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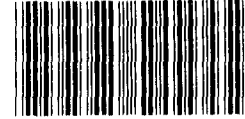


COMPTROLLER GENERAL OF THE UNITED STATES  
WASHINGTON, D.C. 20548

AUGUST 20, 1980

B-199566

The Honorable Gaylord Nelson  
Chairman, Select Committee  
on Small Business  
United States Senate



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The Honorable Neal Smith  
Chairman, Committee on  
Small Business  
House of Representatives

Subject: [Status Report on Small and Small Minority  
Business Subcontracting and Waiver of  
Surety Bonding for 8(a) Firms](CED-80-130)

Public Law 95-507, dated October 24, 1978, requires GAO to evaluate several Small Business Administration (SBA) programs with reporting deadlines of June 30, 1980, and January 1, 1981, depending on the specific program. In a December 17, 1979, letter, we advised you that because of delays in SBA's implementation of program changes, we would not be able to meet certain mandated reporting dates. We stated, however, that we would keep you apprised of SBA's progress in administering these programs. The purpose of this report is to inform you of actions taken by SBA concerning the section 7(j)(3) subcontracting program and the section 8(a)(2) surety bond waiver provision of the Small Business Act.

Under the subcontracting program, SBA, with the assistance of a presidentially appointed Advisory Committee, is supposed to encourage large businesses to place subcontracts with small and small minority firms. We stated in our December letter that according to SBA, it could not move ahead with this program until the Advisory Committee was established. The committee has finally been created and has held two meetings. However, specific committee functions and goals have not been established, no clear functional relationship exists between the committee and SBA, and to date, the committee has focused exclusively on Federal subcontracting.

Notwithstanding these problems, SBA has taken several steps to help small and small minority firms market their products and services in the private sector. These include a pilot marketing assistance program, seminars to explain the provisions of Public Law 95-507, and a proposed agreement with

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a major corporation to aid in developing disadvantaged firms. SBA has also promoted its Procurement Automated Sources System which provides Federal procurement officers and purchasing agents of prime contractors with profiles on the capabilities of small and small minority businesses.

To expedite the implementation of the section 7(j)(3) subcontracting program and to complement the initiatives SBA has taken, we are recommending that SBA and the Advisory Committee develop a specific plan for promoting private sector procurements from small and small minority businesses. We believe this plan should include (1) specific functional responsibilities for both SBA and the Advisory Committee, (2) short-range goals, and (3) a procedure for monitoring and evaluating progress.

Regarding the surety bond waiver provision, proposed rules and regulations for implementing it were not published until April 4, 1980, and to date no firm has been granted a waiver. Also, there is some confusion within SBA concerning which Associate Administrator is responsible for administering this provision. Therefore, we are recommending that the Administrator of SBA clearly define the roles of the offices involved.

SBA reviewed a draft of this report. SBA said that the report is fair and accurate and SBA concurred with our conclusions and recommendations.

Our review was conducted at SBA headquarters in Washington, D.C., and included an examination of the laws and legislative history pertaining to the section 7(j)(3) subcontracting program and the waiver of surety bonding for 8(a) firms. We reviewed procedures and practices established by SBA for implementing these provisions and discussed their administration with SBA program officials. Because activity in both areas was limited, our review objective was to identify reasons for delays in implementing these provisions and to point out matters requiring agency attention.

The details of our work to date are discussed below. We will continue to monitor SBA's progress in implementing both

these provisions. As previously agreed, we plan to issue a final report on the subcontracting program by September 1981. Pending the outcome of H.R. 5612, extending the date for us to evaluate and report on the waiver provision, we would expect to issue a final report on the surety bond waiver provision by February 1982.

PROMOTING SMALL AND SMALL  
MINORITY BUSINESSES  
THROUGH SUBCONTRACTING

Background

Public Law 95-507 amended sections 7(j) and 8(d) of the Small Business Act to emphasize the use of subcontracting as a method of promoting the long-term viability of small and small minority businesses. SBA is authorized under section 7(j) of the act to provide financial assistance to large businesses for the purpose of training and upgrading potential small and small minority subcontractors. Although SBA has had this authority since 1967, S. Rept. 95-1070 states that it generally had not been used.

