

GAO

Report to the Chairman, Subcommittee
on Oversight and Investigations,
Committee on Armed Services, House of
Representatives

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MINORITY CONTRACTING

DOD's Reporting Does Not Address Legislative Goal





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The Honorable Norman Sisisky
Chairman, Subcommittee on Oversight
and Investigations
Committee on Armed Services
House of Representatives

Dear Mr. Chairman:

In response to the request of the former Chairman and discussions with your office, we are reporting on certain aspects of the Department of Defense's (DOD) implementation of 10 U.S.C. 2323.¹ Section 2323 established a goal that a total combined amount equal to 5 percent of DOD contract dollars for procurement; military construction; operation and maintenance; and research, development, test, and evaluation should be awarded, either as contracts by DOD or as subcontracts by DOD's prime contractors, to (1) minority small business concerns, (2) historically black colleges and universities (HBCU), and (3) minority institutions (MI). Specifically, we reviewed DOD's (1) progress toward the 5-percent program goal, (2) use of certain contracting procedures authorized to achieve the section 2323 goal, and (3) progress in increasing participation by minority small business concerns.

Results in Brief

Although section 2323 requires reporting on progress toward meeting the 5-percent goal, DOD's reports for fiscal years 1990 and 1991 did not clearly show its progress toward meeting this goal. Instead of reporting on the section 2323 goal, DOD reported on three separate 5-percent goals—prime contracts with minority small business concerns, subcontracts with such concerns, and prime contracts with HBCUs and MIs. Officials said that such reporting is consistent with their program management and with reporting by other federal departments and agencies.

Our analysis of DOD data shows that more significant progress was made on the overall goal than indicated by reporting on the separate goals. Furthermore, even though DOD's fiscal year 1992 report also does not discuss performance against the section 2323 goal, data in an exhibit in the report shows that DOD exceeded the goal.

¹Section 2323 codifies and amends section 1207 of Public Law 99-661, the Fiscal Year 1987 National Defense Authorization Act, the subject of the Subcommittee's original request.

In fiscal years 1991 and 1992, about 20 percent of the amount of contracts awarded to minority small business concerns involved preferential contracting practices such as set-asides or price preferences. Section 2323 authorized DOD to use these practices that involve less than full and open competition to the extent practicable and when necessary to facilitate achievement of the 5-percent goal. However, DOD exceeded the section 2323 goal in fiscal year 1992, even if awards using preferential contracting procedures are excluded. Therefore, the extent to which these practices will be needed in fiscal year 1993 and beyond is unknown.

Although section 2323 requires the Secretary of Defense, to the extent practicable, to maximize the number of minority small business concerns participating, DOD does not report on the extent of participation by these concerns. Our analysis of DOD data on contract actions over \$25,000 shows that about 29 percent more of these concerns received DOD contract obligations in fiscal year 1992 than in fiscal year 1987. However, a relatively small number of these concerns received the vast majority of the contract dollars.

DOD Not Reporting on Specified Goal

Section 2323 requires DOD to report periodically on its progress toward meeting the 5-percent goal, but reports for fiscal years 1990 and 1991 do not clearly show DOD's progress toward meeting the goal. Instead of reporting the total combined amount against a single goal, DOD reported this information separately. This has led to some confusion about DOD's actual achievements. If DOD had reported on the section 2323 goal directly, it would have shown more significant progress in fiscal years 1990 and 1991. Furthermore, for fiscal year 1992, such reporting would have shown the statutory goal was exceeded.

Section 2323 establishes a DOD procurement goal, which extends through the year 2000, for awards to minority small business concerns² (called small disadvantaged business (SDB) concerns in DOD regulations), HBCUs,³

²These are concerns owned and controlled by socially and economically disadvantaged individuals. The Federal Acquisition Regulation defines socially disadvantaged individuals as those who have been subjected to racial or ethnic prejudice or cultural bias because of their identity as a member of a group without regard to their individual qualities. Economically disadvantaged individuals are socially disadvantaged individuals whose ability to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities.

³Accredited institutions of higher education established prior to 1964 having the principal mission of educating Black Americans.

