

The Underemployment Impact of the HUB Zone Employee Definition Rule

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The Greatest Deterrent to the Goals of the HUB Zone Program

Despite the best intentions of the federal government to rectify historical economic disparities in HUB Zone communities, the employee definition rule has resulted in the underemployment of HUB Zone residents. The underemployment of HUB Zone residents means that they are employed less than full-time in jobs inadequate in meeting their economic needs. The minimal hours (40 hours per month) embedded in the employee definition rule fosters the condition of underemployment.¹ The condition of underemployment among HUB Zone residents is the greatest deterrent to the program's goal of economic development through small business creation in distressed areas.

The content of this article will describe why HUB Zone companies choose to employ residents at the minimal hours required. Further, it discusses the material and psychological impact of underemployment and its connection to the continuing depreciation of the quality of life in HUB Zone communities. Finally, the article will discuss how changes in this rule and other aspects of HUB Zone program policy can be adjusted to make real the vision of the program's architects. The HUB Zone program is not a welfare program that helps protected classes find jobs; it is a congressional mandate to identify economically distressed areas and revitalize them to health for the good of the entire American economy. This article is a call to action to be heard by the Small

¹ Source: <https://www.sba.gov/contracting/government-contracting-programs/hubzone-program/frequently-asked-questions>

Business Administration (SBA), Congress, the federal contracting community, and even HUB Zone residents themselves to correct the employee definition rule as to eliminate its underemployment impact.

HUB Zone Residents Struggle to Survive the Applicant Pool and HUB Zone Companies Struggle to Stay in Business

The HUB Zone certification is not easy to attain as it requires that 35% of a HUB Zone company's employee base reside in HUB Zone census tracts. It further requires that the company's principal office be in a HUB Zone and that the largest contingency of the employer's workforce work in that office. Once these requirements are met HUB Zone companies may only count an employee as part of their 35% employee base ratio if they can prove that the employee has received at least 40 hours in any given four-week period while employed. Finally, the company must be able to prove through federal or state issued identification that the employee lives in a HUB Zone. The SBA through audit may debar a contractor who attains the certification but fails to maintain proof that they continue to meet the certification criteria.

Small businesses covet HUB Zone certification because of the preferential treatment that they receive when seeking a procurement labeled as a "HUB Zone set-aside". Section 48 of the CFR subpart 19.1305 describes how the SBA procurement center may recommend that a federal agency contracting officer set aside an acquisition for competition restricted to a HUBZone small business. As an additional perk contracting officers for HUB Zone set asides will consider granting the contractor a sole source award if certain conditions are applicable². Given these enticements, it can be seen why being a HUB Zone certified company can be lucrative. So why are HUB Zone residents not employed full time? After contracting officers have awarded the

² <https://www.fedgovcontracts.com/chap11.pdf>

HUB Zone set aside contract, the next step is for the HUB Zone company to provide suitable personnel to perform the work. The hiring process requires a consensus between the federal agency department managers and the hiring managers for the HUB Zone company. While the company may hire the employee of their choice, the federal agency department manager has the right to accept or reject the employee for the work they have been assigned to manage. The criticality of the tasks they manage deter department managers from hiring employees or even reviewing the resume of anyone lacking the relative job experience to successfully work in their department on day one. Most department managers working for federal agencies such as the Department of Defense and NASA are tasked with missions critical to national security. For example, a department manager may be tasked with assuring the correct propulsion of a system, the timeliness of a piece of equipment arriving on location for the International Space Station, or the proper ventilation of a space suit. For this reason, professional recruiters I interviewed absolutely hate it when a HUB Zone company says that a position must be filled with a HUB Zone employee. “When you are given a job description and you are limited to providing applicants from historically underutilized business zones you quickly gain a reputation for representing an unqualified and subpar workforce.³” To circumvent the challenge of their employees being turned down by department managers, many HUB Zone contractors have elected to use the minimalist hours rule to maintain their certification while hiring any candidate their federal agency prefers. Some HUB Zone companies choose to hire employees for as little as 40 hours per month and pay them as little as minimum wage to perform off-contract menial tasks just to maintain their certification requirements. When HUB Zone companies engage in this activity underemployment of HUB Zone residents ensues.

