

GAO

Testimony

Before the Committee on Small Business, House of
Representatives

For Release on Delivery
Expected at
9:15 a.m. EST
Wednesday
March 4, 1992

SMALL BUSINESS

The Small Business
Administration's Progress in
Restructuring Its 8(a) Business
Development Program

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Mr. Chairman and Members of the Committee:

We are pleased to be here today to discuss our report that you are releasing today concerning the Small Business Administration's (SBA) progress in implementing changes to its 8(a) program.¹ As you know, the goal of the 8(a) program is to promote the development of small businesses owned and controlled by socially and economically disadvantaged individuals.

The changes we are discussing today are those required by the Business Opportunity Development Reform Act of 1988 and subsequent amendments which were aimed at improving (1) program access, (2) administrative efficiency, and (3) the ability of participating firms to successfully compete in the marketplace after leaving the program. In addition, the 1988 act required that we report on SBA's progress in implementing the changes.

In summary, our work shows that SBA has had difficulty in implementing many of the changes, and that the agency's lack of reliable data on many program activities has hindered its ability to effectively manage the program. Specifically, certification of program participants is taking longer than the act allows, many 8(a) firms do not have approved business plans, difficulties exist in equitably distributing noncompetitive contracts, few 8(a) contracts are competitively awarded, weaknesses exist in SBA's management information system, and the extent of management, technical and financial assistance is unknown.

BACKGROUND

The 8(a) program is administered by SBA's Office of Minority Small Business and Capital Ownership Development. Under the program, SBA, acting as a prime contractor, enters into contracts with other federal agencies and subcontracts the work to 8(a) firms. SBA can also provide financial, technical, and management assistance to the firms to aid their development. As of October 1, 1991, there were 3,922 firms in the program. In fiscal year 1991, the program provided about 4,400 new 8(a) contracts and about 15,600 contract modifications to new and existing contracts, totaling \$3.77 billion, to 8(a) firms.

Specifically, the 1988 act required GAO to examine and report on the

- certification of program applicants,
- development and maintenance of 8(a) firms' business plans,
- geographical distribution of noncompetitive 8(a) contract awards,

¹Small Business: Problems in Restructuring SBA's Minority Business Development Program (GAO/RCED-92-68, Jan. 31, 1992).

- competitive awarding of 8(a) contracts,
- agency's collection and management of program data,
- amount and type of management and technical assistance to 8(a) firms,
- reporting by 8(a) firms about their use of paid consultants to obtain contracts,
- amount and type of financial assistance to 8(a) firms,
- limitations on the transfer of contracts if 8(a) firms change ownership, and
- delays in contract awards resulting from protests of the continuing eligibility of 8(a) firms or of the competition restricted to 8(a) firms.

CERTIFICATION OF PROGRAM PARTICIPANTS
IS TAKING LONGER THAN THE ACT ALLOWS

In an effort to improve access to the program, the act, as amended, requires SBA to process an application and decide on an applicant's program eligibility within 90 days of receiving a completed application. SBA met the requirement for only about 24 percent of the 268 applications that it approved or declined between January and November 1990. The average processing time for these applications was 117 days. As of the beginning of fiscal year 1992, about 17 percent of the 222 applications in processing at SBA headquarters had already exceeded the 90-day requirement. We attempted to determine why the processing delays were occurring. However, until January 1992, SBA used a manual system to track applications in process. This system did not pinpoint where or why processing delays were occurring because (1) it did not track all application review stages and (2) SBA personnel often did not record data for stages that were tracked. SBA has developed an automated system to track applications and began using the system in January 1992.

NOT ALL 8(a) FIRMS HAVE APPROVED BUSINESS PLANS

To aid in the development of 8(a) firms, the act required that (1) each firm entering the program after June 1, 1989, have a business plan approved by SBA before the firm is eligible for contracts and (2) each firm annually review its business plan with SBA and modify it accordingly to help the firm achieve its business development goal.

In response to the act, SBA adopted a new 33-page business plan form and mandated its use by all new firms beginning in January 1990. The agency also required all incumbent firms to submit

revised business plans using the new form. SBA planned to complete its review of incumbent firms' revised business plans by July 1, 1991.

As of October 1, 1991, SBA had received new or revised business plans from 2,700 firms, or 69 percent, of the 3,922 firms in the program. It had reviewed and approved 2,250, or 83 percent, of the plans received. The remaining 17 percent were either awaiting review by SBA or required further revision by the 8(a) firms. According to SBA, some firms have not submitted business plans because of the time and cost involved in their preparation, while other firms that have not received an 8(a) contract have no incentive to revise their plans. However, SBA does not enforce the act's provision requiring approved business plans from incumbent firms before contracts can be awarded. Instead of withholding contracts, SBA has elected to work with the firms to get revised business plans submitted.

