. The office is responsible for gathering data on small businesses and maintaining a small business data base.

Disaster Relief

SBA's disaster loan program provides direct loans to homeowners, renters, and businesses to repair or replace damages resulting from physical disasters. This program, along with the Individual and Family Grant program at the Federal Emergency Management Agency (FEMA), provide the primary sources of federal disaster relief to individuals.

In addition to physical disaster loans, a generally small number of economic injury loans are provided to small businesses for working capital to assist them through the recovery period. The average annual program level is about $0.4 billion. However, in the wake of the Los Angelos riots, Oakland fires, Hurricanes Andrew and Iniki, Typhoon Omar, total disaster loans made in 1992 were nearly $0.8 billion. Total disaster loans are expected to exceed $1.0 billion in 1993, because many obligations made as a result of the severe 1992 activity have not yet been fully disbursed.

Management and Technical Assistance

Business development programs at SBA provide a combination of managerial and technical assistance to present and prospective business owners. Direct counseling, training and business information is available at any of SBA's nearly 100 field offices or through the SBA funded Senior Corps of Retired Executives (SCORE). Much of the agency's business development activities, however, are provided through Small Business Development Centers (SBDCs) located in every state. There are approximately 57 SBDCs and 946 subcenters throughout the country located primarily at colleges and universities.

Minority Assistance

Minority small business assistance programs provide contractual, financial, technical and management assistance necessary to promote business development of small businesses owned by socially and economically disadvantaged individuals. The agency's "Section 8(a)" program has provided more than 10,000 firms with federal contracts totaling more than $40 billion since 1968.

Procurement Assistance

Procurement assistance programs ensure that small businesses receive a fair share of government procurement and sales. This is accomplished through the agency's procurement center representatives, commercial market representatives and the Procurement Automated Source System (PASS) which contains the capabilities of approximately 250,000 small firms for use by procurement officials. In addition SBA administers the Certificate of Competency (COC) program (which certifies the capability of a small firm to perform a federal contract), and the timber sales program. In addition the agency provides grants (approximately 15 million in fiscal 1993) to states for the purpose of contracting with small businesses to plant trees on land owned or controlled by state or local governments.

Other Assistance

In addition to the above programs, SBA also provides guarantees of payment and performance bonds for small contractors; promotes international trade; promotes the expansion of businesses owned by women, veterans and native americans and administers the Small Business Innovation Research (SBIR) program which requires federal agencies to set-aside a small portion of their extramural research and development budgets for contracts with small businesses.

Shifting From Red Tape To Results

The tremendous burden of government regulations on businesses is disproportionately large on small businesses and often results in decreased productivity and increased costs. The Regulatory Flexibility Act, requires federal agencies to analyze the impact on small entities prior to the issuance of rules. Agency compliance is spotty at best. Various administrative solutions have proven to no avail. The National Performance Review's (NPR) solution is to allow small businesses access to the courts when the Regulatory Flexibility Act requirements are not met.

The "Section 8(a)" program is being reinvented to reduce the regulatory burden on program participants and users. The certification process will be streamlined. Federal procuring agencies will be allowed to contract directly with program participants. Additional tools will be developed to provide access to capital and credit to program participants and other minority-owned small businesses.

Introducing Market Dynamics

The lack of access to credit for qualified small business borrowers has wide implications for the nation's economy. Since small and medium size businesses are such an integral part of the nation's job creation and economic growth, the SBA must play an important role in ensuring that qualified small businesses have access to credit.

The NPR recommendations to improve access to credit for small businesses include revising the examination guidelines of financial institutions so that all small business loans of well-capitalized institutions may be placed in a single pool for reviews and increasing the capital reserve requirements for bank holdings of government securities.

NPR recommends changing the micro-loan program from a direct loan program to a 100 percent loan guarantee program, thus allowing these loans to be sold on the secondary market. This would reduce the amount of federal outlays, reduce the reserve for losses and lesson the administrative costs associated with a direct loan program while increasing the number of small businesses assisted by the program.

The NPR recommendation to establish user fees for the management and technical assistance provided by the Small Business Development Centers (SBDCs) will not only create accountability to customers but will ensure that the beneficiaries of the assistance pay a share of the program.

Creating a Quality Management Culture

Over the years the economy and the population of the U.S. has changed, but the staff distribution at SBA has not. This has resulted in severe workload imbalances. SBA has numerous studies to address this issue with broad staff participation, but no actions have been taken because of the continous turnover of Administrators. It is time to improve service and reduce costs.

To improve the delivery of service to the small business community, SBA will establish a basic principle of staff distribution based on administrative efficiency and program workload. The recommendations to support this initiative include realignment of functions, increased use of automation in its loan processing and loan servicing operations, improvement of its data collection and automation efforts and development of objective program performance measures.

Although there is a great deal of hard data about business and industry collected by the Census Bureau, the Bureau of Labor Statistics and the Internal Revenue Service, none of this data are broken down by firm size. As a result, the government lacks the data needed to support its public policy decisions, to target economic assistance to meet small business needs or to evaluate the value of existing programs for small businesses. To improve the quality of data available on small business, federal surveys that collect data on the economic activities of businesses will be required to include a question on business size. While this change is small, the availability of this data to the SBA and the administration would have major implications for environmental initiatives, tax law changes, workplace requirements, export promotion and energy policies by allowing the administration evaluate the impact of its policy changes on small business.

Referral of SBA litigation cases to the Department of Justice is burdensome, duplicative, time-consuming and inefficient. Most of these cases are of a specialized nature concerning primarily SBA programmatic issues. In most cases, SBA counsel are reduced to a supporting role, spending much of their time educating regular Assistant United States Attorneys as to the facts and legal issues present in a case, even though SBA counsel prepares the complaint and other pleadings and briefs.

The recommendation to provide SBA attorneys with independent litigating authority will eliminate the burdensome, duplicative and time-consuming process of referring litigation to the Department of Justice. Giving greater litigation authority to SBA attorneys will increase the government's ability to meet the demand for increased resources for litigation as well as free up Department of Justice attorneys to pursue other cases. The government will benefit from the more effective use of SBA attorneys who have the expertise and motivation o vigorously defend and prosecute SBA litigation.

SBA's Internal Reinvention Activities

Reinventing the SBA has been a priority of Administrator Erksine Bowles from the very beginning of his tenure at SBA. His first official act as Administrator was to introduce Vice President Gore to a group of state small business winners at a meeting to discuss reinventing government. His commitment continures with the establishment of an internal SBA team which will operate the entire four years he is at SBA.

The reinvention effort at the SBA has organized around the Administrator's philosphy that the best way to serve a customer is to listen to his/her concerns. Eight cities across the country have been selected to host a three-part town hall meeting over a two day period to obtain input from small businesses, local lenders and SBA employees.

SBA has established a seventeen member internal reinventing team call the "Entrepreneurial SBA Team (E-SBA)," comprised of employees representing all grade levels and program divisions. The E-SBA team has two important functions and has divided into subgroups. An outreach team has been established to develop ways to continue to involve all of SBA's customers in the reinvention process. Second, an issues team has been created to categorize the suggestions from employees, lenders and small business owners.

Synopsis

In summary, the recommendations outlined in the following issues will provide for increased access to credit for small businesses, a reduction in the burden of federal regulations on small businesses, and improved delivery of the SBA programs. The majority of the recommendations for SBA will have minimal fiscal impact on the agency since the recommendations can be accomplished within the agency's present budget authority. The overall savings from these recommendations is estimated at $17 million annually.

SECTION II

ISSUE PAPERS AND RECOMMENDATIONS

SHIFTING FROM RED TAPE RESULTS

Allow Judicial Review of the Regulatory Flexibility Act

Background

Small businesses are being overwhelmed by well-intentioned regulations that burden them with significant but needless negative consequences. Congress and the President recognized this problem in 1980 and enacted the Regulatory Flexibility Act (RFA). The RFA requires agencies to seek alternate regulatory solutions when rules have a disproportionate impact on small entities, including small businesses, small non-profit organizations and smaller jurisdictions of government. But most agencies have failed to perform the required RFA analysis. Rules continue to be issued whose harm could have been alleviated had they been examined during the rule making process through proper implementation of the RFA.[1]

For example, in 1986, Congress enacted the Emergency Planning and Community Right-To-Know Act, requiring local reporting of hazardous chemicals. The initial Environmental Protection Agency (EPA) implementing instructions required reporting of "any amount" of hazardous chemicals. The potential impact on small business was staggering. Even hot dog stands would have been required to report bottles of solvent or metal polish. The Small Business Administration (SBA) Office of Advocacy, which is directed by law to monitor compliance with the RFA, coordinated small business comments with EPA which explored less burdensome alternatives. As a result of this process, EPA raised the threshold for reporting to 10,000 pounds of hazardous chemical. This threshold eliminated hundreds of thousands of unnecessary reports, yet covered more than 95 percent of the total quantity of stored chemicals and 100 percent of those in quantities necessary to produce the sort of hazard which was the concern of the legislation.