³ Throughout the article references will be made to interviews/experience with professional recruiters, project managers and employees in the HUBZone Aerospace Contractor Industry with the author. These sources prefer that their personal information remain anonymous.

It is true that per capita many HUB Zone applicants lack the relative experience for jobs supporting federal agencies on day one. However, this does not always mean that they can't do the job. In many cases it has meant that they have not been afforded the opportunity to gain the needed experience. The challenge is finding the opportunities. I know this personally as a Human Resources Manager with over a decade of experience in staffing positions for HUB Zone set asides all over the country. I have found my best candidates by walking through HUB Zone communities and having conversations. For example, I met a gentleman who was driving a security cart at a commercial property in a HUB Zone community. This man, in his upper 60's, well-spoken and professional in appearance, joined our HUB Zone community job training program. In reviewing his resume, I found that he had an MBA. After checking his background and legitimizing his education and a completely clean criminal record, I sat with him to find out why he was driving a security cart. It was very simple, when he was younger, his competition were white males with the same degree who were more culturally acceptable to financial firms at that time. As he grew older, everything he had learned was considered outdated. There is nothing wrong with driving a security cart, however, when a person goes to school and achieves an MBA from one of the top business schools in the State it is certain that driving a security cart was not his goal. This is an example of a person who could perform any number of jobs in accounting or finance but could not be hired onto a contract because he did not have the relative work experience. I was able to hire this gentleman but only at 20 hours a week in a non-contract position to assist in meeting the company's diminishing HUB Zone numbers. Absent a billable contract position, his position is a liability that could be eliminated with the next employee roster adjustment or a material decline in the company's revenue.

HUB Zone companies cannot bill the government for employees performing tasks unallowable to the contract. This means that companies hiring employees in non-contract positions are losing money in an attempt to maintain their certification. Ultimately this results in many HUB Zone companies leaving the program. A report on setasidealerts.com reveals that the number of small businesses certified as eligible for HUBZone federal set-aside contracts has fallen dramatically. There has been a 70% decline in Wisconsin, a 67% drop in Pennsylvania, with Alabama, Idaho and Kentucky all reporting decreases of 50% or more. Overall, the total number of HUBZone firms has fallen by 22% in the last five years, from 6,056 firms to 4,750 firms.⁴

The Impact of Underemployment on HUB Zone Communities

A 40 hour per month schedule at minimum wage will not lift anyone above the poverty line, empower their financial impact as a consumer, or much less finance their opening a new business in their community. This means that the HUB Zone program is not achieving its goal or alleviating the conditions for which it was created. It is necessary to understand the conditions in HUB Zone communities in order to understand the importance of correcting the current rules. I grew up in a HUB Zone community and understand the impact of unemployment and underemployment. HUB Zone communities by definition have fewer businesses and those they do have are often subpar. Many of these communities are food deserts, urban areas with underemployed and/or unemployed residents with limited access to affordable and nutritious food. Simply put, finding a grocery store in most HUB Zone communities is a challenge. One can drive for several miles within a census tract and find few food options other than fast food. The closest thing within walking distance with some semblance of a grocery store are the corner gas stations. The food offered at the gas stations are processed foods that inevitably create

⁴ Source: <http://www.setasidealertnews.com/in-depth-reports.html>

obesity in the youngest of HUB Zone residents. When you do find a grocery store, the lights are dim or blown out, the floors are cracked and need replacing, and the posture of the workers emulate the depreciation of their environment. In the Houston HUB Zone communities where I grew up there is an absence of the healthy restaurants, vitamin stores, and coffee shops full of bright faces and conversation found in Uptown and Midtown Houston.