DIFFICULTIES EXIST IN EQUITABLY DISTRIBUTING NONCOMPETITIVE CONTRACTS GEOGRAPHICALLY

The act directs SBA to promote the equitable geographic distribution of noncompetitive 8(a) contracts to the maximum extent practicable. However, the act also directs SBA to award contracts to 8(a) firms recommended by procuring agencies. According to SBA, procuring agencies recommend specific 8(a) firms for about 95 percent of the contracts offered to the program. As a result, SBA has little control over the distribution of contracts. In addition, 8(a) firms are not equitably distributed across the country, and some do a better job of marketing themselves to procuring agencies than others.

In fiscal year 1990, four states and the District of Columbia, which together had about 42 percent of the 8(a) firms that received contracts, received about 60 percent of the total contract dollars awarded. In addition to the issue of geographic concentration, 50 firms, or less than 2 percent of the 3,645 firms in the program in fiscal year 1990, received about \$1.5 billion or 40 percent of the total contract dollars awarded, while 1,914 firms, or about 53 percent, received no contracts. This same situation existed in fiscal year 1989, when 1,648, or 50 percent, of the 3,319 total firms in the program received no contracts during the fiscal year.

FEW 8(a) CONTRACTS ARE COMPETITIVE AWARDS

The act mandates competition among 8(a) firms when the total contract price, including the estimated value of contract options, exceeds \$5 million for manufacturing contracts and \$3 million for all other contracts. Of the approximately 8,300 new 8(a) contracts awarded in fiscal years 1990 and 1991, valued together at about \$3 billion, only 67 contracts, totaling \$136 million, were competitive awards.

While SBA's management information system records the actual value of a contract as awarded, it does not record the estimated value of contract options that may be exercised in the future. As a result, the system does not provide information on how many of the 8,300 new contracts met the financial requirements for competition.

WEAKNESSES EXIST IN SBA'S MANAGEMENT INFORMATION SYSTEM

The act requires SBA to develop a systematic data collection process and to report to the Congress, by April 30 of each year, on the status of 8(a) firms and the program's accomplishments during the prior fiscal year. The first report--due April 30, 1991, for fiscal year 1990 activity--was submitted to the Congress in late October 1991.

SBA's Financial Information System--the primary management information system for the 8(a) program--does not include the data necessary to meet the act's reporting requirements. Instead, SBA had to query its field offices for information needed to compile the fiscal year 1990 report, such as the net worth of firms in the program and information on the firms that had left the program. Additionally, SBA had to query its field offices to respond to our information requests on the 8(a) program.

SBA recognizes that its present information system is inadequate for 8(a) program management. In its Federal Manager's Financial Integrity Act reports for fiscal years 1989, 1990, and 1991, SBA reported a material weakness in internal controls resulting from the system's failure to furnish managers with adequate information about 8(a) services provided through the agency's field offices. SBA has identified several program areas for which new or improved automation is needed, such as 8(a) firms' terminations and graduations from the program and 8(a) contract protests and appeals. As of January 1992, SBA had developed a written plan that identifies steps and time frames for automating field office activities. SBA plans to complete this effort by August 1992. However, the agency still needs to develop specific plans for redesigning its Financial Information System.

REQUIREMENT TO REPORT THE USE OF CONSULTANTS RECENTLY IMPLEMENTED

In order to discourage improper behavior, such as the use of political influence, in obtaining 8(a) contracts, the act required that beginning June 1, 1989, 8(a) firms were to report semiannually to SBA on their use of paid agents, attorneys, accountants, consultants, and others that assist the firms in obtaining federal contracts. Firms failing to report may be terminated from the program. The act also requires SBA to refer any reports raising suspicions of improper activity to the agency's Inspector General.

SBA did not require 8(a) firms to begin such reporting until October 25, 1991--28 months after the original mandate. SBA did not submit the reporting form to the Office of Management and Budget (OMB) for approval until February 1991. OMB approved the form in May 1991. SBA attributed the delay in submitting the form primarily to higher-priority 8(a) program work and to the turnover of key staff.

