

August 5, 2022

**Comments of the Washington Lawyers' Committee for Civil Rights, the Collateral Consequences Resource Center, and 24 additional organizations on the Small Business Administration's Proposed Rule amending 13 CFR 121, 125 and 128.**

**Re: Veteran-Owned Small Business and Service-Disabled, Veteran-Owned Small Business—Certification, 87 Fed. Reg. 40141**

Dear Administrator Casillas Guzman:

Access to Small Business Administration programs is essential for many small businesses, particularly those in developing communities. Yet, encounters with the criminal law system far too frequently exclude people in these communities from access to these essential programs, particularly Black and other business owners of color. It is with this concern in mind that the undersigned organizations offer the following comments on the Small Business Administration's recently released proposed Rule amending 13 CFR 121, 125 and 128, which would govern the Veteran-Owned Small Business and Service-Disabled, Veteran-Owned Small-Business concerns participation in the Veterans Certification program ("Proposed Rule").

The proposed removal of categorical exclusions for those on parole, probation, or who are incarcerated is an important step. However, the Proposed Rule's continued use of "good character," as well as the absence of any substantive or procedural criteria to guide decision-making, will continue to deny certification to individuals with significant business ability who otherwise could effectively and responsibly perform federal government contracts and contribute to the development of their communities.

**The Importance of Encouraging Small Business Owners with a History of Arrest or Conviction**

People with a record are subject to a myriad of barriers in seeking to reintegrate into society, including bank lending policies, housing, employment, licensing, education, voting, and other areas. Entrepreneurship is particularly important for people with an arrest or conviction record because they are often unfairly shut out of employment with others due to, among other issues, overly broad criminal background checks, incorrect cultural assumptions made by employers, and vague occupational licensing standards.<sup>1</sup> Formerly incarcerated people have a rate of unemployment nearly five times of those without arrest or conviction records, regardless of the state of the labor market.<sup>2</sup> Further, veterans are disproportionately represented among those with

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<sup>1</sup>Justin Sabley, *People leaving prison have a hard time getting jobs. The pandemic has made things worse* (Mar. 31, 2021), <https://www.pbs.org/newshour/economy/people-leaving-prison-have-a-hard-time-getting-jobs-the-pandemic-has-made-things-worse>

<sup>2</sup> Sabley, *supra* n.1; Lucius Couloute & Daniel Kopf, *Out of Prison & Out of Work: Unemployment Among Formerly Incarcerated People*, PRISON POL'Y INITIATIVE (July 2018), <https://www.prisonpolicy.org/reports/outofwork.html>.

a criminal record. Veterans make up 7.9% of the state prison population and 5.3% of the federal prison population,<sup>3</sup> and nationally representative surveys have found that almost a third (31.1%) of veteran respondents had been arrested and booked, a rate significantly higher than among non-veteran respondents (18%).<sup>4</sup>

A significant number of people with arrest or conviction history have established their own small businesses. According to a recent study by the RAND Corporation, approximately 3.8% of small business owners nationwide have an arrest or conviction record.<sup>5</sup> This percentage corresponds to approximately 1.1 million small business owners.

Not only do businesses owned by formerly incarcerated people open the doors to economic opportunity for the owners, but these businesses also tend to be more willing to hire employees with a record, thereby creating jobs for others who may otherwise be locked out of the workforce. Small business ownership provides critical pathways to economic opportunity for many, including individuals with records.

As a result, the SBA's approach to integration or exclusion of small business owners with arrest and conviction records, including business owners who are veterans, is of paramount importance. Accordingly, we urge the SBA to adopt a data-based, transparent, and objective method of assessing whether a business owner's criminal record reflects adversely on their responsibility to perform a contract, as opposed to some amorphous idea of their "good character." In doing so, the SBA may find helpful the work of the many states legislatures that in recent years have reformed their professional licensing regulations to eliminate vague "good moral character" standards that invite unwarranted and invidious discrimination.<sup>6</sup>

### **The Proposed Rule Rightfully Eliminates Categorical Exclusions for Individuals in Prison, or on Parole or Probation**

The Proposed Rule takes the correct approach by eliminating categorical barriers to certification for business owners who are on parole, probation, or who are incarcerated.

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<sup>3</sup> U.S. DEPARTMENT OF JUSTICE, *Veterans in Prison: Survey of Prison Inmates 2016* (March 2021), available at <https://bjs.ojp.gov/content/pub/pdf/vpspi16st.pdf>.