Fewer businesses, underemployment, and unemployment translate into lower property value and taxes. Thus, the schools are dilapidated, and after-school programs are few. Inherently such conditions lead to crime, drug use, and low expectations for what can be achieved among residents. A program mandated by the federal government that targets the revitalization of these areas is one of the most phenomenal achievements by Congress. The HUB Zone program is phenomenal because its intention is blind financial equity. Every community which is found economically distressed is targeted regardless of its demographic makeup. It is phenomenal because it is a self-correcting measure by our government to seek and find forgotten citizens in this Country and offer them an opportunity at the American dream. This program properly executed could change the lives and trajectory of people that live under these conditions. Each of us who have benefited from the government contracting industry have a duty to assure the full realization of this program. We can do this by changing the employee definition rule to assure meaningful employment of HUB Zone residents.

The SBA Proposes New Rules to Address Employee Definition Concerns⁵

The SBA is considering revising the definition of an employee to raise its requirement from 40 hours per month to 20 hours per week. This change has come about because of concerns that the

⁵ <https://www.federalregister.gov/documents/2018/10/31/2018-23285/small-business-hubzone-program-government-contracting-programs>

40 hours per month requirement is not enough to stimulate the revitalization of HUB Zone communities. The SBA is requesting comments on whether they should count only full-time employees or full-time equivalents. This request is part of the reason that this article and your support of the remedies it contains is important. The SBA has created a window of opportunity for itself to be educated by federal agencies, contractors and citizens on the needs of the HUB Zone community. Everyone should comment, especially HUB Zone residents. If this proposed rule is passed, HUB Zone residents would see some relief as constituents who had been primarily offered underemployment opportunities. Unfortunately, according to the U.S. Department of Health & Human Services, the poverty level for a household of four is an annual income of \$25,750. Therefore, even at 80 hours per month multiplied by \$10.00 per hour (above minimum wage but consistent with many wage-determined entry-level jobs) a HUB Zone resident would only make \$9,600 per year. So, while the recognition of the SBA that the concerns outlined in this article are material, their remedy remains anemic in establishing true economic revitalization of HUB Zone communities and resolving the issue of underemployment. The mission of the HUB Zone program requires a commitment to employing HUB Zone employees at a rate of pay and number of hours that fosters their being financially capable of being contributors to their community's economic development.

A second proposed rule change may add to the problems described in this article. The SBA has proposed to remove the reference to primary residence and eliminate the requirement that an individual demonstrate that they have and will continue to live in a HUB Zone during the course of their employment. The former rule required contractors to maintain records that their HUB Zone employees continue to live in a HUB Zone community in order for them to be counted in the 35% ratio. Under the proposed rule, residency will be defined as living in the HUB Zone for

at least 180 days immediately prior to the date of application or date of recertification, as applicable. Going forward the employee may be counted by the company as a HUB Zone employee even if the employee moves. While this will provide relief to HUB Zone company staffing concerns, it will not motivate HUB Zone employees to stay and revitalize their communities. This new rule now being proposed allows for an influx of applicants who could lease in a HUB Zone community for six months to attain employment and then move out as soon as they are hired or their company recertifies. The employer would have no motivation to maintain a long-term population of HUB Zone residents that work and live in the HUB Zone community. Thus, the community would not really see any material advancement or revitalization. The value of the HUB Zone resident's employment, already in peril, would be devalued as a company may hire temporary employees to meet their numbers and release them after recertification. The rule also makes the SBA's ability to effectively audit HUB Zone company rosters and contracting officers' ability to investigate disputes over awards much more difficult because of the constant movement of employees.

Changing the Game

The test of our progress is not whether we add more to the abundance of those who have much; it is whether we provide enough for those who have too little.