The RFA, which works in conjunction with the fundamental agency rule-making law, the Administrative Procedure Act (APA), leads rule makers to one of two outcomes:
1. For rules that will have a significant economic impact upon a substantial number of small entities, the agency is required to perform a regulatory flexibility analysis. This analysis defines the burdens of the rule and examines alternatives that will lessen those burdens for

small entities.

2. For rules that will *not* have a significant economic impact upon a substantial number of small entities, the agency must so certify with a brief statement explaining the rationale for that conclusion.

While SBA's Office of Advocacy can request of agencies that they follow the RFA, there is no mechanism for enforcement of compliance. As a result, federal agency compliance is spotty. A few agencies, such as the EPA, the Food Safety Inspection Service, and the Nuclear Regulatory Commission, consistently and appropriately use the RFA to reduce the regulatory burdens imposed on small entities. Most agencies employ *pro forma* analyses that barely meet even the minimal requirements of the RFA. Others, including the Internal Revenue Service with its daily impact on small entities, define their rule making activities in the *Federal Register* as "interpretative," a category excluded from RFA responsibilities.

Several administrative efforts have been made to improve the level of responsiveness to RFA, but all have failed. The fundamental solution is judicial review, an approach favored by small business. Such judicial review is permitted for agency rule making under the APA. However, the RFA prohibits judicial review of agency compliance with the RFA. Courts have further restricted the use of RFA analyses as evidence in suits brought under the APA.

For the RFA to succeed at its goal avoiding needless government regulatory burden on small entities, there must be sanctions for non-compliance. Small entities injured by rules written without review of the impact on them as required by the RFA should have access to court, just as they do for the APA.

With judicial review, small entities could challenge an agency's failure to perform an RFA review or a flawed RFA review. They could sue in the appropriate federal court and, if they won, the court could remand to the agency with an order to explain their RFA determination or search for appropriate alternatives under the RFA. The goal would not be to create new lawsuits but to create a credible threat of lawsuits so that agencies would have a strong motive to ensure that the RFA is followed.

Judicial review is strongly supported by all of the major small business associations, including the American Small Business Association, the American Trucking Associations, the

National Association for the Self-Employed, the National Association of Manufacturers, the National Federation of Independent Business, National Small Business United, the National Society of Public Accountants, the Small Business Legislative Council, and the U.S. Chamber of Commerce.[2]

To bring about a better compliance with RFA, and to avoid needless lawsuits, it is important that the availability of judicial review be accompanied by systematic compliance guidelines to the agencies in how to carry out the RFA reviews. Most agencies have failed for more than a decade to develop this on their own.

Recommendations

1. Congress should amend the Regulatory Flexibility Act of 1980 to allow judicial review of agency determinations under the RFA.[3] This approach would enable small entities that have been injured by an agency action to seek judicial relief--but only when an agency had published a final rule, not at any earlier point in the rule making process.

2. The President should issue an executive order requiring Small Business Administration's Office of Advocacy to issue government wide guidance on appropriate processes for complying with the analytical requirements of RFA.[4] This approach would provide workable, consistent, technical guidance--the foundation for avoiding law suits.

Implications

The potential for judicial review will provide greater incentive to agencies to meet their present statutory obligations to consider the impact of their rules on small entities. Agency lawyers would ensure that the agency would properly comply with the RFA to avoid the valid threat of litigation if judicial review of RFA determinations were available.

Judicial review is not expected to lead to a large number of lawsuits.[5] There would be no basis for suit if agencies conducted an appropriate RFA review--the primary impact of this proposal. As a practical matter, most of the regulations to which small entities have great objection are already in litigation; judicial review of RFA would at most add another ground to the challenge. A few new cases solely based on RFA failure may result in those instances in which the impact of rules on small entities is sufficiently negative to impose greater costs than the cost of litigation--a fairly high threshold. In these rare cases, a challenge may be in the best interests of the country.

In the most extreme case, judicial review of RFA could lead to an initial flurry of lawsuits. Once the first few cases were decided, however, the boundaries between acceptable and unacceptable agency behavior under the RFA would become well known to agency attorneys and to the administrative law bar. After that, legal challenges could be expected to drop off dramatically.[6]

Both the process for developing the SBA guidance and the guidance itself will help achieve compliance with the RFA. First, the notice, comment, and public hearings will raise the level of awareness in federal agencies about the RFA. Second, the Office of Advocacy expects that the guidance ultimately developed will provide agencies with a sufficiently detailed map that they can navigate their way through the RFA in a real and substantive way, with a minimal investment of effort.

The RFA does not impose a requirement for an agency to collect additional data except in the rare instance where insufficient data was originally collected to understand the problem the rule was trying to solve.[7] In this case the additional task of information collection should not be attributed to the RFA but to an agency's failure to meet its obligations for reasoned decision making.

Agencies may view judicial review as simply another barrier in developing rules. But potential judicial review of final outcomes would not prohibit any rule making activity. It would merely delay implementation of a course of action until the agency properly identified the impacts of the rule on small entities and any alternatives to relieve those impacts. The effort in most such cases will be small relative to the work required to conduct rule making, and small relative to the benefits in enhancing national economic growth and small business competitiveness.

Fiscal Impact

Judicial review of RFA imposes no costs outside the government. In rare cases where there is no court challenge of regulations on other grounds besides the RFA *and* the cost of unnecessary or overly burdensome regulations is greater than the cost of litigation, small entities may choose to incur the cost of bringing suit based solely on violation of the RFA. The cost to these entities can not be estimated, but is seen by the entities as a net savings.

The procedures to implement the RFA would be limited to federal agencies. The costs inside the Federal government are difficult to estimate, as the costs of rule making are not a line item and are generally not well measured. The best estimates available suggest a maximum average of one work day per rule where there is no substantial impact on small entities, a total effort that can be absorbed in the current ceiling.[8]

Over the years, SBA has found that only 30-50 rules a year have significant negative impact on small entities. Assuming all of these were uncovered in the analysis, a more thoughtful review of alternatives would be necessary. This number is based on those already being identified as needing additional work, so this should not be seen as a new requirement.

If agencies do not comply with RFA, costs for litigation will certainly accrue. The marginal cost of the RFA suits can not be calculated in advance. Additional funds should not be budgeted for such costs, however, as an added incentive to avoid the costs by complying with the RFA.

End Notes

1. See annual reports on the Implementation of the Regulatory Flexibility Act, U.S. Small Business Administration, Office of Advocacy, 1981-1992.

2. U.S. House of Representatives, Committee on Small Business, in testimony of James Morrison, July 28, 1993. The organizations listed are the Regulatory Flexibility Act Coalition, which supports judicial review of RFA.

3. Judicial review can be established with the following language:

> (a) Section 611 of title 5, United States Code is amended by striking subsections (a), (b), and (c) and inserting a new subsection (a):
>
> "For purposes of section 702 of title 5, determinations made pursuant to this chapter shall only be reviewable upon publication or service of a rule as required by section 553(d) of title 5."

4. Implementing instructions for complying with the analytical requirements in sections 603, 604, and 605 of the RFA can be brought about by the following Executive Order:

> The Small Business Administration Office of Advocacy shall:
> Issue guidance to federal agencies for the implementation of the Regulatory Flexibility

Act. Such guidance shall be developed after consultation with affected agencies and after such public hearings as may be appropriate. The guidance will be designed to ensure that the analyses conducted under the Act provide data and reasonable alternatives.

This approach was used successfully in 1977 to provide a framework for all federal agencies in meeting the requirement to examine environmental impacts of federal actions as mandated by the National Environmental Policy Act of 1969 (NEPA). This approach was tested in the Supreme Court, and has been favorably commented on by that court several times. Such guidance would help agencies defend their actions in any legal challenges under the RFA.

5. Conflicting interpretations of NEPA requirements by various agencies often lead to litigation; this problem will be avoided by the systematic guidance called for in Recommendation 2.