To emphasize the importance of this authority and to encourage its use, the Public Law made this provision a separate subsection of the act (7(j)(3)) and mandated that the President appoint an Advisory Committee to assist SBA in implementing the provision. The law specified that the committee be composed of five high-level officers from U.S. businesses and five representatives from small minority businesses. It also required that the committee report annually to the President and the Congress on its activities.

In addition, section 211 of Public Law 95-507 amended section 8(d) of the act to provide small and small minority businesses with a maximum practicable opportunity to participate in the performance of contracts let by Federal agencies. The amendments required that a certain implementation clause be included in all contracts exceeding \$10,000 except those for services personal in nature and those to be performed outside of the United States, its territories, and its possessions. They also required that construction contracts in excess of \$1 million and other contracts in excess of \$500,000 contain subcontracting plans designed to achieve the statutory aims.

SBA is authorized under this section to review the subcontracting plans for any Federal contract exceeding these amounts for the purpose of determining whether maximum practicable opportunity has been afforded to small and small minority businesses. SBA is also required to report annually to the House and Senate Small Business Committees on the results of these reviews.

Problems in implementing  
section 7(j)(3)

Delays in establishing the advisory committee, the lack of specific committee functions and goals, and the exclusive focus of the committee on Federal subcontracting have impeded progress in implementing section 7(j)(3). According to the Associate Director of Presidential Personnel (White House) selection of the 10 members currently serving on the Advisory Committee was not finalized until late 1979 or early 1980. The Associate Director told us that delays in obtaining congressional approval of several committee members partly contributed to the length of time in establishing the committee. However, neither this individual nor SBA officials could provide a satisfactory explanation as to why it took 18 months from the passage of Public Law 95-507 until the committee held its first meeting on April 18, 1980.

Committee objectives unclear

Public Law 95-507, does not explicitly define the objectives of the Advisory Committee. Rather, the law states that the committee is to "facilitate" the achievement of the purposes of section 7(j)(3). Presumably, the Congress intended that more definitive objectives and functions would be developed jointly by the committee and SBA. However, our review disclosed that, to date, a clear understanding of the committee's role and relationship with SBA has yet to be resolved.

Executive Order 12190, dated February 1, 1980, which created the Advisory Committee in accordance with the legislative mandate, and the committee's charter also do not provide definitive objectives or functions for the committee. Rather, both simply state that

"\* \* \* the Committee shall assist in monitoring and encouraging the placement of subcontracts by the private sector with eligible small businesses, particularly with small minority businesses, and shall study and propose the incentives and assistance needed by the private sector to help in the training, development, and upgrading of such businesses."

We believe that the major problem in establishing objectives for the Advisory Committee has been the lack of a clear definition of the intent of section 7(j)(3). We have concluded, based on our review of the legislative history of this provision, coupled with our discussions with staff on both the House and Senate Small Business Committees, that the provision's primary objective is to encourage large businesses in the private sector, as a general and voluntary subcontracting practice, to make greater use of small and small minority businesses. The committee's very composition--five members from large businesses and five members from comparatively small minority businesses--implies that the Congress expected that the committee members would have firsthand experience on how best to promote the products and services of small and small minority businesses in the private sector.

Confusion regarding the committee's purpose is reflected in the transcript of the April 1980 meeting. SBA's Associate Administrator for Minority Small Business and Capital Ownership Development stated that the committee's mission was to help with the marketing effort of eligible firms to do business with private sector firms. He added that SBA would like to take advantage of the many contacts the committee members had in the private sector in promoting this marketing effort. However, the Associate Administrator did not specify whether he thought the committee's role should be primarily directed at helping SBA promote small and small minority business subcontracting in the Federal sector, in accordance with section 8(d), or whether the committee should concentrate on promoting voluntary small and small minority business subcontracting in the private sector outside of Federal procurements.