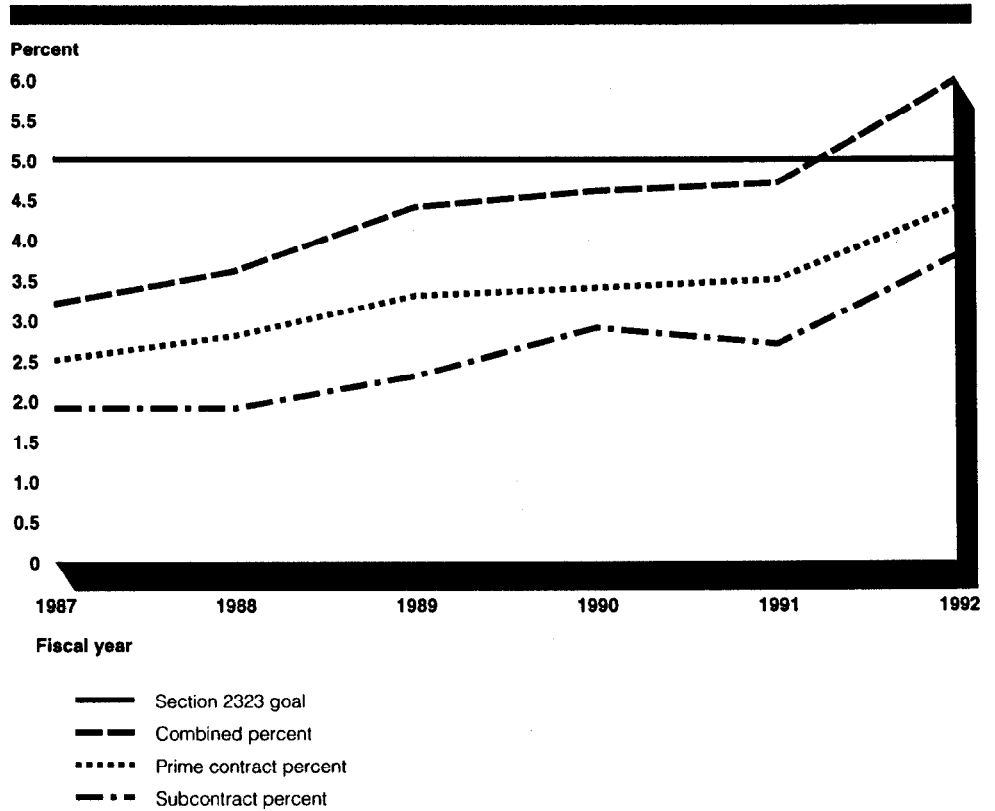
and MIS.⁴ The goal is that a total combined dollar amount equal to 5 percent of DOD's contract dollars in four appropriation areas be awarded as DOD contracts or subcontracts by DOD prime contractors to SDBs and HBCU/MIS.

DOD's reports to Congress, required by section 2323, were not in a consistent format that allowed direct comparison to the 5-percent goal. The final reports for fiscal years 1987, 1988, and 1989 directly reported this information. However, the final reports for fiscal years 1990 and 1991 show DOD's performance separately for SDB prime contract, subcontract, and HBCU/MI procurement. Though the 1990 and 1991 reports included data that could be used to compute performance against the section 2323 goal, DOD's progress toward accomplishing the goal could not be determined directly from the reports. The fiscal year 1992 report also does not report against the goal in its narrative, but does include data in an exhibit that shows the combined total was 6 percent.

More specifically, the fiscal years 1990 through 1992 year-end reports showed 3.4-, 3.5-, and 4.4-percent prime contracting accomplishments, as well as separate subcontract and HBCU/MI data. If these reports had presented combined data as specified in section 2323, DOD would have shown 4.6, 4.7, and 6.0 percent, respectively. For fiscal year 1987 through fiscal year 1992, figure 1 contrasts DOD's performance against the goal using the separate prime and subcontracting percents reported by DOD with the combined percent specified in section 2323. (DOD contract dollars to HBCU/MIS is not shown because such dollars, while about 5 percent of dollar awards to institutes of higher education, represent about 0.03 percent of the goal.)

⁴Minority institutions were defined as institutions of higher education that had a specified percentage enrollment of selected minorities. However, for reasons not related to section 2323, this definition was eliminated by the Higher Education Amendments of 1992.

Figure 1: DOD SDB Statistics



In addition to increasing the percent of obligations, DOD also increased the amount of obligations to SDBs, even during periods when the overall obligations by DOD decreased. Obligations to SDBs were 61 percent higher in fiscal year 1992 than in fiscal year 1987, while DOD's prime contract obligations decreased 13 percent in that period. Table 1 shows, using data from DOD year-end reports, the total combined amounts contracted and subcontracted to SDBs during the 6 years, fiscal years 1987 through 1992, and the total amount of DOD contracting.