EXTENT OF MANAGEMENT AND TECHNICAL ASSISTANCE TO 8(a) FIRMS UNKNOWN

The act directed us to report on the amount and type of business management and technical assistance provided to 8(a) firms and the criteria SBA uses to measure the effectiveness of such assistance. While 8(a) firms, as small businesses, are eligible to receive management and technical assistance from various sources, such as SBA's Service Corps of Retired Executives,² SBA's 7(j) program targets assistance specifically to 8(a) firms. Under the 7(j) program, SBA hires contractors to conduct seminars and provide one-on-one assistance in 16 specialized categories, such as accounting and loan packaging, usually at no cost to 8(a) firms. In fiscal year 1990, SBA spent about \$2.3 million providing assistance under the 7(j) program to 1,204 8(a) firms.

Each year, SBA field offices estimate the type and amount of management and technical assistance needed for 8(a) firms in each of the 16 categories. However, SBA does not track, by category, the actual amount of assistance provided because SBA does not have a computer network that enables the agency to collect this information. Consequently, SBA does not know the actual amount of assistance provided to 8(a) firms in each 7(j) assistance category, nor whether the initially estimated amounts of assistance address 8(a) firms' needs. In addition, SBA does not record or report data on management and technical assistance provided to 8(a) firms by its other programs.

In addition to not knowing the specific amount or type of assistance provided to 8(a) firms, SBA also lacks objective criteria to measure the effectiveness of the 7(j) assistance. SBA currently relies on various indicators, such as (1) reports prepared by the contractors providing the assistance and (2) satisfaction surveys of the 8(a) firms receiving the assistance to get some idea of the quality of the assistance. SBA recognizes that objective criteria, such as long-term follow-up with 8(a) firms that have received assistance, are needed to better measure the effectiveness of the assistance. SBA's Office of Advocacy has been requested to develop such criteria, but because of limited

²SBA's Service Corps of Retired Executives is a volunteer program that matches retired volunteers with small businesses that need expert advice.

resources and the difficulty of this task, SBA considers the development of such criteria to be a long-term goal. In the interim, SBA is concentrating its efforts on improving the evaluation and use of information that it currently receives on the program.

EXTENT OF FINANCIAL ASSISTANCE PROVIDED
TO 8(a) FIRMS NOT FULLY KNOWN

The act directed us to report on the type and amount of financial assistance provided to 8(a) firms by SBA. In addition to the new 8(a) direct loans--established by the act--financial assistance is available to 8(a) firms through SBA-guaranteed loans; advance payments, which are cash disbursements made by SBA to an 8(a) firm prior to or during the performance of a specific 8(a) contract; and equity or investment capital from SBA-sponsored Small Business Investment Companies (SBIC). While 8(a) direct loans and advance payments are solely for 8(a) firms, the other types of financial assistance are available to all eligible small businesses.

The Congress appropriated \$5 million in each of fiscal years 1990 and 1991 for 8(a) direct loans. SBA made 22 direct loans totaling \$2.8 million in fiscal year 1990 and 22 direct loans totaling \$2.5 million in fiscal year 1991. SBA attributes the low number of 8(a) direct loans to legislative restrictions placed on the use of loan funds and the process established to obtain a direct loan. SBA interprets the act as allowing only manufacturing firms to use loan proceeds as working capital--a major need of many 8(a) firms. As of December 1990, only 13 percent of the firms in the 8(a) program were manufacturing firms. Also, before a firm can apply for an 8(a) direct loan, it must first be denied a conventional loan and an SBA-guaranteed loan. According to SBA, most 8(a) firms receiving financial assistance from SBA do so through SBA's guaranteed loan program. In fiscal years 1990 and 1991, SBA disbursed \$17.9 million in advance payments to 8(a) firms. SBA, however, does not track information on the amounts of assistance provided to 8(a) firms through its guaranteed loan and SBIC programs and, as a result, does not know the extent of such financial assistance.

SBA REVIEWS 8(a) FIRMS' CHANGE-IN-OWNERSHIP REQUESTS

The act directed us to report on how SBA administers the act's limitations on the transfer of ownership and control of 8(a) concerns that have 8(a) contracts. In order to control the transfer of 8(a) contracts to firms outside the program, the act requires that any 8(a) contracts awarded on or after June 1, 1989, be performed by the concern that initially received the contracts. Should the owner or owners upon whom eligibility was based relinquish ownership or control of the concern, the contracts are to be terminated for the convenience of the government. However, the act also provides that the SBA Administrator may waive the

requirement to terminate a contract under certain conditions, such as when ownership and control of the concern performing the contract passes to another small business concern that is eligible for the 8(a) program.

