

Comments Supporting the Proposed Increase to \$10 Million

The 21 comments in favor of the proposed rule raised a number of issues in support of a higher size standard. The most important issue discussed was the requirements contained in Federal contracts. Six commentators cited a pattern of increased Government requirements in recent years as leading to the result in which testing laboratories under the present size standard of \$6 million often cannot adequately perform on a Federal contract. These Federal Government requirements for laboratory operations include: reporting requirements, quality assurance plans, emergency contingency plans, analytical requirements, electronic data deliverable requirements, audit requirements, management costs, health and safety requirements, regulatory requirements and insurance and liability requirements. In addition, radioactive and non-radioactive hazards often required testing by environmental radiochemistry laboratories that have the licenses, procedures, insurance protection, and approvals for both types of hazardous samples. Therefore, the general belief among these commentators is that large capital and labor expenses are required for a testing laboratory to be active as a successful Federal contractor. These commentators believed that the size standard should be raised so that more Federal contracts will be set aside for small businesses, and there will be a larger pool of small testing laboratories to compete for those contracts.

Three commentators cited a recent pattern of increasing consolidation in the industry as one or more very large testing laboratories have acquired a number of smaller testing laboratories, while competing testing laboratories have gone out of business. They claimed that this trend has resulted in greater concentration in the industry, and less ability for small testing laboratories to compete for Federal contracts.

Two commentators, both large firms, supported the higher size standard because they have found it difficult to find competent small testing laboratories to meet their Federal subcontracting goals under the present size standard. A higher size standard would immediately qualify more testing laboratories as small, while permitting additional small testing laboratories to expand in size and still be qualified as small.

Finally, two commentators believed that a higher size standard would allow them to expand. These commentators

contended that the present size standard tends to frustrate growth and reduce competition.

Comments Opposing the Proposed Increase

The strongest criticism of the proposed increase focused on the claim that testing laboratories in the \$6 million to \$10 million size range are relatively successful and well capitalized compared to testing laboratories with less than \$6 million in sales. Eight of the 14 commentators opposing the proposed change asserted that testing laboratories in this size range are too successful to be considered small. They indicated that these larger testing laboratories have lower costs than smaller testing laboratories due to higher volume. They also view larger laboratories as better able to target Federal contracts. A common observation is that testing laboratories in the \$6 million to \$10 million size range have larger facilities than smaller testing laboratories, and that Federal contracts are often awarded on the basis of individual facility qualifications. Four commentators believed that a higher size standard would give significant advantages to the large, single-site testing laboratories when competing for Federal contracts.

Commentators opposing the proposed change also generally believed that there is a stagnant market for Federal contracts and that increasing the size standard in such an environment would increase competition for Federal contracts. This additional competition would have a negative impact on testing laboratories that are presently under the \$6 million size standard.

The comments opposing the proposed size standard also raised an issue regarding the performance of small testing laboratories on subcontracts awarded by large businesses in fulfillment of subcontracting goals on Federal contracts. They contended that small testing laboratories are very successful and competitive in obtaining subcontracts, and thus, a higher size standard was not needed. One comment provided data on such subcontracts awarded by several large businesses. These data indicated that small testing laboratories were able to achieve a higher proportion of subcontracts than Federal contracts.

Other commentators opposing the proposed change cited information in two key areas identified in the proposed rule as reasons supporting an increase in the size standard. First, three commentators noted that the trend toward consolidation in the industry was associated with one or more very

large companies buying out smaller, less successful, testing laboratories. These commentators recognized that there has been a shakeup in the industry, with smaller testing laboratories often unsuccessfully competing with very large testing laboratories for Federal Government contracts. Second, three commentators also contended that recent Federal Government requirements have tended to reduce the pool of small testing laboratories that can effectively bid on Federal contracts. They viewed these developments as reasons for retaining the current size standard rather than supporting an increase.

Response to Significant Issues Raised by Comments

The SBA believes that the trends in the Testing Laboratories industry and the level of small business participation in Federal contracting support a size standard higher than \$6 million and the adoption of the proposed \$10 million size standard. Since the time of the proposed rule, Federal contracting data have become available for fiscal years (FY) 2001–02. These data show small testing laboratories have increased their level of participation in Federal contracting over previous years. Small testing laboratories obtained 23.1% of testing contract dollars in FY 2002, and 29.7% in FY 2001. However, these levels remain significantly below the small business share of 44% of total industry revenues. The SBA found in a detailed review of fiscal years 2001–02 Federal testing contracts that small testing laboratories are successful in obtaining contracts of varying sizes. However, the consistent discrepancy between the Federal and industry share does lend credence to the arguments advanced by the comments supporting the proposed size standard that Federal contract requirements have become more restrictive in recent years, and that this pattern favors larger, more heavily capitalized firms. The SBA also agrees with the view that the industry has become more concentrated over time with a much greater presence of very large testing laboratories. In 1997, \$3.1 billion out of \$6.4 billion in sales were generated by testing laboratories with more than \$10 million in sales. This share, almost 50%, has probably increased significantly with the recent consolidation in the industry and the departure of small testing laboratories. The SBA believes that these patterns of more stringent contracting requirements and greater industry concentration support a higher size standard.

The SBA is aware that firms that are larger in size will often possess greater