Table 1: DOD Comparative Obligation Data

Dollars in millions

Fiscal year	Contract obligations	SDB contract and subcontract obligations	SDB percent
1987	\$135,340	\$4,340	3.2
1988	130,815	4,765	3.6
1989	120,003	5,299	4.4
1990	123,821	5,723	4.6
1991	125,878	5,972	4.7
1992	117,151	6,972	6.0

Reporting Justified Based on Management Goals and Other Laws

DOD officials said that its minority procurement program set separate 5-percent goals for prime contract awards by DOD, subcontract awards by DOD's prime contractors, and HBCU/MI awards. They said that these separate goals (1) enhance visibility over activity in each of the areas, (2) accommodate prior management practices, and (3) are consistent with other federal minority contracting programs. If DOD had achieved the separate 5-percent goals in fiscal year 1988 and the following years, the minority contracting dollars would have exceeded 7 percent in each of those years as compared to the section 2323 goal.

According to DOD's Small and Disadvantaged Business Utilization Office representatives, three separate 5-percent goals (prime contract awards as a percent of prime contracts, subcontract awards as a percent of applicable subcontract dollars, and HBCU/MI awards as a percent of higher education institution awards) is the most appropriate way to manage the program and allows both DOD and oversight organizations to specifically identify the program's successes and deficiencies. These officials said that DOD's reporting practice is comparable to other federal departments and agencies reporting on similar minority contracting programs. Specifically, they said the Office of Federal Procurement Policy, in interpreting section 502 of Public Law 100-656, the Business Opportunity Development Reform Act of 1988, required⁵ separate 5-percent goals for prime contracting and subcontracting in its Policy Letter 91-1. In addition, section 832 of Public Law 101-510, the Fiscal Year 1991 National Defense Authorization Act, required DOD to establish a specific goal within the overall 5-percent goal for the award of prime contracts and subcontracts to HBCU/MIS.

⁵The Office of Federal Procurement Policy, as part of the Office of Management and Budget, is responsible for providing governmentwide procurement policies for executive agencies.

Preferential Procedures Used to Achieve Goal

To assist DOD in meeting the 5-percent goal, Congress authorized contracting procedures that provided preferential treatment for SDBs, including less than full and open competitive procedures and advanced payments to SDBs. According to section 2323, DOD is authorized to use these procedures to the extent practicable and when necessary to facilitate achievement of the 5-percent goal. However, DOD would have achieved the goal in fiscal year 1992 even if the awards using preferential contracting procedures were excluded.

DOD procurement activities have used less than full and open competitive procedures to increase awards to SDBs. In awarding these contracts, activities have used the previously authorized section 8(a) program and section 2323 authorized SDB set-asides and price preferences. SDB set-asides are to be used when there is a reasonable expectation that at least two SDBs will submit offers and the price will not exceed fair market price by more than 10 percent. DOD reports show that SDB set-aside contracts totaled \$652 million in fiscal year 1991 and \$796 million in fiscal year 1992, or about 15 percent of the amount of prime contracts awarded to SDBs in those years. Price preferences allow a contracting officer, in evaluating competitively offered prices, to make SDBs' offers more competitive by increasing other offers by 10 percent. DOD reports show that price preferences were used in contracts totaling \$181 million in fiscal year 1991 and \$264 million in fiscal year 1992, or about 5 percent of the amount of prime contracts awarded to SDBs in those years. DOD officials said that advanced payments have not been used extensively because they entail a level of risk to the government that is often unacceptable.

In fiscal year 1992, DOD would have achieved the goal even if the awards using SDB set-asides and price preference were excluded. DOD officials believe that it is premature to assume that the goal can be achieved without such procedures. However, because section 2323 authorizes preferential contracting procedures to the extent practicable and when necessary to achieve the 5-percent goal, DOD needs to evaluate the continued use of preferential contracting procedures.

DOD Not Reporting on Extent of SDB Participation

Section 2323 requires the Secretary of Defense, to the extent practicable, to maximize the number of SDBs and HBCU/MIS participating in the program. However, DOD's reports do not show the number of minority small business concerns receiving contract obligations and the distribution of obligations among those firms. Such data would assist in assessing the

extent to which DOD has made progress in expanding participation in the program.

DOD increased the number of SDBs receiving contract obligations of \$25,000 or more by about 29 percent from 2,776 in fiscal year 1987 to 3,593 in fiscal year 1992.⁶ However, during this 6-year period DOD obligated a large portion of the SDB contract dollars to a small number of firms. For example, in fiscal year 1992, DOD buying activities obligated 25 percent of the contract dollars to about 34 companies (about 1 percent of the minority small business concerns receiving obligations) and 75 percent of the contract dollars to 486 companies (about 14 percent of the total number). Table 2 shows the distribution of SDB procurement dollars.