6. This occurred with litigation under NEPA.

7. NEPA imposed a significant obligation on agencies to collect data on environmental impacts, something they had not been doing prior to the passage of NEPA. This was a source of substantial cost and concern to agencies.

8. SBA reviews about 1,500 rules per year which may be relevant to small entities. An average RFA analysis is 2 paragraphs to 2 pages, and should require well less than one work day. Taking the extreme assumption that no RFA analysis is being done now and that each new one was done at the high end of the range, this would generate a total government-wide burden of about six work years for the routine cases. This burden is spread over the policy staff of hundreds of agencies, so it seems unlikely that additional positions would be required.

REINVENTION OF THE SECTION 8A PROGRAM

First Draft

Background

While the efforts of the federal government and the Congress have helped to mitigate the effects of the historic exclusion of minority businesses from the competitive marketplace, and a broad spectrum of minority businesses have benefitted from the programs available under the Small Business Administration, the Department of Commerce and other federal agencies, minority businesses continue to experience obstacles in entering and thriving in the free enterprise system. The most recent statistics indicate that while minorities comprise ___ percent of the population, they own 8.9 percent of American businesses. These businesses account for only 3.9 percent of the nations gross business receipts and generate less than __ percent of the employment produced in this country annually---figures that have not changed in the past twenty years.

Minorities have a business participation rate of only one-fourth of that found among non-minorities. Despite the actions taken to date, it is clear that much remains to be done to bring the Nation closer to the goal of ensuring equal participation of all Americans in the free enterprise system.

The U.S. Small Business Administration's (SBA's) "Section 8(a)" program is one of the federal government's major programs providing assistance to minority-owned small businesses. The program has provided over 10,000 firms with federal contracts of $40 billion since 1968.

The "Section 8(a)" program is a business development program administered by SBA for small businesses owned and controlled by socially and economically disadvantaged U.S. citizens. To participate, firms must apply and be found by SBA to meet eligibility criteria. Program participation is limited to nine years. Firms may receive a variety of business development assistance including management and technical assistance, direct SBA loans, surety bond waivers, the transfer of government surplus property and federal government contracts awarded under special procedures.

SBA enters into contracts with federal agencies and subcontracts the performance of the contracts to eligible 8(a) participant firms. Competition is required under the 8(a) program for manufacturing contracts with a total value, including all options, over $5 million, and for contracts in all other industries valued at over $3 million.

While the program has produced a limited number of successful minority-owned small businesses, the program has been subject to much criticism and scrutiny by the Congress, the General Accounting Office (GAO), SBA's Inspector General (IG) and the National Academy of Public Administrators (NAPA).

Congress in passing legislation in 1989 to revise the program, found that the program had failed to meet the objectives of improving opportunities for small business concerns owned and controlled by socially and economically disadvantaged individuals to participate in the nation's economic mainstream. It found access to the program to be inordinately lengthy and burdensome and administration of the program to be inefficient and inequitable. Many federal procuring agencies have failed to identify and offer the necessary amount of contract support in order to allow for diversification and growth of disadvantaged businesses participating in the program. Congress determined that insufficient attention and support has been given to business development objectives of the program so that few concerns were prepared to compete successfully in the marketplace upon exit from the program.

The Section 8(a) program has still not met its business development objectives. The application process remains burdensome and lengthy, program reporting requirements are numerous, a number of program participants receive limited or no contract support, the program's data collection and automation efforts have not been fully implemented, some federal procuring agencies have failed to give serious consideration to the goal setting process for 8(a) set-aside and small business set-aside contracts and there have been delays in making contract awards because of the volume of activity in some SBA offices. Recent reports on the program show that almost 50 percent of the firms completing the program have ceased business operations or seriously curtailed operation within three years after program completion. Minority-owned firms, even after 8(a) program participation appear to have made little progress in competing in the private sector, obtaining major government procurements and increasing its share of the nation's gross business receipts.

SBA's role as a prime contractor in the 8(a) contracting process has been questioned by the U.S. Commission on Minority Business. The Commission concluded that the tripartite arrangement is a "process which consumes more time than needed, but contributes nothing of real substance to the development of the 8(a) firm". The Department of Defense (DOD) Advisory Panel on Streamlining and Codifying Acquisition Laws (Section 800 Panel) reached the same conclusion.

Prior to fiscal year 1993, SBA provided "advance payments" to 8(a) program participants for the purpose of assisting the concern to meet financial requirements related to the performance of a specific 8(a) sole-source subcontract. Advance payments were considered a source of last resort financing and were only available to a firm after it demonstrated that it had been unsuccessful in obtaining financing from any other commercial or governmental source. Advance payments and contract proceeds were jointly controlled by SBA and the 8(a) participant through the use of a special bank account, and SBA was repaid during the course of contract performance.

Effective October 1, 1992, SBA's ability to provide advance payments ended. The termination of this program resulted from SBA's determination that the advance payment program was a loan program under the meaning of the Credit Reform Act of 1990, and, therefore, required specific appropriation. Despite SBA's request, Congress did not appropriate funds for advance payments for fiscal year 1993. In addition, when reprogramming of funds was sought to finance this program, the staff of the House Small

Business Committee questioned whether SBA was authorized to provide advance payments.

Recommendations

1. The SBA Administrator should reduce the amount of time it takes to process 8(a) applications by streamlining the process and the application forms. The current application process takes on average 140 to 150 days compared to the Congressionally mandated time of 90 days. While, it is recognized that most of the current eligibility requirements were put in place to avoid fraud, waste and abuse, it is possible to identify parts of the application process that should be revised, modified or eliminated.

2. Congress should amend the Small Business Act to allow the Associate Administrator for Minority Small Business and Capital Ownership Development the authority to delegate the determination of Section 8(a) program eligibility. The current legislation requires all determinations of program eligibility and terminations to be made by one individual, the Associate Administrator for Minority Small Business and Capital Ownership Development. The substantial number of annual eligibility determinations that have to be made negatively, impacts on the ability of this individual to focus on the entire program. Consistent application of the rules and regulations by either delegating this authority to the Director of Eligibility and/or the Deputy Associate Administrator for Program, Policy, Certification and Eligibility would still be maintained.

3. Congress should amend the Small Business Act to allow SBA to delegate contract award to federal procuring activities so long as the activities consistently abide by federal acquisition and SBA 8(a) program regulations. This recommendation would not alter SBA's authority to insure that a requirement offered for the program is appropriate for award under the program, or that the concern selected to perform the contract is eligible for the award.

4. Congress should amend the Small Business Act to require federal procuring activities to use their existing statutory authority to provide advance payments on 8(a) contracts when such funding is necessary to contract performance. This would not require any additional appropriation of funds since it would involve an advance of contract proceeds.

5. The Administrator of SBA and the Secretary of Commerce should establish a working group to review all federal minority business assistance programs, with particular attention on the "Section 8(a)" program and the programs of the Minority Business Development Agency and make recommendations for improving assistance to minority-owned small businesses to the President within __ days of the date of this report.

6. The SBA Administrator should develop legislation to revise the Section 8(a) program within __ days of this report. The revised program should incorporate strategies which provide incentives for participation by major American corporations in the governments effort to promote minority business development. These strategies should include, economic incentives for the private sector such as tax credits for providing assistance to minority-owned firms or for every job created in the minority-owned firm as a result or providing the minority-owned firm with subcontracts. The Administrator should also consider the use of tax credits for investing in minority-owned businesses. The revised program should have an open or self certification process for anyone meeting the revised standards for participation, with criminal sanctions for false certifications.

Additional elements to be considered for inclusion in the revised program should include, establishment of a specialized lenders pool to provide loans to 8(a) participants and other minority small businesses and financing programs linked to the mircoloan program for 8(a) participants.

The review of the 8(a) program should include input from SBA employees, program particpants, federal procuring officials, representatives of the minority community and other interested inidviduals and organizations.

Implications

Improving assistance to minority small businesses will contribute to the growth of the U.S. economy. Establishment of effective programs to promote the ability of minority business enterprises to participate in the competitive market is an important element in the planning and implementation of strategies to reduce employment and other economic and social problems in minority communities. Coordination of the two major federal minority assistance programs will more effectively address the practical problems that hinder the development of minority businesses.

Reducing the regulatory burden of 8(a) certification and program participation should reduce the cost of applying for and participating in the program. Further, streamlining the application process will make the program more accessible and increase the number of program participants.

