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Compliance with Subcontracting Plan Requirements

Statement of
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Committee on Small Business
United States House of Representatives

COMPLIANCE WITH SUBCONTRACTING PLAN REQUIREMENTS

SUMMARY OF STATEMENT BY
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GAO reviewed how well the General Services Administration, the Department of Energy and the Department of the Navy are complying with Section 211 of Public Law 95-507 by examining contract awards and modifications made in 1985 and 1986. This statute requires that large federal contracts, with certain exceptions, contain a plan providing for the maximum practicable utilization of small and small disadvantaged businesses as subcontractors. GAO also reviewed compliance with this requirement by public utility companies providing service to the government with special emphasis on utility services acquired by GSA, Energy, and the Department of Defense.

GAO found that:

-- Almost a third of the contract actions examined at Navy that did not contain a subcontracting plan did not have a justified reason for lacking a plan. This compares to 2 percent of the contracts without a plan at GSA and 6 percent at Energy.

-- At least 23 public utility companies provide service to federal agencies but have declined to enter into formal, written contracts with the government. GAO believes that these companies are nonetheless subject to the requirements of Section 211 of Public Law 95-507.

-- When utility services are obtained under contract, compliance with the requirement for a subcontracting plan varies widely. All GSA utility contracts that should have had plans were in complete compliance. Several instances of noncompliance were noted with Energy's utility contracts. At the Department of Defense, it does not appear that any utility contracts contain subcontracting plans because procurement staff are using outdated guidance.

Mr. Chairman and Members of the Committee, it is a pleasure to appear before you today to discuss our reviews of the compliance with statutory subcontracting plan requirements at certain government agencies. The Committee requested us to review the compliance of the General Services Administration (GSA) and the Departments of Energy and the Navy with the statutory requirement that, with certain exceptions, large federal contracts contain subcontracting plans for the maximum practicable use of small and small disadvantaged businesses. Our report on the results of that review (GGD-88-83, May 24, 1988) is being released by the Committee today.

In June of last year the Committee made another request and asked us to provide information and legal opinions on the compliance with federal subcontracting requirements of public utility companies providing service to the government, with particular emphasis on utilities acquired by GSA, Energy and the Department of Defense. These agencies purchase more utility services than any other federal agencies. Our testimony today will highlight our recent report to the Committee and also deal with the related issues and questions raised by the Committee concerning public utilities.

REQUIREMENTS FOR SUBCONTRACTING PLANS

As you know, Section 211 of Public Law 95-507, enacted on October 24, 1978, requires that, with certain exceptions,

contracts and contract modifications awarded by federal agencies that exceed $500,000, or $1 million in the case of construction contracts, contain a subcontracting plan providing for the maximum practicable utilization of small and small disadvantaged businesses.

Subcontracting plans, which are prepared by contractors subject to the review and approval of the agency awarding the contract or modification, must contain certain provisions such as:

-- separate percentage goals for using small and small disadvantaged businesses as subcontractors, and

-- assurances that the contractor will require all subcontractors (except small businesses) that receive awards in excess of $500,000 ($1 million for construction subcontracts) to also prepare and implement a subcontracting plan.

Subcontracting plans are not required for contracts

-- with small business concerns,

-- for personal services,

-- to be done entirely outside the United States, and

-- where the contracting officer certifies that no subcontracting opportunities exist.

Failure to comply in good faith with the requirements of the subcontracting plan can be considered a material breach of contract.

COMPLIANCE WITH SUBCONTRACTING PLAN REQUIREMENTS AT GSA, ENERGY, AND NAVY

As requested, we examined how well GSA, Energy and the Navy are

complying with the federal statute requiring subcontracting plans. To accomplish this, we reviewed 2,052 contract files at 15 procurement offices located in the Washington, D.C. and San Francisco metropolitan areas and New York City, Chicago, and Oak Ridge, Tennessee. Our sampling plan did not include a random selection of locations throughout the country so we cannot project conditions on an agencywide basis.

At GSA, we visited the 8 offices which had awarded almost two thirds of all GSA contracts for $500,000 or more in the 18-month period ending in March 1987. Of the 968 contracts we examined, 503 did not contain subcontracting plans, most for valid reasons. For example, 413 of these were awarded to small businesses and thus did not require a plan.

While almost all of the other contracts without plans at GSA had justified reasons, we found 11 contracts that should have had plans but did not. All 11 cases were multiyear contracts with a total face value exceeding the dollar threshold. However, the GSA contracting officers had erroneously calculated the dollar value on an annual basis which resulted in dollar values less than the $500,000 level where plans are required.

At Energy, we examined over 60 percent of all contracts with a value of $500,000 or more that were open during fiscal year 1986. Of the 457 contract awards and modifications we examined, 233 did

not have subcontracting plans. Similar to GSA, most of the contract actions without plans had justified reasons. We found 15 actions, however, that should have had plans. Six of these were multiyear actions where, as at GSA, the dollar value had been calculated on an annual basis. The remaining nine cases were the result of oversight.