<sup>4</sup> Timko C, Nash A, Owens MD, Taylor E, Finlay AK. *Systematic Review of Criminal and Legal Involvement After Substance Use and Mental Health Treatment Among Veterans: Building Toward Needed Research*. SUBST ABUSE. 2020 Feb 24;14:1178221819901281. doi: 10.1177/1178221819901281. PMID: 32132821; PMCID: PMC7040926, available at <https://www.ncbi.nlm.nih.gov/pmc/articles/PMC7040926/>

<sup>5</sup> Bushway, Shawn D., Dulani Woods, Denis Agniel, and David Abramson, *The Prevalence of Criminal Records Among Small Business Owners*. Santa Monica, CA: RAND CORPORATION, 2021. [https://www.rand.org/pubs/research\\_briefs/RBA1295-1.html](https://www.rand.org/pubs/research_briefs/RBA1295-1.html).

<sup>6</sup> See, e.g., Fair Chance Employment and Occupational Licensure: A National Survey, Collateral Consequences Resource Center, Feb, 24, 2022, <https://ccresourcecenter.org/2022/02/25/fair-chance-employment-and-occupational-licensure-a-national-survey/>

Specifically, the Proposed Rule will “eliminate consideration of whether an individual who is currently incarcerated, or on parole or probation owns or controls and applicant concerns in determining whether the applicant possesses good character and qualifies as a VO SBC or SDVO SBC.” Proposed Rule at Fed. Reg. 40142.

Categorical exclusion of individuals who are incarcerated, or on probation or parole, imports the biases and disparities of the criminal law system into the economic realm, erecting hurdles to reintegration and perpetuating inequality. According to the U.S. Department of Justice Bureau of Justice Statistics, an estimated 3.9 million adults, or 1 in 66 adult U.S. residents, were under parole or probation at yearend 2020.<sup>7</sup> The racial disparities in incarceration, parole and probation nationwide are stark. While Black people comprise 13% of the U.S. population, in 2020 they were 21% of those on probation and 28% of those on parole.<sup>8</sup> Incarceration rates across the USA are similarly skewed along race, with Black Americans incarcerated at more than five times the rate of white people.<sup>9</sup> One-third of Black American men have a felony conviction,<sup>10</sup> and one in three Black men born today can expect to be incarcerated in his lifetime.<sup>11</sup>

The undersigned organizations support the SBA’s Proposed Rule insofar as it removes categorical exclusion of individuals who are in prison, or on probation or parole. Categorical exclusions do not support the SBA’s stated goals of assessing individual business owners’ responsibility and integrity. The undersigned organizations are not aware of any evidenced-based justification relating to economic responsibility and contracting integrity that would justify an across-the-board exclusion of businesses solely because one of their owners happens to be on probation or parole or in prison. As noted in the next section, the eligibility requirements of the Proposed Rule apply to all “[i]ndividuals having an ownership or control interest in certified businesses,” including part owners as well as sole proprietors. Any automatic exclusion of a business based solely on the fact that one of its part-owners has an open criminal case would seem hard to defend on any ground related to business operations.

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<sup>7</sup> U.S. Department of Justice, Probation and Parole in the United States 2020 (Dec. 2021), <https://bjs.ojp.gov/content/pub/pdf/ppus20.pdf>

<sup>8</sup> *Id.*

<sup>9</sup> *Criminal Justice Fact Sheet*, NAACP, <https://www.naacp.org/criminal-justice-factsheet/> (last visited June 15, 2020).

<sup>10</sup> *Race & Justice News: One-Third of Black Men Have Felony Convictions*, SENTENCING PROJECT (Oct. 10, 2017), <https://www.sentencingproject.org/news/5593/>.

<sup>11</sup> *An Unjust Burden: The Disparate Treatment of Black Americans in the Criminal Justice System*, VERA INSTITUTE FOR JUSTICE, (May 2018), <https://www.vera.org/downloads/publications/for-the-record-unjust-burden-racial-disparities.pdf>

## **The Proposed Rule’s Vague “Good Character” Standard Invites Arbitrary, Inconsistent and Unjust Decisions**

Despite its elimination of categorical exclusions for certain categories of arrest and conviction records, the Proposed Rule nevertheless utilizes an open-ended and potentially invidious test to determine eligibility for certification, requiring that any individual having an ownership or control interest “*must have good character.*” See Proposed 13 C.F.R. § 128.201(b)(Emphasis added). The Proposed Rule extends well beyond the existing rule in providing no specific guidance as to what may be required to establish “good character” (or more likely what demonstrates a lack of “good character”).<sup>12</sup> Nor does it specify how these character determinations will be made.