Allowing SBA the authority to delegate its contracting function to federal procuring activities will provide an additional incentive to procuring agencies to offer requirements to the program.

Requiring federal procuring agency's to use their existing statutory authority to provide advance payments to 8(a) participants will create a source of needed financial assistance without any additional appropriation.

A complete review of federal minority business assistance program will result in comprehensive legislation to ensure minority small businesses are provided the necessary assistance to compete and grow in the U.S. economy.

Fiscal Impact

All of these recommendations can be implemented within the present budget authority with the exception of the proposed provisions for tax credits and financing programs.

INTRODUCING MARKET DYNAMICS

Increase Small Business Lending by Adjusting

Bank Regulator Review Standards

Background

The President, as well as numerous professional and business groups, have identified the difficulty in obtaining credit for qualified small business borrowers as a "credit crunch." This lack of access to credit has wide implications because small businesses are the fastest growing segment of the economy, the major source of new jobs.

Two major causes of the credit crunch for small business are: (1) the stringent review and resulting documentation requirements of small business loans imposed by the banking regulators; and (2) the differential requirements for the capital reserve that banks must hold for different types of loans, resulting in disincentives for commercial loans. In combination, these factors have discouraged banks from making small business loans and encouraged them to shift their resources elsewhere.

There is a substantial burden of documentation required for commercial loans. On a large loan, the cost of this burden can be amortized over a large base. But the paperwork burden, almost a fixed cost, is proportionately much greater for a small loan. Banks report that their cost for letting small business loans has reached the point that many find it not worth the trouble. This is particularly unfortunate since such loans are frequently collateralized in excess of the amount of money lent, and thus are a force for banking stability rather than risk.

In response to these problems, President Clinton introduced a mechanism to pool "character" loans for regulator review.[1] The regulators look only at the success of the group of loans rather than requiring detailed documentation for each individual loan, thereby reducing the stringent documentation requirements and increasing their attractiveness to banks.

The anticipated credit expansion has not yet been forthcoming. Character loans are only a small portion of small business loans; some banks have concerns that character loans have become second class loans. A recent survey of 25 banks showed that only one had chosen to use the character loan pool.[2] Additional steps are clearly needed.

The solution to the administrative burden is to extend the loan pool to include all loans to small businesses provided by well capitalized financial institutions.[3] The banking regulators would then assess the performance of the pool as a whole in accordance with the financial institution's safety and soundness guidelines. If a loan does not perform (i.e., is 60 days overdue), it would be pulled from the pool and reviewed individually by the regulators.

The capital reserve requirements are a more complex matter. The Committee on Banking Supervision of the Bank for International Settlements (the Basle Committee) has been meeting for more than a decade to establish global minimum capital rules for banks that are internationally active. The Basle Committee includes the banking supervisors of the largest industrial countries, with participation of the Federal Reserve Board, Comptroller of the Currency and Federal Deposit Insurance Corporation (FDIC) for the United States. In the Basle Accords of 1988 the Committee reached agreement on global minimum capital standards for "credit risk," a debatable measure because risk is usually the product of many variables rather than an inherent constant.

There are two types of risk, credit (default) and market (interest rate fluctuation). Prior to the Basle standards, U.S. regulators imposed the same six percent capital requirement irrespective of the type of asset held by the bank. This meant that banks were equally free to lend to the government (purchase bonds) or lend to small business. The Basle standards increased the percentage of assets a bank must hold as capital for business loans from six percent to eight percent. But the Committee was unable to reach agreement regarding market risk, so set no standard. This *reduced* the reserve requirement from six percent to zero percent.

This differential reserve requirement created an enormous preference for banks to buy government bonds rather than make loans to businesses. The results were immediate and sweeping.

In the first six months after the new capital reserve requirements, U.S. bank assets grew by 18 percent ($545 trillion), and bank holdings of government securities mushroomed by 71 percent ($263 billion), while the volume of new bank "commercial and industrial" loans began to fall precipitously. In the following three years, less than one half of one percent of bank asset growth went into commercial loans--the remainder went into government securities.[4]

Big business has other avenues to credit, and was not greatly affected--corporate indebtedness continued to rise, showing that the demand remained high. The difference was made up by a virtual evaporation of credit for small business. In the words of the Chairman of the U.S. Securities and Exchange Commission, "...the burden of the credit crunch fell on the small business sector."

The decision to raise capital standards for banks around the world at that time was a sensible step in light of the magnitude of recent losses in bank loan portfolios. As a result, banks increased their capital reserves and became more stable. In the last two years, banks have enjoyed record profits. It is now time to shift some of their investment back to qualified loans to assist the rest of the economy.

In addition, the lack of reserves for bonds opens the way for a repeat of the savings and loan (S&L) crisis. While the Basle Accord assessment of the risk of default on government bonds is accurately set at zero, the value of U.S. Treasury bonds fluctuates widely as interest rates rise and fall. The insolvency in S&Ls was initially the result of investing short-term deposits (which reprice with rising interest rates) in long-term, fixed rate mortgages. Investing overnight deposits in long-term, fixed rate bonds without capital reserves is exactly the same formula.

The solution for both the risk of interest rate fluctuation for bonds with no capital reserves and the shortage of credit for small business is the same: increase the capital reserves for bank holdings of government securities. This step would provide the needed reserve and make commercial loans suitably attractive to banks.

Increasing the capital reserve requirement is allowable under the Basle Accords, which set only *minimum* requirements. And it is easily implemented by amending the Department of the Treasury (Office of Comptroller of the Currency and the Office of Thrift Supervision) bank regulator guidelines set in the 1989 *Federal Register*. This covers national banks only--additional agreements would be needed with the other regulatory agencies.

The exact rate of capital reserves appropriate for government securities is a highly technical issue and a matter of substantial debate by the Basle Committee for more than a decade. But there is general agreement that the rate should be somewhat less than the requirement for commercial loans. The 6 percent level was the historical practice in the

U.S. and is an appropriate interim standard until the Basle Committee finishes their work and sets a world wide standard.

Since March of 1989 when the Basle Accords were implemented, bank assets have increased from around $3.1 billion to around $3.6 billion. If bank loans had kept pace with bank assets, loans would have increased proportionately from about $624 billion to about $724 billion. Instead, they fell by about $27 billion. A return to proportionate growth in loans brought about by eliminating the capital reserve disincentives for such loans, coupled with a decrease in the paperwork burden on loans to small businesses brought about pooling, would be sufficient to end the credit crunch.

Recommendations

1. By Executive Order, the President should initiate the revision of the examination guidelines of financial institutions by the banking regulators so that all loans to small businesses by a well-capitalized institution may be placed in a single pool for review.

2. The President should direct the Treasury Department to amend 54 *Federal Register* 4186 dated January 27, 1989, to return banks' capital reserve rate for government securities from zero percent to six percent, phased in over a two-year period, and effective until the Basle Accords are amended to establish an international standard. Legislation is not required, as the changes are in the review practices of the regulators, not in the stipulations of law. However, coordination between the various regulatory agencies would be required, including the Federal Reserve and the Federal Deposit Insurance Corporation. The above actions are completely within the framework agreed to in the Basle Accords.

Implications

The loan pool review process is well understood. It is currently being used for home-equity, car, and other general consumer loans, as well as in the specifics of the "character" loan initiative by the President. The mechanism is easily adaptable for small business loans, and speedy implementation can be expected.

The pooling proposal introduces little risk, as it is limited to well capitalized banks. The definition of well capitalized is firmly established in regulation and regulator review practice, and universally understood within the banking industry. Limiting the pool to these banks excludes banks with risky practices or limited resources.

The pooling proposal builds in incentives to ensure that the loans are sound without emphasizing stringent documentation requirements. If a well-capitalized institution has an abundance of overdue loans, bank regulators would be permitted to review all loans in the pool. Financial institutions realize that making unnecessarily risky loans will not only jeopardize their status as a well-capitalized institution but could also lead to higher insurance premiums.

Returning the bank capital reserve requirement for government securities to the previous six percent level would require banks to shift assets, probably requiring selling off bonds or loans to raise capital for reserves. The impact on the securities market is hard to foresee, but would probably remain fairly stable with increased holdings by foreign banks. Banks have recently enjoyed the highest earnings in two decades, and for the last year bonds have been getting more valuable, so this is the best time for such a move. The relatively small number of banks in capital trouble would be stressed by such a move. The level of stress is substantially smaller than if interest rates were again to go up by a few points. In summary, increasing the capital reserve requirements for bank holdings of government securities would *decrease* the risk of bank losses due to interest rate fluctuations.