At the Navy, we examined the three largest commands in terms of procurement dollars. Together, these commands accounted for slightly more than half of all Navy procurement dollars during fiscal year 1986. We reviewed 627 contract actions that met the dollar threshold for requiring a subcontracting plan and found 272 without a plan. While many of these were justified in not having a plan, 84 of them, or 31 percent, were not. In all 84 cases the reason given for the lack of a plan was oversight.

SUBCONTRACTING GOALS FOR SMALL AND SMALL DISADVANTAGED BUSINESSES

Slightly more than half of the contract awards and modifications we examined had subcontracting plans which contained goals for the use of small and small disadvantaged businesses as subcontractors. These goals are expressed as percentages of the total amount of subcontracting to be done under the procurement action and selected statistics for the goals are presented in our report. Our analysis shows that the average small business goal for GSA, Energy and the Navy was 23 percent, 39 percent, and 40

percent, respectively. The average small disadvantaged business goals were 2 percent, 7 percent, and 3 percent, respectively.

Although these statistics provide a useful overview of the program at each agency, we would caution that they should not be used for comparative purposes. The adequacy of a subcontracting plan's goals should be assessed on a case by case basis. Consequently, it is neither feasible nor reasonable to formulate quantitative criteria for subcontracting goals. Without such criteria, one plan's goals cannot be compared to another's and one agency's statistics cannot be compared to another's.

During our review, we attempted to determine how successful contractors are in achieving the goals contained in the subcontracting plans. Although the available data permitted only a limited analysis on an aggregate basis, it appears that in general, most of the subcontracting goals at the three agencies we reviewed are being achieved.

COMPLIANCE OF PUBLIC UTILITY COMPANIES WITH SUBCONTRACTING PLAN REQUIREMENTS

GSA has statutory authority to enter into long-term contracts for utility services for federal agencies for periods not to exceed 10 years. These contracts may be in the form of an areawide contract furnishing service to several federal agencies located within the supplier's area of service or a contract to provide

service to a single user. GSA may also delegate authority to other agencies to negotiate and award their own utility contracts.

The prices charged by public utilities are determined by rate schedules which apply to all users and are based on such factors as normal volume and peak usage hours. Contracts between utilities and the government generally specify only that the government will pay the rates and receive the discounts to which it is entitled. They do not specify a rate to be paid by the government or affect the rate in any manner.

Although federal procurement regulations require agencies to obtain a contract for all purchases exceeding $25,000, some utility companies, for various reasons, have declined to enter into contracts with the federal government. In most instances, federal agencies have no choice but to purchase these utility services without a contract since alternative sources are not available.

As requested, we identified which utility companies have declined to enter into contracts with GSA and have listed them in the attachment to this testimony. Of the 23 companies listed, 10 specifically objected in whole or in part to the requirement for subcontracting plans. The other 13 cited more general objections to entering into contracts for service.

GSA has made progress in persuading more public utilities to provide services to the government under formal contract. In 1976 there were 41 areawide contracts in effect with utility companies. As of June 1988 this number had increased to 67. In addition, 12 single-user contracts had been awarded by GSA.

Based upon our review of the pertinent federal statutes, it is our opinion that a public utility which sells services to the federal government, but which declines to enter into a formal contract with the government, is nonetheless legally required to satisfy the subcontracting plan requirements of section 211 of Public Law 95-507. We are providing our legal opinion on this matter to the Committee under separate cover.

In our opinion, the most realistic remedy available to the government in cases where there is no formal contract is to seek judicial enforcement of the subcontracting plan requirements by obtaining an injunctive order enjoining the utility from failing or refusing to comply with the statutory requirements.

The practicality of pursuing this remedy is a matter the agencies should consider in light of the individual circumstances. While judicial enforcement of the subcontracting plan requirements is generally available to the government, our examination of case law suggests that the probability of success in obtaining an

injunction to effect this remedy is uncertain.

SUBCONTRACTING PLANS CONTAINING MODIFIED CLAUSES

In January 1984, in an attempt to encourage more utility companies to execute contracts, GSA requested approval from the Small Business Administration to modify the clause required in subcontracting plans that specifies that all subcontractors other than small businesses that receive awards meeting the dollar threshold must also prepare and implement a subcontracting plan. In order to address the concerns of a number of utility companies over this so called "flowdown" clause, GSA proposed to modify the clause so that it would have required plans only from subcontractors receiving subcontracts of more than $500,000 to construct and operate facilities directly pertinent to providing service to the government. SBA approved the modification the following month.

In October 1986, in response to an inquiry from this Committee, SBA reversed its position on allowing modified clauses to subcontracting plans. Although GSA has subsequently stopped using the modified clause in its negotiations with utility companies, 26 contracts were awarded which contained the modified clause in the subcontracting plans. GSA informed us that three of these have been corrected and that it will attempt to correct the others as time and resources permit.