The preamble to the Proposed Rule hints at what this “good character” determination may involve:

“Whether an individual involved with the applicant is currently incarcerated, or on parole or probation is a responsibility issue, and whether a concern possesses the responsibility to perform a contract is a contract specific issue, not an underlying eligibility issue. SBA views the issues as to whether the concern has *the necessary integrity to perform a contract* in the same way as it does questions relating to whether the concern has the necessary financial wherewithal, capacity or tenacity, and perseverance to perform a contract. All are responsibility issues determined by a contracting officer relating to a specific contract.” (Emphasis added).

This explanation makes clear that individual contracting officers are permitted to consider a business owner’s criminal history as a matter of “responsibility,” and specifically whether the business owner has “the necessary integrity to perform a contract.” Like “good character,” the concept of “integrity” is a moral concept, which is ripe for the injection of bias.<sup>13</sup>

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<sup>12</sup> The preamble to the Proposed Rule states that the SBA considered adopting additional eligibility requirements found in other SBA programs, such as those applicable to the 8(a) program set forth in § 124.108, but decided instead, “for continuity purposes . . . to adopt the additional eligibility requirements directly from 38 CFR part 74.” Proposed Rule at Fed. Reg. 40142. But the definition of “good character” in 38 CFR part 74 is both definite and specific, extending not just to individuals in prison, or on parole or probation, but also to individuals who have been suspended or debarred pursuant to general federal rules on non-procurement, and to individuals who have been “formally convicted” of any crime that might be grounds for debarment and only “during the pendency of any subsequent legal proceedings.” See 38 C.F. R. § 74.2(b). This limited definition of “good character” in §74.2(b) is nowhere in evidence in the Proposed Rule.

<sup>13</sup> “Good character” tests have a long and problematic history in the United States, from use in immigration proceedings to occupational licensing. See, e.g., Deborah L. Rhode, *Virtue and the Law: The Good Moral Character Requirement in Occupational Licensing, Bar Regulation, and Immigration Proceedings*, LAW & SOCIAL INQUIRY (2017), [https://law.stanford.edu/wp-content/uploads/2017/11/Rhode-2017-Law\\_26\\_Social\\_Inquiry.pdf](https://law.stanford.edu/wp-content/uploads/2017/11/Rhode-2017-Law_26_Social_Inquiry.pdf) (“in the era of mass incarceration and widespread racial bias in the criminal justice system, such character exclusions should be a matter of substantial public concern.”)

The Proposed Rule contains no guidance, criteria, factors, or metrics to cabin the discretion of contracting officers in determining whether an individual possesses, or lacks, “the necessary integrity” to constitute “good character.” Nor does the Proposed Rule spell out the process for such a determination. Such a lack of criteria and process could undermine the removal of categorical exclusions referenced above, and extend disqualifications to a range of other criminal records.

Left with a myriad of choices, contracting officers may look to the “good character” standards in other SBA programs, including the 8(a) contracting program, which still exclude those on probation, parole, and incarceration, thereby undoing the progress that SBA has achieved by eliminating these exclusions. The 8(a) program’s “good character” provision also sweeps broadly to potentially exclude many types of closed criminal cases, and the “good character” provisions in SBA lending programs under 7(a) of the Small Business Act are even more exclusionary. In the absence of guidance in this rule, contracting officers may well look to “good character” standards from other programs that the SBA did not intend to apply to the Veterans Certification Program; or they may even develop and apply their own. A full delegation of unbounded discretion invites arbitrary, inconsistent, and unjust results.

The absence of criteria makes it impossible for small business owners with criminal records to know how to maximize their chances of certification, understand how their application will be evaluated, and predict the likelihood of certification. The opaque “good character” test makes it likely that people will be deterred from using SBA’s program, instead of incentivized to take advantage of certification and set-aside contracting opportunities as intended by the statute. Those who do take advantage will have to find their way through a black-box process through trial and error.

It is possible that SBA intends to develop criteria for “good character” determinations in forthcoming Standard Operating Procedures (SOPs), after implementation of a final rule. But the criteria and process for determining “good character” should go through notice and comment, and they should not be unilaterally developed by the SBA without opportunity for public input. We note that the “good character” criteria for the 8(a) contracting program are contained in a rule, and as long as this program also contains this measure the particulars ought also to go through notice and comment rule-making. Because “good character” is a determination that ultimately determines the substantive rights of a small business owner, that is whether they can be certified for certain contracts or obtain certain loans, it is important for small business owners and other relevant stakeholders to give their input to the agency.