Table 2: Distribution of Obligations to SDBs

Percent of dollars obligated	Number of SDBs receiving obligations by fiscal year					
	1987	1988	1989	1990	1991	1992
10.0	7	8	5	7	7	6
25.0	32	32	24	33	37	34
33.3	52	53	44	56	63	66
50.0	120	118	108	125	145	164
66.7	249	245	228	270	296	340
75.0	358	361	341	398	420	486
100.0	2,776	2,823	3,040	3,222	3,249	3,593

Also, the same companies received a substantial percent of the total dollars obligated to SDBs from year to year. One company was among the 10 SDBs receiving the largest amount of contract dollars obligated in each of the 6 years. This company plus another company were awarded contract actions totaling \$734 million, about 3 percent of the 6-year total obligations.

Recommendations

We believe that improved reporting by DOD on the 5-percent goal established by section 2323 and on the extent of SDB participation would help clarify program accomplishments and status and ensure appropriate oversight. Accordingly, we recommend that the Secretary of Defense

⁶This and the following data relate only to obligations of \$25,000 or more because the data was extracted from reports on DD Form 350, which are prepared only when the contract action is for \$25,000 or more. During the years reported, these obligations generally amounted to more than 90 percent of the DOD total dollars to SDBs. Also, because the same company is apparently listed under slightly different names in the reports, the number of companies would be less if duplicate listings were eliminated.

direct the Under Secretary of Defense for Acquisition, in meeting the reporting requirements established by section 2323, to include in the report, along with the currently reported data on program management goals, data on

- SDB procurement performance that directly corresponds to the section 2323 goal and
- the extent of SDB participation in the program, including information on the overall number of companies receiving awards and the percent of dollars obligated to these companies.

In addition, since DOD achieved the 5-percent goal in fiscal year 1992, we recommend that the Secretary evaluate the extent to which the preferential contracting procedures are needed to meet program goals.

Agency Comments and Our Evaluation

We requested fully coordinated comments from DOD, but none were provided. Officials in the Office of Small and Disadvantaged Business Utilization within the Office of the Secretary of Defense agreed with the findings and said that future reports to Congress on section 2323 would highlight performance against the legislative procurement goal and include data showing the extent of SDB participation in the program. However, they did not fully concur with our recommendation to evaluate the use of preferential contracting procedures. They said such an evaluation could lead to prematurely curtailing the use of the procedures. Our position is not that the use of the procedures should be curtailed based on the results achieved in 1 year. However, given the language of section 2323 and the results achieved in fiscal year 1992, an evaluation is needed to assist in determining the extent of continued use of these procedures.

Scope and Methodology

We obtained information and interviewed officials from the Office of Secretary of Defense, each military service of DOD, the Office of Federal Procurement Policy, and Headquarters of the Small Business Administration in Washington, D.C. We also obtained data and interviewed officials from Headquarters Air Force Materiel Command and Aeronautical Systems Center at Wright-Patterson Air Force Base, Ohio; Headquarters Defense Logistics Agency at Cameron Station, Virginia, and its Defense Electronics Supply Center in Dayton, Ohio; and Small Business Administration offices at two locations. These officials included small and disadvantaged business utilization officials, small business specialists and liaison officers, Small Business Administration representatives,

contracting officers, procurement officials and analysts, and procurement law administrators.

We reviewed applicable laws, regulations, policies, program documentation, and reported program performance statistics. We also extracted information on the number of SDBs receiving contract awards and the amounts awarded to them from DOD data based on "Individual Contracting Action Reports," DD Form 350. However, we made no attempt to verify information in the DD Form 350 data files or the data reported by DOD in its required reports.

We conducted our work between May 1992 and February 1993 in accordance with generally accepted government auditing standards. We obtained oral comments on this report from officials in the Office of Small and Disadvantaged Business Utilization within the Office of the Secretary of Defense.

We will send copies of this report to the Chairmen, House and Senate Committees on Small Business, Senate Committee on Governmental Affairs, House Committee on Government Operations, and Senate Armed Services Committee; the Secretary of Defense; the Director, Office of Management and Budget; and other interested parties upon request.

Please contact me at (202) 512-4587 if you or your staff have any questions concerning this report. Major contributors to this report are listed in appendix I.

Sincerely yours,



Paul F. Math
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