During the meeting the question was raised as to whether the committee should get involved in promoting relationships between small and small minority businesses and big business

aside from Government contracting. Several members commented that they believed the committee's role was to help minority and other small businesses in obtaining greater participation in Government contracts. While this latter sentiment seemed to prevail, the committee did not discuss or resolve to develop any definitive strategy for working with SBA in promoting small and small minority business subcontracting in the Federal sector. Rather, the committee's resolution at the conclusion of the first meeting was to have SBA select 10 large Federal contracts awarded by the Departments of Defense and Energy and assess the adequacy of the subcontracting plans required by section 8(d). The apparent objective of this review was to determine whether the subcontracting plans made adequate provisions for the use of small and small minority firms. The results were expected to provide a basis for proposing suggestions to the President on ways to make the Federal subcontracting program more effective.

The committee held its second meeting on June 16, 1980. Because it was an open meeting and the subcontracting plans contain proprietary information they were discussed after the meeting. However, SBA's Director, Office of Capital Ownership Development, told us that no decision was reached on whether the committee would make any suggestions to the President.

During the June meeting, which we attended, several SBA officials briefed the committee on actions being taken to implement various provisions of Public Law 95-507. Again, considerable attention was focused on the Federal subcontracting provision contained in section 8(d). For example, several committee members suggested that SBA contact the 20 largest Federal procurement agencies to solicit their comments on the feasibility of requiring that small and small minority businesses be identified in the Federal subcontracting plans. Presently, the law requires that these plans include percentage goals for subcontracting with small and small minority businesses.

However, an initiative was taken at this meeting which we believe was more in keeping with the intent of section 7(j)(3). Specifically the Director, Office of Capital Ownership Development, presented a draft letter which he proposed be sent under the signature of the Committee Chairman to four large corporations as a pilot effort to promote procurement opportunities for small and small minority businesses. This

letter suggests that a meeting be arranged between SBA's management and the head of the corporations' procurement divisions to discuss these procurement opportunities. The Director told us that the Committee Chairman intends to send these letters. We believe this is precisely the type of effort that was intended under section 7(j)(3).

Because the Federal Government spends billions of dollars annually in private sector contracts (e.g., about \$82 billion in fiscal year 1979), we believe it is appropriate for the committee to consider ways to make the Federal subcontracting program more effective. However, we do not believe the Congress intended this to be the primary objective of the committee. Under section 8(d), SBA is given specific authority to monitor and evaluate Federal agency compliance with this subcontracting provision. Presumably, had the Congress intended this to also be the committee's primary mission it would have established the committee under section 8(d) rather than section 7(j)(3).

Accordingly, we believe the relationship between SBA and the committee in the future should focus primarily on exploring ways to promote subcontracting opportunities for small and small minority businesses outside of Federal procurements. This opinion is consistent with S. Rept. 95-1070, which, in referring to section 7(j)(3) states that the private sector holds the greatest potential for developing small and small minority businesses.

Actions SBA has taken to  
assist small and small  
minority businesses

In spite of the problems in implementing section 7(j)(3), SBA has taken several actions to help small and small minority businesses compete in the private sector. For example, in January 1980, it initiated a pilot marketing assistance program designed to assist 8(a) firms and other minority small businesses improve their marketing skills. The program uses experienced marketing volunteers who are retired executives from private industry. As of June 1980 SBA had implemented the program in six cities and plans to start the program in five others by the end of calendar year 1980. Staff in the Offices of the Associate Administrator for Minority Small Business and the Associate Administrator for Management Assistance will be responsible for monitoring and evaluating

the results of this program and for recommending whether to expand it nationwide.