Banks are essentially in the business of making loans, but the differential capital reserve requirements are driving them into being little more than mutual funds for government securities. If this trend continues, there is question if FDIC insurance should be continued--without loans there is no reason that bank mutual funds should enjoy government insurance while the other mutual funds of government securities do not. The two recommended actions should eliminate the disincentives and get banks back in the business of making commercial loans. The actions accomplish this by using tried and true capital reserve standards, and without requiring additional federal guarantees or funds. This increased willingness to make small business loans should result in an additional credit expansion of at least three to four percent, an amount sufficient for the current growth potential.

The proposals are likely to lead to increased community re-investment, as most small loans to small businesses are made by community banks which tend to loan in a local sphere.

Fiscal Impact

There are no direct costs in these recommendations. The indirect costs are limited to the cost of writing the regulations and guidance at the various agencies which regulate banks.

The pooling proposal has no implications for insurance or risk because the recommendations are restricted to well capitalized institutions. The capital reserve proposal has no risk implications for insurance as it increases the stability and credit worthiness of banks.

There will be some transaction costs for banks to set aside capital reserves.

Endnotes

1. On March 10, 1993 President Clinton initiated a new regulatory policy concerning small business loans. This policy was implemented on March 30,1993 by a banking regulators policy statement which detailed documentation requirements for small business loans and permitted financial institutions to make loans on the "character" of the borrower. These loans would be examined by the regulators as a whole instead of reviewing each loan individually.

2. According to John P. LaWare, Governor, Board of Governors, Federal Reserve System, testimony before the House Banking Subcommittee, June 29, 1993.

3. "Well capitalized" is defined by the Federal Deposit Insurance Corporation Improvement Act of 1991. The FDIC, Federal Reserve, and Office of the Comptroller of the Currency regulators use CAMEL ratings: capital adequacy, asset quality, management, earnings, and liquidity. The Office of Thrift Supervision uses MACRO ratings: management, asset quality, capital, risk management, and operating results. Both provide a comprehensive rating of the overall safety and soundness of the bank.

4. There is an overall leverage limit for the entire bank portfolio that would impose a capital requirement if a bank's portfolio was largely composed of bonds, but this overall standard does not have an impact until a very substantial part of the bank's portfolio has been transformed into bond holdings.

Change the Microloan Program To Increase Loans for Small Business

Background

The Small Business Administration's (SBA) Microloan Demonstration Program, a five-year pilot program, is almost two years old. The program that provides direct loans to nonprofit intermediaries who in turn provide loans of up to $25,000 to small businesses with a current average loan amount being $9,700. Microloans are made to low-income individuals, women, minorities, and other entrepreneurs unable to obtain credit through traditional lending sources. The program fills a void in the credit market, where very small loans (those under $25,000) are not available from mainstream lenders due to the high costs associated with making and servicing such financing. As Erskine Bowles, the Small Business Administrator Administrator, has pointed out: "Two-thirds of the business started in America are started with less than $10,000 in capital; one-half with less than $5,000." [1]

In addition to lending capital, the Microloan program also provides grants to intermediary lenders and other technical assistance providers which are used to strengthen the skills of the small business owners in such areas as accounting, marketing and other basic business practices.

As of the end of July 1993, SBA had selected 96 nonprofit intermediaries to participate in the program nationwide. The program is fully supported by the Administration and by Congress. In a recent Rose Garden ceremony President Clinton commented: "The Microloan program, by encouraging entrepreneurial instincts, can help change an economically dependent person into a productive and financially self-reliant citizen."[2]

Currently, SBA is making direct loans to intermediary lenders. These loans can be as high as $1.25 million to any single intermediary (single intermediary means one intermediary or a consortium of many). SBA charges a rate equal to a 5-year U.S. obligation (Treasury Bill). SBA then reduces the interest rate to the intermediary by up to two percent based on the average loan size of the intermediary's microloan portfolio. Grants are provided to intermediaries in the amount of 25 percent of any loan amount disbursed from SBA to intermediaries. Further grant dollars are made available to non-lending technical assistance providers.

In 1994, the President's budget requests $33.7 million for the direct loans to the intermediaries. The subsidy rate (reserve for losses) for this direct loan program will be 15.25 percent of the total amount appropriated, plus an additional amount of approximately 5 percent to cover the interest rate buy-downs in the program.

The expansion of this program will require either an increase in appropriations for further cash outlays or a change in the program to affect lower costs and stretch the current appropriation. Currently, SBA provides 100 percent direct loan funding to the nonprofit intermediaries under this program. The proposal to change this direct loan program into a guaranty program would call for banks to directly lend to nonprofit intermediaries with SBA to guaranty 100 percent of these loans. The nonprofit intermediaries would in turn make microloans to small businesses. This proposal means a reduction of federal cash outlays, a reduction of the reserve for losses (subsidy account) and the lessening of the administrative burdens associated with direct lending.

Recommendations

Congress should amend subsection (m) to Section 7 of the Small Business Act, 15 U.S.C. 636 to give the Small Business Administration authority to provide a 100 percent guaranty on loans made by approved lenders to intermediaries selected by SBA. This recommendation changes the Microloan program from a direct loan program to a loan guarantee program. The amendment should also give SBA the authority to sell such loans on the secondary market. These changes would allow the agency to make loan capital available to intermediaries under a guaranty authority and would provide the agency with the authority to sell the guaranteed loans on the secondary market, providing the full faith and credit backing of the U.S. government to the investor. SBA would still provide technical assistance grants and interest rate buy-downs.

Implications

The recommendation would keep all the current authorities and program elements in place but would allow SBA to provide financial support to micro-enterprise development under a guaranty loan program, rather than under a direct loan program.

Agency authority to sell the guaranteed loans on the secondary market would allow private investors, such as pension funds, to participate in the program. The proceeds from sales on the secondary market would be returned to intermediaries providing fast access to capital for continued microlending under this program.

The establishment of credit history for small businesses through the microloan program would hopefully ease the transition into traditional lending when business credit needs exceed the maximum $25,000 permitted under the Microloan program.

Changing the program would realign the current anticipated administrative burden on the agency to a point where a $100 million (as opposed to $33.7 million) program could be delivered with little or no increase in overhead. Front end costs may increase regarding selection and oversight of intermediaries. However, estimations regarding servicing and collection costs will decrease as these functions become the responsibility of the lenders. Secondary marketing costs would be introduced.

Realignment of the Microloan Demonstration Program from a direct loan program to a guaranty loan program will provide real use expansion from $33.7 million to $100 million with minimal change (as discussed above) in the budget. Private sector involvement will increase; estimations for future agency outlays will be reduced; the goal of the program expansion will be reached.

Fiscal Impact

The 1994 budget provides $33.7 million for direct loans to Microloan intermediaries. It also contain $6 million for technical assistance grants. The subsidy rate (loss reserve) currently used in the Microloan program was based on the results of direct loans approved under the 7(a) program. The current subsidy rate is 15.25 percent. An additional 5 percent is provided for interest rate buydowns. This provides a total subsidy rate (losses + buydowns) of 20.25 percent. By changing the program to a guaranty program, the subsidy rate could be lowered, given the 1993 7(a) guaranty rate, to a rate of 5.47 percent plus the 5 percent for interest rate buy-down making the total subsidy rate for the Microloan Demonstration Program approximately 10.47 percent or approximately half the current proposed rate of 20.25 percent.

The program would be expanded ten-fold as follows:

- $10 million of that $33.7 million would provide guarantees for approximately $100 million dollars in loans to intermediaries.
- The remaining $23.7 million, added to the $6.0 million already allocated for grants, would provide funding for the 25 percent technical assistance grants required for a $100 million program.

ENDNOTES

1. Comments at the Mircoloan Announcement Ceremony, the White House, Washington, DC. May 24, 1993.
2. Ibid.

Establish Users Fees For SBDC Services

Background

The Small Business Development Center (SBDC) program in the Small Business Administration was established in 1980 to further economic development by providing management and technical assistance to small businesses.

Fifty-seven lead SBDCs are located in all 50 states, Puerto Rico and the Virgin Islands with a network of approximately 946 service delivery locations. To receive federal funds, SBDCs must provide an equal amount of matching funds from sources other than the federal government. The fiscal year 1993 appropriation is $67 million.