### **The Proposed Rule is Inconsistent with Other SBA Policies Related to Evaluating A Record of Arrest or Conviction**

The SBA’s disjointed approach to “good character” determinations in its various programs is evident when this Proposed Rule is compared to the rules and SOPs in other programs the agency administers. For example, the SBA’s 8(a) business development program requires that small businesses possess “good character,” and while its criteria are still somewhat opaque, contains the most detailed articulation of SBA’s processes for making “good character”

determinations.<sup>14</sup> On the other hand, SBA’s Historically Underutilized Business Zones (HUBZone) program, which helps small businesses gain preferential access to federal procurement opportunities similarly to the Veterans Certification program, commendably does not appear to contain a “good character” requirement at all.<sup>15</sup> Nor does SBA’s Women-Owned Small Business Federal Contract Program have such a requirement.<sup>16</sup> Relatedly, the SBA’s 7(a) loan program requires a “good character” determination for business owners with certain types of arrest and conviction records, but it apparently lack both criteria and procedures for making those determinations.<sup>17</sup> Against this backdrop, the SBA’s Proposed Rule raises concerns of inconsistency with other related SBA programs.

## **Conclusion**

The SBA should not proceed in an opaque, arbitrary manner. While the undersigned organizations applaud the removal of categorical exclusions for people who are incarcerated, on probation, or on parole, the open-ended “good character” standard is vague and potentially unfair to business owners with a record. We urge the SBA to abandon entirely a “good character” test for contractor responsibility, and to take an evidence-based approach to determining the relationship (if any) of criminal history to the performance of contracts, both as a general matter and in particular cases. Promulgation of clear standards and procedures in a formal rule will serve the interests of both the SBA and applicants for certification, as well as the national interest in reintegration of justice-affected individuals.

In this effort, SBA could look to recent state reforms in occupational and professional licensing statutes, in which states have rooted out similarly vague statutory terms such as “good moral character” or restrictions applicable to crimes of “moral turpitude.”<sup>18</sup> Instead of using such ill-defined terms, licensing reforms have required assessment of candidates on a case-by-case basis guided by clear standards and processes that examine whether, among other things, a

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<sup>14</sup> See 13 CFR 124.101; see also SOP 80 05 5, available at [https://www.sba.gov/sites/default/files/files/SOP\\_80\\_05\\_5\\_\\_1.pdf](https://www.sba.gov/sites/default/files/files/SOP_80_05_5__1.pdf)

<sup>15</sup> See 13 CFR 126. The undersigned organizations have searched for any Standard Operating Procedures might govern the HUBZone or WOSB programs that contain a “good character” requirement but have not found any. We have also been unable to identify any published SOP that applies to these programs.

<sup>16</sup> See 13 CFR 127.

<sup>17</sup> Through a series of FOIA requests, the Washington Lawyers’ Committee for Civil Rights has learned that the SBA lacks specific criteria, guidance, metrics, or factors to determine the “good character,” of loan applicants of the SBA 7(a) loan program. In addition, while SBA made 907 “character determinations” in 2020-21 for applicants for 7(a) loans, the agency does not track how many of these decisions resulted in a determination that the individual has “good character” so as to be eligible for a loan, and how many resulted in a determination that the individual lacks “good character” and is therefore ineligible.

<sup>18</sup> See *Fair Chance Employment and Occupational Licensure: A National Survey*, *supra* note 4.

conviction is directly related to the occupation or profession, how much time has passed since the conviction, and evidence of mitigating circumstances and subsequent rehabilitation. Denial of a license must in many cases be based on a demonstrated public safety risk. The reforms have also promoted transparency by providing clear guidance to license applicants regarding potential grounds for disqualification, permitting appeal and reconsideration processes which are also guided by transparent metrics.<sup>19</sup>

In sum, instead of relying on an undefined and potentially invidious “good character” test, the undersigned organizations urge SBA to adopt an evidence-based, transparent, and objective method of assessing the intersection between criminal record and effective contract performance.

Respectfully submitted,

The Washington Lawyers’ Committee for Civil Rights and Urban Affairs

The Collateral Consequences Resource Center

Alabama Justice Initiative

Georgia Justice Project

Illinois Alliance for Reentry & Justice

Justice and Accountability Center of Louisiana

Legal Action Center/National H.I.R.E. Network

LIFELine to Success

Main Street Alliance

Motherhood Beyond Bars

National Association of Criminal Defense Lawyers

National Community Reinvestment Coalition

National Incarceration Association

NewLife-Second Chance Outreach

Ohio Justice and Policy Center

REDF

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<sup>19</sup> *Id.* This report describes influential models recommended by national organizations with differing political perspectives, the National Employment Law Project and the Institute for Justice.

Reform Georgia

RestoreHER US.America

Safer Foundation

The Centre for HOPE LLC

The Leadership Conference on Civil and Human Rights

The National Council for Incarcerated and Formerly Incarcerated Women and Girls

The Ordinary People Society – Prodigal Child Project

The Public Interest Law Center

Tzedek Georgia

Women on the Rise