In November and December 1979 SBA co-sponsored with the National Contract Management Association, which is made up of contracting personnel from both Government and industry, 1-day conferences in 13 cities. The conferences covered various aspects of Public Law 95-507 emphasizing the requirements for Government contractors to subcontract with small and disadvantaged businesses. SBA's Deputy Associate Administrator for Procurement Assistance told us that the conferences were well attended by the small and small minority business community. Also, SBA's Associate Administrator for Procurement Assistance stated that SBA and its field offices have co-sponsored similar seminars over the last year. In addition to these activities, SBA sponsored a seminar in Houston on June 14, 1980. An objective of the seminar was to inform small and small minority businessmen of the Federal subcontracting provisions contained in Public Law 95-507 and of the types of financial and management assistance SBA provides.

SBA is also in the process of finalizing a 1-year agreement with a major corporation to aid in the development of 8(a) firms which have demonstrated the capability of performing successfully on Government contracts. Under the agreement, SBA is to provide the corporation with selected firm profiles which corporate personnel will review, and whenever appropriate, make onsite visits to determine the firms' potential for becoming a corporate supplier. The corporation has agreed to keep SBA informed of what business it does with the firms. SBA is also negotiating similar agreements with four other corporations.

Aside from these initiatives, SBA is required under section 8(b)(2) of the Small Business Act to maintain a source list on small and small minority businesses having an interest in Government contracting or subcontracting. In accordance with this requirement, SBA, with the assistance of the Department of Energy, developed the Procurement Automated Sources System (PASS), which became operational in October 1978. Under PASS, small and small minority businesses complete a profile application specifying their size, capabilities, and prior experience. Once in the system, this information can be accessed through 39 display terminals and printers located at SBA regional offices and major purchasing centers of the



Department of Energy, select Government agencies, and Department of Defense installations. Through SBA's promotional efforts the system's inventory has grown from about 3,000 firms in 1978, to over 29,000 as of July 1980, including more than 5,000 minority-owned companies. SBA expects to have 50,000 firms in the system by 1982.

Although PASS was designed primarily for Government contracting, any private company or organization can use the system's data base by contacting SBA. At present, however, no private company has direct on-line access; although according to the Chief of SBA's Technology Assistance Division such access has been requested by approximately 100 private companies and Government agencies. He stated that in response to this interest SBA is developing a time-sharing plan whereby private companies and Government agencies would have direct terminal access and would be charged a fee based on actual usage. While we did not evaluate PASS, it seems to have considerable potential for marketing the goods and services of a large number of small and small minority firms in the private sector.

RECOMMENDATIONS TO SBA  
AND THE ADVISORY COMMITTEE

In accordance with the intent of section 7(j)(3), SBA and the Advisory Committee must jointly resolve how to best promote the goods and services of small and small minority businesses in the private sector. The Congress has given SBA the primary responsibility for ensuring compliance by Federal agencies with the subcontracting provisions of section 8(d). Because the Federal Government awards billions of dollars in contracts each year, we believe the Advisory Committee should be kept informed of Federal compliance with this section so that it will be in a position to suggest ways to make it more effective. However, greater attention needs to be given to promoting subcontracting opportunities for small and disadvantaged firms outside of Government procurement. The vast marketing opportunities in the private sector is where we believe the Congress intended, under section 7(j)(3), that the Advisory Committee and SBA concentrate their attention.

Accordingly, we recommend that the Administrator of SBA together with the Advisory Committee develop a specific plan for promoting private sector procurements from small and small minority businesses. This plan should include specific

functional responsibilities of both SBA and the Advisory Committee, specific short-range goals, and a monitoring and evaluating component, so that problems impeding its implementation can be identified and resolved. Also, in developing the plan, SBA and the Advisory Committee should consider expanding those activities already initiated by SBA, such as seminars, personal contacts with chief executive officers of major corporations, and private sector use of PASS. Finally, because the resources of the committee and SBA are limited, the feasibility of enlisting the support of outside organizations concerned with developing small and small minority businesses should be assessed.

We believe that by taking these steps, SBA and the Advisory Committee will be in a better position to report to the President and the Congress on their success in developing private sector procurement opportunities for small and small minority businesses. Also, the experience gained by implementing such a plan should provide additional insight into the types of incentives appropriate for training and upgrading potential small and small minority subcontractors consistent with the intent of section 7(j)(3).