SBDCs undertake a wide variety of activities designed to assist the economic development of a state or region through growth of its small business sector. The core activities of one-on-one counseling and a broad spectrum of training events is augmented by specialized assistance in such areas as procurement assistance, exporting assistance, mentoring programs for women owned businesses, veterans and minority assistance programs. Presently by law all counseling is provided free. SBDCs also offer their counseling and other services to state and local economic development agencies currently responding to the loss of defense-related jobs and businesses.

In fiscal 1992, SBDCs counseled 222,497 clients and trained 319,535 clients. From 1980 through 1992 over 1.2 million clients received counseling and more than 2.5 million attended training.

Economic impact data contained in the 1991 and 1992 annual reports of a sample of ten SBDCs (of the fifty-seven currently in the program) show that for a total of $11.4 million federal dollars, in over a twelve-month period, these ten SBDCs created 11,190 jobs, and preserved and stabilized 6,559 other jobs. Additionally, six of these 10 SBDCs which reported on capital investment secured $189.6 million in capital investment for clients in their states.

If those 10 sample SBDCs are extrapolated to reflect the activity of all 57 SBDCs, it is estimated that the current level of funding of $67 million could provide as many as 80,000 new jobs and preserve 148,000 jobs for a total impact on 228,000 jobs in a single year. The cost to the federal government using this extrapolation is approximately $300 per job, which is minimal as compared to the tax and other benefits relative to employment. In addition, the assistance provided by the SBDCs to the small business entrepreneur in securing capital investment is significant.

In 1989, the U.S. General Accounting Office evaluated the SBDC program. The evaluation found that:

> Overall, 69 percent of clients were satisfied with the counseling they received. Similarly, 76 percent indicated they would contact the program for future help if needed, and 82 percent would recommend the SBDC program to others. SBDC clients also said they were assisted quickly, received the kind and amount of assistance they wanted, and found the assistance useful. About 17 percent of clients counseled by the program were not satisfied with the assistance they received. Dissatisfied clients believed they were not assisted quickly and did not receive the kind and amount of assistance they wanted, and they reported that the assistance received was not useful. Few of these dissatisfied clients indicated they would use the program in the future or recommend it to others. About 14 percent of those counseled by the program were neither satisfied nor dissatisfied with the assistance they received. [1]

Given the high level of satisfaction and perceived value of the program, the establishment of a user fee would not dampen the enthusiasm for the program by its users. Such a fee should be set at a level which is easily affordable to the average small business owner.

Recommendation:

Congress should amend Title II of the Small Business Development Center Act of 1980, Public Law 96-302, to give the Small Business Administration the authority to establish user fees for SBDC counseling services of $15.00 per hour. This rate is not intended to fully recover the actual cost of the services provided. The full cost of these services is approximately $25.00 per hour, but such a rate would be burdensome to the vast majority of customers, as they are predominantly start up businesses. The $15.00 hourly rate is based on what these customers can reasonably afford.

Implication:

The implementation of the user fee charge would generate significant revenues for the SBDC program. It would return to the most productive SBDCs program income which can be used to operate their programs. The $15.00 fee is generally well under the rate charged by consulting, accounting, legal or other professionals. In addition, receiving services from an SBDC allows the small business owner to receive comprehensive services without having to find and engage multiple consultants in different locations. The SBDC would continue to be a one-stop shop at a reasonable price. Since SBDCs are widely dispersed geographically, they are accessible to most small businesses without significant travel time required.

Fiscal Impact:

The proposed user fee is based on the number of hours utilized for counseling purposes. The fee would yield an estimated $17.0 million per year to be used towards current and future program costs. The Small Business Administration in fiscal year 1993 received $67 million to support the SBDCs. With establishment of user fees the amount could be reduced by $17 million.

FISCAL IMPACT TABLE

($ in Millions)

	1993	1994	1995	1996	1997	1998	1999
Budget Authority $	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Outlays	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Revenues	17.0	17.0	17.0	17.0	17.0	17.0	17.0
Change in FTEs	0	0	0	0	0	0	0

It is assumed that these reveneus would be used to reduce current appropriations to SBA for the SBDC program.

ENDNOTE

1. United States General Accounting Office, Briefing Report to the Chairman, Committee on Small Business, United States Senate, *Small Business Development Centers Meet Counseling Needs of Most Clients*, (Washington, DC., November 1989) p.2.

CREATING A QUALITY MANAGEMENT CULTURE

Distribute Small Business Administration Staff Based on Workload and Administrative Efficiency

Background

The average tenure of nine of the last twelve Small Business Administration Administrators has been approximately 16 months. This high turnover rate has allowed a substantial amount of management difficulties to go unresolved, including problems in substantively addressing issues of efficient staff distribution. During this period, the number of staff has gone down, and the number of programs being managed has gone up. Substantial improvements in computer capability have been made but not fully implemented. There has been an increase of positions into overhead, and the relative need for SBA programs by geographic area has changed with the population and economic shifts in the country.

As a result, the distribution of staff in SBA has increasingly diverged from the distribution of workload. For example, in largely rural Region VII (Kansas City), there is one employee per 54,000 people, while in largely urban Region V (Chicago), there is one employee per 131,000 people. This staff distribution problem is widely recognized within SBA, and numerous studies have been undertaken to rectify various aspects, most of them with broad staff participation. In 1991 the Resource Allocation Task Force, consisting of both headquarters and field staff, made a detailed review. While there was some disagreement about the precise index that should be used for comparison (total population, business population, etc.), there was no disagreement that the staffing was disproportionate by both region and program. The Task Force made specific recommendations. But none of the studies has been implemented, again largely because none of the Administrators has been in place long enough to deal with them.

Currently, each of the 67 district office has a small cadre of loan officers that service its loans. SBA has conducted a successful pilot program in Fresno, California, which provides routine loan servicing for several District Offices. It has been demonstrated that a highly automated loan servicing center could substantially reduce the number of loan servicing officers required in the district offices.

Another problem is redundant support systems. By legislative mandate, SBA has a number of different direct loan and loan guarantee programs, each targeted at a different sub-population. The various programs use the same application forms and credit analysis, but must maintain duplicative regulations, training, staff and administrative support because they are seen as separate programs. Much can be gained by making the procedures uniform so that the programs are easier to support.

A third problem is the current headquarters structure. About 75 percent of the agency personnel resources fall under one division: Finance, Investment, and Procurement Assistance. However, the finance and investment portions demand so much management attention that procurement assistance and minority business development receive little attention from division management. In addition, procurement programs are distinctly different from either finance or investment programs. One solution is to separate out procurement assistance and minority small business programs. This would elevate the attention they receive, and make it more likely that their manager was experienced and could focus exclusively in these areas.

The general solution to each of these problems is to establish a basic principle of staff distribution based on administrative efficiency and program workload. The mechanics of accomplishing this should be left to SBA.

The new Administrator has stated that he wants to address these issues from the ground up and has called for a series of proposals from the various levels of SBA toward streamlining administration and reallocating more employees to work in direct client services. It is his intention to combine these proposals with the previous studies and his own management judgement to develop an efficient and effective management structure. While the results were not yet in when this report was prepared, all initial indications are that the needed fundamental improvements will finally be made.

The analytic work conducted over the years suggests that the major actions could be initiated immediately and simultaneously so as to optimize moves and minimize disruption. The turnover rate may permit many of the changes to be accomplished over time through attrition. The amount of likely change falls within agency authority to reprogram funds, so new legislation does not appear to be required, unless the fiscal year 1994 budget dictates otherwise.

Recommendations

The President should issue a Presidential Memorandum to the Administrator of Small Business Administration, requesting that staff at SBA be allocated on the basic principles of administrative efficiency and program workload. The Administrator should be instructed by this Order to review the existing studies in conjunction with his own studies and develop a comprehensive plan for speedy implementation to improve service delivery, taking whatever personnel actions are needed to achieve highly automated administrative efficiency, establish objective workload measures, allocate program staff based on objective and uniform workload indicators, and thereafter fill vacancies only if workload studies show that to be the optimal use of that position.

Implications

Reallocating staff based on these principles would substantially improve the service provided to small businesses. The exact improvement is unknown until the Administrator finishes his study and develops his plan, but previous studies have suggested that as many as 600 positions could be shifted to direct client support.