-Franklin D. Roosevelt

The purpose of the Historically Underutilized Business Zone (HUB Zone) Program is to increase employment opportunities, investment, and economic development in distressed urban and rural communities by providing federal contracting opportunities to qualified HUB Zone small businesses.⁶ Who is ultimately responsible for the success or failure of the HUB Zone program? The SBA is responsible for certifying eligible firms as qualified HUB Zone small businesses and conducting program examinations of eligibility status, protests, and decertifying firms who don't meet the eligibility requirements. Acquisition agencies which I have referred to as federal agencies are responsible for achieving annual procurement goals for HUB Zone set asides. However, both of these entities answer to a common creator, Congress. In 2007, the Senate Committee on Small Business and Entrepreneurship ranking member Olympia J. Snowe (R-ME) and Senator Kit Bond (R-MO) requested that the Government Accountability Office (GAO) review the HUB Zone program. This was meaningful because Senator Bond was instrumental in the program being created. In 2007, they requested examination of the following by the GAO⁷:

- Examine the barriers that inhibit small business from utilizing the HUBZone program;
- Analyze the obstacles that federal agencies are encountering in implementing the HUBZone program to award contracts to certified HUB Zone firms;

⁶ https://www.sba.gov/sites/default/files/sops/serv_sops_8006.pdf

⁷ <https://www.sbc.senate.gov/republican/HTML/news/07.17.07%20Hubzone%20Review.htm>

- Recommend legislative or regulatory proposals to increase small business utilization of the HUB Zone program, as well as to mitigate any implementation difficulties facing federal agencies;
- Propose recommendations to ensure that economically depressed areas of the country are properly classified as HUB Zones.

Since 2008, the GAO has made 11 recommendations to improve the HUBZone program⁸. To date, the SBA has implemented seven of these recommendations, not implemented two and is in the process of implementing the other two. The oversight by the architects of the HUB Zone program reflect a good faith effort to enhance overall effectiveness. Unfortunately, the oversight and the recently proposed changes have not and will not impact the issue of underemployment. Therefore, in meeting with 10 HUB Zone company project managers this April, I asked for the most significant challenges in remaining HUB Zone-certified which have led to the underemployment of HUB Zone residents⁹. The unanimous answer was HUB Zone employees moving out of the HUB Zone after employment. None of the aforementioned GAO activities nor steps taken by the SBA have addressed as a cause for the underemployment concern. The impact when a HUB Zone employee becomes non-HUB Zone is catastrophic to a company because they must subtract that HUB Zone employee and in turn count them as a non-HUB Zone employee decreasing their certification ratio. This quantitative impact leads to companies under-employing a larger number of HUB Zone residents at nominal hours in order to maintain their HUB Zone certification. In retrospect, our remedies must not only address the underemployment of residents

⁸ <https://www.gao.gov/assets/690/683096.pdf>

⁹ Comments attained in a meeting at the Bay Oaks Country Club with 10 Project Managers representing HUB Zone set asides 04//30/2019

due to gaps in employment experience but also underemployment created by employees moving out of the HUB Zone.

Changing the Game Step One

We will begin our remedies discussion with the exodus of full-time HUB Zone employees from their communities after employment. To rectify this concern, it is proposed that Congress create a budget for the HUB Zone program that awards annual bonuses to full-time HUB Zone employees who remain in the HUB Zone. HUB Zone employees want a better quality of life for themselves and their families. This quality of life need not drive them away from their HUB Zone communities. HUB Zone employees should receive financial incentives upon the renewal of their lease or the purchase of a home in a HUB Zone. These incentives should be part of the fringe benefits cost in set-aside contracts billable to the government. Annual bonuses for new/renewed leases should be reflective of the first and last month rent. 10% of the closing cost of a new home should be distributed to HUB Zone employees on the closing date. As an incentive not to sell their homes, HUB Zone employees should be eligible for a 10% yearly stipend to assist in paying for property tax costs. Eligibility for these benefits will be contingent on the HUB Zone employee providing proof of residency and patronage in the HUB Zone communities where they live.

I began testing these strategies over a decade ago at my company and have seen a 85% reduction in HUB Zone residency turnover. These initiatives have allowed my company to expand its portfolio to become one of the largest HUB Zone contractors in the country because we have been able to maintain our roster ratio. We have done this without funding from the government as part of corporate strategy; however, funding could make this activity much easier for smaller or newer HUB Zone companies. Funding for these initiatives should be part of the budget for

every HUB Zone set aside. This action will assure that employees are remaining in communities long enough to make a financial impact.