Between June 1, 1989, when the requirement became effective, and September 30, 1991, SBA headquarters staff received 25 change-in-ownership requests. SBA approved 17 of the requests and declined 5. The remaining three requests were still pending. For the five declined requests, SBA staff advised us that the requested changes in ownership would have rendered the concerns ineligible for the 8(a) program. As a result, no changes in ownership occurred.

SBA did not grant a waiver or terminate a contract for any of the 17 change-in-ownership requests that it approved because (1) the persons upon whom the concerns' eligibility for the 8(a) program was based did not relinquish ownership or control (six cases); (2) ownership and control continued to be held by socially and economically disadvantaged individuals (three cases); and (3) ownership and control of the 8(a) concern was relinquished, but at a time when the concern had no 8(a) contracts (one case). For the remaining seven cases, information provided by SBA was not sufficient for us to determine whether ownership or control of the concerns was relinquished or, if ownership or control was relinquished, whether the concerns had any 8(a) contracts at the time.

FEW PROTESTS OF 8(a) CONTRACT AWARDS

The act directed us to report on delays in contract awards resulting from the protest of an awardee's continued participation in the 8(a) program or of competition restricted to program participants. SBA's 8(a) program regulations specify that challenges to the eligibility of a firm to continue in the program must be filed separately with SBA and cannot be part of a bid or contract protest. SBA, however, does not know the actual extent to which such challenges occur because it does not collect this information. SBA estimated that only four to six challenges occurred during fiscal years 1990 and 1991.

Our search of a computerized data base of contract protests decided by GAO and the General Services Administration Board of Contract Appeals (GSBCA) showed that between the passage of the act in November 1988 and June 30, 1991, 24 protests (involving various issues concerning eligibility or competition) were decided--18 by GAO and 6 by GSBCA. We reviewed in detail the nine protests that GAO decided during fiscal year 1990. One of these protests specifically involved the issue of continuing eligibility; two others dealt with the competitive awarding of 8(a) contracts. GAO denied or dismissed the three protests. While the protest of SBA's eligibility decision delayed that contract's award by 45 days, the other two protests did not delay the other contract awards. The

While the act encourages the equitable geographical distribution of 8(a) contracts, SBA has limited control over such distribution because the act also directs the agency to award contracts to 8(a) firms recommended by procuring agencies. Because these two provisions appear to work against each other, in our report we also suggested that the Congress may wish to consider (1) clarifying its intent in directing SBA to equitably distribute contracts or (2) eliminating the directive from the act. Should the Congress decide to keep this directive, it may wish to revise the act's provision that requires SBA to award contracts to the firms recommended by procuring agencies in order to give SBA greater control over the distribution of the contracts.

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Mr. Chairman, this concludes my prepared statement. I would be glad to respond to any questions that you or members of the Committee may have.

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remaining six protests dealt with various other eligibility or competition issues, and as a result, we did not determine whether delays occurred.

In addition to filing contract protests with GAO and GSBICA, contractors can also file a protest with the procuring agencies. However, no central data base of such protests exists.

CONCLUSIONS, RECOMMENDATIONS, AND MATTERS
FOR CONGRESSIONAL CONSIDERATION

SBA has had difficulty in implementing many of the changes mandated by the Business Opportunity Development Reform Act of 1988, as amended. These changes were designed to improve the effectiveness of the 8(a) program. In addition, the lack of reliable data on many program activities has hindered SBA's ability to effectively manage the 8(a) program in a manner consistent with the requirements contained in the act.

In order to ensure that the 8(a) program achieves its objective of promoting the development of small businesses, in our report we recommended that the Administrator, SBA, direct the Associate Administrator, Office of Minority Small Business and Capital Ownership Development, to

- fully implement the new 8(a) application tracking system and use it to identify where and why delays are occurring in the application process, and work to meet the legislatively mandated 90-day processing time frame;
- either withhold contracts, as required by the act, from all 8(a) firms that fail to provide business plans to SBA for review and approval or request that the Congress revise this provision of the act;
- complete the development and implementation of written plans that detail the specific tasks and time frames for actions to be taken to correct the problems with the 8(a) program's management information system;
- determine the type and amount of management and technical assistance required by 8(a) firms, use this information to procure such assistance in the future, and work with the Office of Advocacy to develop objective criteria for better measuring the effectiveness of assistance provided under the 7(j) program to 8(a) firms; and
- determine the amount of loans and other forms of financial assistance provided to 8(a) firms by all SBA programs and use this information to determine the future financial needs of 8(a) firms.