In our opinion, neither GSA nor SBA has the authority to modify clauses in a way which affects the implementation of the statutory subcontracting plan requirements. The remedies available to the government regarding contracts with subcontracting plans that have been altered in an unauthorized manner are to modify the contract so that the plan contains the correct clause, terminate the contract and resolicit the procurement, or, as previously discussed, seek judicial enforcement. Again, the practicality of pursuing any of these remedies should be considered in light of individual circumstances. A contract modification, if made unilaterally by the government, might not be complied with by the contractor. Contract termination does not appear to be realistic, since generally, the utilities are monopoly suppliers. Finally, as noted earlier, judicial enforcement is uncertain.

UTILITY SUBCONTRACTING PLANS AT GSA, ENERGY, AND THE DEPARTMENT OF DEFENSE

Finally, you asked that we compare the efforts of GSA and the Departments of Energy and Defense to assure that contracts for utility services comply with subcontracting plan requirements.

All of the utility contracts awarded by GSA that should contain subcontracting plans do contain plans.

The Department of Energy annually procures utility services costing about $1 billion. Because centralized data and files for these procurements are not available, we did not make a detailed review of files at Energy and cannot specify the extent to which the Department is obtaining utility service under contract and which of these comply with the subcontracting plan requirements. Based on the contract files we did review, however, and the discussions we had with Energy officials in the field offices, we identified several instances where utility companies declined to enter into contracts with Energy and where contracts that should have had subcontracting plans did not. These include the following examples:

-- Six utility companies have declined to enter into contracts with Energy generally because of objections in whole or in part with the subcontracting plan requirement.

-- Three utility companies have signed contracts but insisted that the subcontracting plan requirement be removed from the contract.

-- One company has a contract but has not submitted the required plan.

-- A number of contracts were awarded before the implementation of Public Law 95-507 and therefore do not require subcontracting plans. Many of these contracts, however, are more than ten years old in spite of federal and Energy regulations which limit contracts for utility services to ten years. At least one utility company has declined to renew an outdated contract because of the subcontracting plan requirement.

All of the information we obtained at the Department of Defense is based on interviews with officials at various levels throughout the Office of Secretary of Defense and the Army, Navy,

and Air Force Departments. Because the necessary records are dispersed at numerous locations across the country, we did not review any contract files.

In fiscal year 1987 the Department of Defense purchased almost $2 billion of utility services. We were informed that most of these services were acquired under contract although some utility companies, as is the case at GSA and Energy, have declined to sign contracts with the military services. Our discussions with various officials responsible for procuring utility services indicate that very few of the military's utilities contracts, if any at all, contain subcontracting plans.

When awarding contracts for utility services, each branch of the military follows the policies and procedures contained in guidelines issued in 1974. These guidelines also provide a standardized format for utility contracts. Because the guidelines predate the law requiring subcontracting plans for certain federal procurements, contracts that are written in the suggested format do not say that subcontracting plans are required.

An official responsible for utility acquisitions on a Department-wide basis said that, in all probability, utility contracts written for the military would not contain subcontracting plans because contracting officers were using the 1974 guidelines and

were not aware of the requirement.

In discussions we had with officials responsible for utilities procurement at eight major commands within the Army, Navy, and Air Force, we were also told that most did not know of the requirement and that none were enforcing it. None of the individuals that we spoke with knew of any contract for utility services awarded by the military that contained a subcontracting plan.

This concludes my comments on the two reviews done for the Committee. My colleagues and I would be pleased to answer your questions.

PUBLIC UTILITY COMPANIES DECLINING TO SIGN CONTRACTS WITH THE GENERAL SERVICES ADMINISTRATION

*Alaska Electric Light and Power Co.
Juneau, Alaska

*Department of Public Works
Arlington, Virginia

*Department of Public Utilities
Newport News, Virginia

*The Cleveland Electric Illuminating Company
Cleveland, Ohio

*The East Ohio Gas Company
Cleveland, Ohio

The Florida Power & Light Company
Miami, Florida

The Long Island Lighting Company
Patchogue, New York

*The Oklahoma Electric Company
Oklahoma City, Oklahoma

*The Potomac Electric Power Company
Washington, D.C.

*The San Diego Gas & Electric Company
San Diego, California

*The Tucson Electric Power Company
Tucson, Arizona

*The Washington Suburban Sanitary Commission
Hyattsville, Maryland

The Arkansas Power & Light Company
Little Rock, Arkansas

The Baltimore Gas and Electric Company
Baltimore, Maryland

The Consolidated Edison Company of New York, Inc.
New York City, New York

* Companies that objected in whole or in part to the requirement for a subcontracting plan for small and small disadvantaged businesses.

PUBLIC UTILITY COMPANIES DECLINING TO SIGN CONTRACTS WITH THE GENERAL SERVICES ADMINISTRATION

The Consumers Power Company
Jackson, Michigan

The Florida Power Corporation
St. Petersburg, Florida

The Louisville Gas and Electric Company
Louisville, Kentucky

New Orleans Public Service Inc.
New Orleans, Louisiana

The Public Service Company of North Carolina, Inc.
Gastonia, North Carolina

The Memphis Light, Gas and Water Division
Memphis, Tennessee

The Kentucky-American Water Company
Lexington, Kentucky

The Johnson City Power Board
Johnson City, Tennessee