We asked SBA to review the draft of our report. SBA said the report accurately documented problems experienced in implementing the subcontracting program and agreed with our overall conclusion that greater attention needs to be given to promoting subcontracting opportunities for small and small minority firms in the private sector. SBA said that the report and our recommendations will be discussed with members of the Advisory Committee.

SURETY BOND WAIVERS FOR  
CERTAIN 8(a) CONTRACTORS

SBA has been slow to implement the Public Law 95-507 provision which authorizes the SBA Administrator to waive any bond required by a Government procurement officer for and in connection with any 8(a) contract. The Administrator may waive the bond requirement on an 8(a) contract only if

- SBA takes appropriate measures to protect laborers and suppliers under the contract;

- SBA assists the business to develop, within a reasonable time, such financial and other capabilities needed to obtain surety bonds;
- SBA determines that the small business cannot obtain a bond from a surety with or without an SBA guarantee; and
- the small business is a start-up concern and has not participated in the 8(a) program for more than 1 year.

SBA Has Been Slow to Implement  
the Surety Bond Waiver Provision

Although Public Law 95-507 was enacted on October 24, 1978, SBA did not publish proposed rules and regulations for implementing the surety bond waiver provision until April 4, 1980--17 months later. SBA has received several sets of comments on the proposed rules and regulations, and officials hope to have them finalized sometime in the near future.

A major cause for the delay in implementing the surety bond waiver provision appears to be a disagreement or misunderstanding between two SBA offices--the Office for Minority Small Business and Capital Ownership Development (OMSB) and the Office of Special Guarantees. Public Law 95-507 clearly places responsibility for the surety bond waiver provision with OMSB. On the other hand, the Office of Special Guarantees administers SBA's Surety Bond Guarantee Program and therefore has personnel with surety bonding knowledge. OMSB personnel have relied on the Office of Special Guarantees to get the surety bond waiver provision off the ground. However, Office of Special Guarantee personnel did not take any action since they view their office as playing the role of a technical advisor and not having any direct responsibility for implementing or administering the surety bond waiver provision.

OMSB's priorities have also contributed to the delay in implementing the surety bond waiver program. OMSB officials decided that certain other Public Law 95-507 provisions deserved priority attention. Thus, the surety bond waiver provision fell by the wayside for a period of time.

Use of the Surety Bond  
Waiver Will Be Limited

The Director, Office of Capital Ownership Development, said he believed that surety bond waivers will be issued very infrequently. He pointed out that SBA approves about 98 percent of all surety bond guarantee applications. When the bond waiver eligibility criteria are applied to the remaining 2 percent, very few contractors will even qualify for a bond waiver.

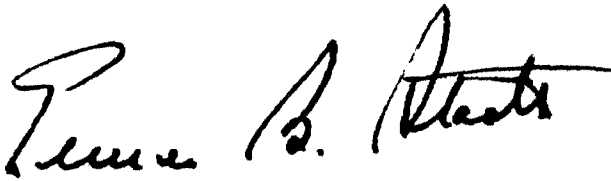
CONCLUSIONS AND RECOMMENDATIONS TO SBA

We recognize that since the Office of Special Guarantees has some surety bonding expertise, OMSB will have to closely coordinate with it. Also, many if not all of the waiver referrals will probably come from the Office of Special Guarantees. Since confusion or disagreement between these two offices has significantly contributed to the delay in implementing the surety bond waiver provision, we recommend that the SBA Administrator clearly define the roles of these two offices in order to prevent any additional delays. We also recommend that when SBA issues instructions for the waiver program, they should spell out the process for identifying and referring potential waiver candidates to the appropriate office for consideration.

SBA agreed that the roles of the two offices need to be clearly defined. Also, SBA said that it intends to issue an instruction which will include procedures for identifying and referring potential bond waiver candidates.

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We are sending copies of this report to the Administrator, Small Business Administration; the Director, Office of Management and Budget; and other interested congressional committees and individuals.

  
Comptroller General  
of the United States