Changing the Game Step Two

Changing the certification rule from an employer assuring that 35% of its employees are HUB Zone residents to a formula in which 35% of an employer's payroll must be paid to HUB Zone residents; will completely change the game. This action assures that employers hire HUB Zone employees at a number of hours and rate of pay that is material to the income statement of the company. More importantly, it will prevent the underemployment of HUB Zone residents because certification will no longer be based on the number of HUB Zone employees hired but the amount of payroll distributed to HUB Zone employees.

To ease the burden of HUB Zone companies finding qualified candidates to fill their positions under this new rule it is recommended that Congress mandate that all HUB Zone employees on set aside contracts be allocated to the HUB Zone company receiving the set aside. Implementing this strategy means that all employers on a contract are actively recruiting for HUB Zone residents even if they are not a HUB Zone company. In November of 2018, our implementation of this strategy produced a 12-employee turnaround at our New Mexico facility increasing our HUB Zone ratio overnight. 12 employees working for the prime contractor voluntarily switched companies after realizing that their HUB Zone residency could positively impact the certification of the HUB Zone company on the contract. The prime contractor received 12 non-HUB Zone employees from the HUB Zone company in return. This initiative works only when there is a teaming agreement in place where all contractors provide comparable benefits and pay to their employees so that employees experience minimal fringe benefit impact.

Changing the Game Step Three

HUB Zone residents who don't have experience should immediately be viewed as fresh-out of college students rather than dismissed as not valuable to the federal agency mission. If we take age out of the equation, HUB Zone residents whose skills have been underutilized are really candidates fresh from college who need the opportunity to gain experience. How do we create jobs for these mature "fresh-out" candidates? Long time federal contract employees, who have not been promoted or transferred, often achieve skills and wages superior to their private sector counter-parts. The jobs they hold are often administrative and entry-level in nature representing opportunities for HUB Zone residents entering the industry for the first time. It should be mandated in HUB Zone set aside contracts that project managers engage in career analysis and seek to promote workers with 5 or more years of experience in the same job to the next level to make room for employment of HUB Zone candidates into entry-level positions. These full-time entry level positions far surpass many of the current jobs HUB Zone employees are offered and will reduce their underemployment.

Final Thoughts

This has been a healthy and candid discussion about the HUB Zone program focused specifically on the concern of HUB Zone resident underemployment. The reason for their underemployment is the attempt of HUB Zone companies to maintain their certification under the current employee definition rule. The rule as currently written and even with proposed modification placed on the table recently, allows employers to hire HUB Zone residents at a number of hours and pay below the poverty level. The underemployment of HUB Zone residents undermines the mission of the program to revitalize HUB Zone communities through injection of business and patronage. The challenge of hiring HUB Zone residents into positions material to their financial upliftment is

often the lack of skills they possess relatively to their occupational counterparts. Finally, HUB Zone employees who have achieved full-time status often move out of the HUB Zone leaving companies scrambling to meet their HUB Zone goals resulting in their increasing underemployment initiatives.

Though these concerns are challenging, the success of the HUB Zone program is far too important to the revitalization of American communities to be ignored. I have therefore presented proven strategies that employed through regulation by Congress and supported by the SBA, federal agencies and contractors will remedy the underemployment concerns. The recommendations require redefining the employee definition rule so that it is material to sustained community residency, equity in payroll distribution, and career development. These changes will focus employers and federal agencies on meaningful strategies measured by economic impact rather than the number of residents hired. Together with a strong educational rollout that fosters an understanding of why the HUB Zone Program is important, we can expect a decrease in the underemployment concern of HUB Zone residents. Readers of this article are invited to respond to the SBA's call for comments on the proposed rule and the HUB Zone program in general at hubzone@sba.gov.

Honor's Pledge

"On my honor, I submit this work in good faith and pledge that I have neither given nor received improper aid in its completion."

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