Fiscal Impact

The studies to date suggest that these principles can be accomplished within the current fiscal year 1993 SBA budget. No net savings are anticipated in the number of positions, as all saved positions will be reinvested in the district offices to improve service. This increase in the district offices will lead to better service while the concentration of the administrative support will lead to faster response times and better data. Both of these lead to stronger small businesses.

Improve Federal Data on Small Businesses

Background

Although there is a great deal of hard data about business collected by the Census Bureau, the Bureau of Labor Statistics (BLS), and the Internal Revenue Service (IRS), none of this wealth of data is broken down by firm size for businesses with less than $10 million in assets or receipts--in other words, small businesses. This means that even the most basic small business indicators such as capital flow, job creation, or business dynamics cannot be extracted from the data already gathered.

As a result, the government lacks the small business data needed to support its policy making, to target economic recovery programs to meet small business needs, to evaluate the value of existing programs, or meet Congressional mandates.

Even in the rare cases where agencies have attempted to obtain data by firm size, its usefulness is very limited. Census's *Enterprise Statistics* is five years out of date. IRS's limited data on sole proprietorships are three years out of date and ignores most significant parts of the small business sector such as partnerships, sub-chapter S corporations, and regular "C" corporations. Although BLS collects data on business "establishments" and "reporting units," neither of these categories are related to firm size, making comparisons between large and small firms impossible.

Significant amounts of money are being spent on the collection of business data: BLS alone has a statistical research budget of $190 million. By adding a simple question on firm size to existing statistical research and data collection conducted by federal agencies, we can improve efficiency and gain much needed information, which would otherwise require a substantial increase in the SBA statistical research budget to acquire independently.

Recommendations

1. The President should issue an Executive Order specifying that future federal household and employer surveys that collect data on the economic activities of businesses should be required to include a size of firm question. A single demographic item is sufficient:

About how many people are employed by this employer in total, counting ALL locations?

□ less than 10	□ 100 - 249
□ 10 - 19	□ 250 - 499
□ 20 - 49	□ 500 or more
□ 50 - 99	□ Don't know

These are standard size breakdowns used by SBA.

2. The Order should also direct OMB to provide enforcement of this requirement during the approval process for questionnaires going to the public.

Implications

These recommendations do not affect any current studies and do not propose any new studies.

These recommendation affect only a narrow segment of future federal studies. A survey of recent federal economic activity questionnaires identified only 10 documents that would have provided useful information on small businesses. These were issued by the Department of Health and Human Services (HHS), Department of Treasury (including IRS and Customs), and the Department of Commerce (including BLS and Census). It is unlikely there would be much applicability outside these three departments, or that many studies would be affected.

The result of this small change, however, would be very large in the quality of information made available to shape Federal legislative and regulatory actions which have a differential effect on small and large businesses. There are implications for environmental initiatives, tax law changes, changes in workplace requirements, trade, and energy policies. Public actions, in turn, affect private sector decisions regarding hiring and firing, opening and closing locations, introducing new products, investing in new plant and equipment, human resource development expenditures, and the magnitude, timing, and choice of financing.

Agencies may raise two concerns with including this additional demographic item: they would have to drop an important item to make room for it, and it opens the door for other additions. As a practical matter, the addition of one item is not a great burden, particularly since the requirement will be known during the design stage. And if there are indeed other items which would have a significant impact on economic recovery, perhaps the door to their addition should be open.

Fiscal Impact

This proposal would create some additional costs, however they would be negligible.

Congress Should Grant the Small Business Administration Independent Litigating Authority

Background

An amendment to the Small Business Act is needed to streamline the referral of Small Business Administration (SBA) cases for litigation purposes.[1] This change would make case management and litigation more efficient, less time-consuming and more resource effective. Such an amendment would give the SBA Administrator the authority to determine whether it would be most effective for a case involving the agency or its officials to be referred to the Department of Justice (DOJ) for litigation or retained for handling by SBA counsel.

SBA litigation consists primarily of either affirmative litigation involving claims against defaulting businesses and guarantors or participating lenders and sureties and similar cases, or defensive litigation, which most often arises under specific SBA programs.

SBA attorneys must refer all claims litigation (also called affirmative litigation) to the Department of Justice. This litigation is then referred back to the U.S. Attorney or originating SBA District Office to institute suit, thus wasting valuable time that could have been spent pursuing the debtor. This referral process to DOJ and then back to the U.S. Attorneys' Offices or to SBA is burdensome, duplicative, time-consuming and inefficient. The DOJ referral process currently takes one to three months per case. Staff hours spent filling out the required forms total two to four hours per case.

Moreover, currently, SBA lenders are using private counsel for debt collection litigation for assets they hold in their name (currently more than 2,500 cases). Part of the reason for this is their perception that DOJ is less timely and aggressive than private sector specialists.. The reluctance to use Department of Justice counsel costs the U.S. Treasury about $5 million in private attorney fees. Since SBA pays expenses in accordance with its guarantee percentage (approximately 80%), there would be a savings of approximately $4 million if SBA counsel would take over all the cases. Since some lenders will utilize private attorneys even when SBA has the authority to litigate, 3 million is a conservative estimate of the potential savings if SBA gets its own independent litigating authority. However most of that savings might be offset by additional SBA litigating costs.

Finally, a recurrent problem that compounds those listed above is that DOJ has no uniform policy for the appointment of SBA counsel as Special United States Attorneys ("SAUSAs") to pursue litigation, but leaves it to the determination of each U.S. Attorney. In most cases, SBA counsel are reduced to a supporting or clerk's role, spending much of their time educating regular Assistant United States Attorneys as to the facts and legal issues present in a case, even though SBA counsel prepares the complaint and other pleading and briefs.

As of September 30, 1992, SBA had approximately $578 million in defaulted loans and accounts receivable classified "in litigation." Approximately 40 percent of this litigation is presently handled by SBA counsel informally or as SAUSAs. SBA has an extensive field office network with almost 300 attorneys. The rest of this litigation is handled by either counsel for participating lenders or by referral to various U.S. Attorneys' Offices.

Currently, there are approximately 335 cases of a defensive nature pending against SBA or its officials, in various federal district courts throughout the country. Most are in fact of a specialized nature concerning primarily SBA programmatic issues such as disputes over the meaning of various provisions in SBA guaranty agreements, regulations, policy directives or the actions of SBA officials. As with affirmative litigation, much of the time, SBA counsel is relegated to a supporting or clerk's role. There is an even greater lack of utilization of SBA counsel's programmatic expertise in the defensive area than in claims litigation. Problems are found in referral of defensive cases when SBA is sued. Often, DOJ does not refer the complaint to the SBA Central Office for months. Frequently, SBA receives the complaint from DOJ months after is has been served. Also, many times, SBA is informed of adverse lower court decisions with insufficient time to adequately respond.

Frequently, in defensive litigation, temporary restraining orders are sought. This form of injunctive relief is sought immediately giving the regular AUSAs virtually no time to familiarize themselves with the issues in the case involving SBA programs. This puts the agency at a serious disadvantage, since the result is poor performance at oral argument that often leads to the granting of temporary injunctive relief, or waffling by AUSAs where SBA must agree to temporarily suspend the effective date of the administrative action taken until the AUSA can become educated.

In many cases, SBA defensive litigation is neglected or given short shrift by AUSAs who are overworked. There have been several cases where AUSAs have pressed for a settlement just to be rid of the case.

There is precedent for such litigating authority. Several agencies which engage in financial and other specialized litigation like SBA have their own statutory litigating authority. These include, among others, the Overseas Private Investment Corporation, the Federal Deposit Insurance Corporation, the Securities and Exchange Commission, the TVA, the Pension Benefit Guaranty Corporation, the Commodities Futures Trading Commission, and to a limited extent with respect to debt collection, the Department of Veterans Affairs and the Farmers Home Administration.

Recommendations

Congress should amend the Small Business Act, 15 U.S.C. § 634(b) to include independent litigating authority for SBA. This authority would give SBA the option to prosecute or defend civil actions brought on behalf of or against the Agency, or where best, refer the case to the Department of Justice for handling.

No additional SBA personnel would be needed as SBA already has in place an extensive field network capable of handling a much greater percentage of its litigation in the various judicial districts in which they are located.

Additionally, the Justice Department would be relieved of the need for additional staff to prosecute and defend SBA cases.

Implications

Giving greater litigating authority to SBA counsel will increase the government's ability to meet the demand for increased resources for litigation as it will free up Department of Justice attorneys to pursue other cases without causing the government to spend more in attorney resources.

The government will benefit from the more effective use of SBA counsel who have the expertise and motivation to vigorously defend and prosecute SBA litigation.

Fiscal Impact

This recommendation involves no extra cost to the government. Approximately $3 million a year will be saved on fees paid to outside attorneys which might more than offset any additional litigating costs. Increased collateral collection will occur. Since litigation costs which might offset savings and increased collateral collections cannot be quantified at this time, the fiscal impact of this recommendation cannot be estimated.

ENDNOTE

1. 15 U.S.C. § 634(B).

SECTION III

AGENCY REINVENTION ACTIVITIES

CS 3

THE U.S. SMALL BUSINESS ADMINISTRATION'S REINVENTION EFFORTS

Summary of Agency Reinvention Effort

Reinventing the U.S. Small Business Administration (SBA) has been a priority for Administrator Erskine Bowles from the very beginning of his tenure at SBA. His first official act as Administrator was to introduce Vice President Albert Gore to a group of state small business winners at a meeting to discuss reinventing government. His commitment continues with the establishment of an internal SBA team which will operate the entire four years he is at the SBA. At a presentation before the National Small Business United and the National Association of Women Business Owners in May, 1993, Erskine Bowles described the reinvention process in the following way: "If a reinvented government is operating more efficiently, it means that small companies will be able to work more productively with that government." He went on to say, "there is no more important reason to move ahead with this than to provide a better environment in which America's entrepreneurs can continue to be the nation's job creators and innovators."

The reinvention effort at the SBA has been organized around the Administrator's philosophy that the best way to serve a customer is to listen his/her concerns. For the SBA, there are three types of customers: the small business owner, the lender, and "internal" customer -- the employee.

The information gathering component of the SBA's reinvention effort can not be overemphasized. In addition to utilizing traditional methods for soliciting input such as asking small business owners, lenders, and employees, to submit their ideas in writing to Administrator directly, he has gone one step further. This Administrator is going right to the source.

Eight cities across the country have been selected to host a three-part town hall meeting over a two day period. A meeting with small business owners takes place on the first evening. The meetings will be held in a talk show format which allows the Administrator to answer questions and hear suggestions and ideas. A meeting between the Administrator and local lenders takes place on the morning of the second day to discuss their experiences with SBA programs. The third meeting, focuses on getting input from SBA employees.

The first town hall meeting, held in Hartford, CT on July 15-16, generated numeruous ideas. Similar meetings in Los Angeles, CA, Des Moines, IA, Atlanta, GA, Portland, OR, Cleveland, OH, Houston, TX, and Denver, CO, will be held through November, 1993.

The Administrator also seized the opportunity to use his first national meeting with the SBA District Directors as a reinvention vehicle. With an agenda entitled "Reinventing SBA," the three-day long meeting provided numerous opportunities for SBA's top management to provide ideas and suggestions on ways to improve the program delivery at SBA. The hundreds of suggestions submitted at that meeting have been compiled into a report and is being utilized in the agency's reorganization plan currently underway.

In addition, a 17-member group has been established in SBA's Central Office to organize a permanent internal reinventing SBA team. Called the "Entrepreneurial SBA Team (E-SBA)," the organizing group is comprised of employees representing all grade levels and program divisions. The employees were selected, in part, for their substantial experience in SBA's field offices.

The E-SBA team has two important functions and has divided into two sub-groups. First, an outreach team has been established to develop ways to continue to involve all of SBA's customers in the reinvention process. Second, an issue team has been created to categorize the suggestions from employees, lenders and small business owners. Its goal is to ensure that each idea receives a fair an impartial review. Both teams meet regularly. The full E-SBA team meets weekly.

Specific Reinvention Projects

Five themes have emerged among the ideas and suggestions SBA has received through the reinvention process. Although a final evaluation process for individual ideas has not been officially adopted, it appears that SBA's reinvention projects will fall into the following areas:

Reallocation of Resources -- Doing more with less is not a new concept to SBA. One thing that Administrator Bowles has assured everyone is to expect less resources in Washington, less resources at the Regional Office level, and more resources in some district offices. In this time of downsizing, there is consensus among most that resources can best be utilized at the most local level where the services are delivered to the small business owner.

This is the guiding principle behind the SBA's reorganization plan.

Customer Service -- All of SBA's customers have submitted ideas on how to make SBA more "user friendly" and efficient. These suggestions run the gamut from how to best handle initial inquiries to designing new lending vehicles.

New Way of Measuring Performance -- As with many federal agencies, SBA has measured its program success by the number of people that have utilized its services. It has been recommended by small business owners, lenders, and employees alike that a more meaningful way to measure SBA's effectiveness is to link its performance to job creation and other small business indicators. This type of measurement holds SBA accountable in ensuring that SBA's programs actually assists individuals to go into and stay in business as its mission states.

Personnel -- About 40 percent of the reinvention suggestions from employees deal with some personnel matter or procedure.

Lines of Comunication -- Like in all large organizations, good communication continues to challenge even the most earnest manager. Many suggestions have revolved around improving lines of communication within and outside of the agency.

LESSONS LEARNED

Because Administrator Bowles envisions the reinvention effort to be a ongoing process at SBA, a substantial amount of effort continues to be placed on creating the best possible mechanism for how ideas submitted are considered. SBA is a very decentralized agency (10 regional offices and 66 district and branch offices). The most challenging component of the reinvention effort organizationally has been to develop an infrastructure where field staff could be not only participate by submitting ideas, but be involved in the evaluation process as well.

Currently being tested as a pilot project is an evaluation process that would incorporate field input. The procedure is as follows: An issue would be sent to the person in the headquarters office with the most hands-on working knowledge of the designated program. This process intentionally bypasses one or more levels of management who may or may not have reviewed this idea previously and had a negative opinion.

The staff person will be asked to respond with a brief "good-idea" or "bad-idea" assessment and why. They would also select two appropriate field employees-- one from a regional office and one from a district office -- to provide additional evaluations. The evaluations are returned to the E-SBA Issue Team for a final determination as to whether or not the recommendation should be forwarded to the Administrator for consideration.

SYNOPSIS

SBA's reinvention effort has short and long term goals. Many of the initial ideas and suggestions offered through this process will be incorporated into the reorganization plan slated for unveiling by the end of this fiscal year. The long range benefit is that a permanent reinvention vehicle will be in place so that good ideas and suggestions to make SBA more effective and efficient always have a forum.

Administrator Bowles understands that reinventing SBA is not merely a management exercise. He is very clear and has communicated to his staff that a more efficient and effective SBA will provide better assistance to small businesses who, in turn, will create jobs and help the families and communities in which they are located. This invigorated small business community will contribute in creating and maintaining a healthier national economy.

SECTION IV

FISCAL IMPACT SUMMARY

SMALL BUSINESS ADMINISTRATION
FISCAL IMPLICATIONS SUMMARY

CHANGE IN BUDGET AUTHORITY
Numbers in Millions

Ch. Ref.		Recommendation	Fiscal Year 1994	1995	1996	1997	1998	5-YRS	Change in FTEs
CS	20	Encourage small business lending with loan pool	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	21	Strengthen Regulatory Flexibility Act	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	22	Strengthen Minority business programs	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	23	Distribute SBA staff based on workload	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	24	Add item on business size to economic surveys	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	25	Change Microloan Program from direct to guarantee	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	26	Independent litigating authority for SBA Counsel	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	27	Establish User Fees for SBDC services	$17.0	$17.0	$17.0	$17.0	$17.0	$85.0	0
CS	29	Enforce government wide compliance of procurement laws	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
		Total, Small Business Administration	$17.0	$17.0	$17.0	$17.0	$17.0	$85.0	0

CHANGE IN OUTLAYS
Numbers in Millions

Ch. Ref.		Recommendation	Fiscal Year 1994	1995	1996	1997	1998	5-YRS	Change in FTEs
CS	20	Encourage small business lending with loan pool	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	21	Strengthen Regulatory Flexibility Act	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	22	Strengthen Minority business programs	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	23	Distribute SBA staff based on workload	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	24	Add item on business size to economic surveys	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	25	Change Microloan Program from direct to guarantee	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	26	Independent litigating authority for SBA Counsel	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
CS	27	Establish User Fees for SBDC services	$3.0	$14.0	$17.0	$17.0	$17.0	$68.0	0
CS	29	Enforce government wide compliance of procurement laws	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	0
		Total, Small Business Administration	$3.0	$14.0	$17.0	$17.0	$17.0	$68.0	0