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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

The SBA 8(a) Procurement Program--A Promise Unfulfilled

The Small Business Administration's 8(a) Procurement Program gives noncompetitive Government contracts and other aid to help disadvantaged business owners become self-sufficient. Few aided firms have graduated as competitive businesses. The bulk of 8(a) contracts has gone to a select group of firms. Many firms have not built up commercial sales, rely on 8(a) contracts, and view the program as an end in itself.

SBA is reluctant to remove from the program firms that are needed to meet yearly contract volume goals. Because of this, other disadvantaged firms cannot participate. Insufficient staff, vague graduation criteria, and poor records also hamper the program's effectiveness. Further, the small business community is concerned about the program's future impact on its businesses.

GAO proposes several alternatives and recommendations to restructure the 8(a) program and resolve its problems.

UNITED STATES GENERAL ACCOUNTING OFFICE

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COMPTROLLER GENERAL OF THE UNITED STATES
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To the President of the Senate and the
Speaker of the House of Representatives

This report, which was prepared pursuant to Public Law 95-507, discusses the Small Business Administration's implementation of the 8(a) Procurement Program. The report discusses the need for better management of the program and recommends that the Small Business Administration make a number of improvements.

This report is one in a series under Public Law 95-507. We are sending copies of this report to the Director, Office of Management and Budget, and the Administrator of the Small Business Administration.

Milton J. Socolar
Acting Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

THE SBA 8(a) PROCUREMENT PROGRAM--A PROMISE UNFULFILLED

D I G E S T

The Small Business Administration's (SBA's) 12-year old 8(a) Procurement Program is designed to channel noncompetitive Federal contracts to disadvantaged small businesses to help them become self-sufficient. The program also provides management, technical, marketing, and financial aid. Over the years, 4,598 participating firms have received 8(a) contracts totaling $5.5 billion.

However, the Government's endeavor to introduce disadvantaged entrepreneurs into the economic mainstream has remained a promise unfulfilled. Redirecting the program could free up the limited staff to better serve program participants, provide an opportunity for other disadvantaged firms to participate, and enhance the program's credibility within the small business community.

8(a) PROGRAM'S LIMITED ACHIEVEMENTS

On the positive side, the program has had some benefits. The formation of many disadvantaged firms was spurred on by the program, and some of the more than 2,000 active 8(a) firms are continuing to operate because of the program's support. Participants also gained experience in managing a business. Lastly, being certified as 8(a) helped some firms get other commercial and non-8(a) Government work. (See pp. 42 to 45.)

But the program has fallen short of its intended goal. According to SBA statistics, only 166 of the 4,598 participating firms graduated from the program as competitive businesses. A large volume of 8(a) contracts--more than $1.7 billion, or 31 percent, of the total $5.5 billion--went to 50 firms which continue to be active participants. Over three-fifths of these firms have been in the program between 7 and 11 years. (See pp. 7 to 11.)

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FACTORS IMPEDING PROGRAM'S EFFECTIVENESS

GAO believes that several interrelated factors have limited the program's effectiveness. The major factor is the President's yearly 8(a) contract goal imposed on SBA, which has become the dominant force behind the program and has clouded its intended goal of developing competitive disadvantaged firms. Other factors handicapping the program's effectiveness include

--vague program graduation criteria,

--missing business plan and financial statement data, and

--limited staff resources.

The limited staff was discouraged from graduating competitive firms since these very firms made it easier to meet the yearly 8(a) contract goals. Without adequate data and graduation criteria, the staff could not even begin assessing the status of many firms. In GAO's opinion, SBA has functioned as a contract broker between Federal buying agencies and the participating firms. Because of these factors, it is doubtful whether the expanded business development envisioned when legislation was passed will become a reality. (See pp. 24 to 33.)

HARD CHOICES AHEAD

The program's problems have been known for years. Criticism, mostly justified, has come from many sources, yet meaningful corrective action has not been taken. Decisions about the future of the 8(a) program must be made. The merits of a properly administered and structured program to aid disadvantaged businesses in gaining a toehold in the competitive marketplace cannot be emphasized enough. However, the program should be structured so that it is accepted by both the disadvantaged and nondisadvantaged small business communities. This acceptance will occur if SBA can demonstrate that 8(a) firms will not remain in the program indefinitely.

--Replace the 8(a) program because of the many problems discussed in this report. SBA would no longer act as prime contractor. Instead, contracts to disadvantaged firms would be awarded through a separate disadvantaged small business set-aside program.

RECOMMENDATIONS TO THE SBA ADMINISTRATOR

The SBA Administrator should take several actions to immediately strengthen the management of the program and protect the interests of both disadvantaged and nondisadvantaged small businesses. These recommendations, if implemented, should minimize some of the problems noted by GAO and others and provide adequate safeguards for other small businesses. (See pp. 38 and 53.)

SBA COMMENTS AND GAO's EVALUATION

SBA generally agreed with GAO's recommendations to the Administrator for improving the 8(a) program. However, SBA did not think that the last three of GAO's alternatives for changing the program's direction were appropriate.

GAO continues to believe that the three alternatives represent valid ways to redirect the 8(a) program's emphasis. (See pp. 38 to 40.)

Contents

CHAPTER 1

INTRODUCTION

On October 24, 1978, the President signed Public Law 95-507 which amended the Small Business Act. The new law requires us to evaluate several Small Business Administration (SBA) programs designed to aid socially and/or economically disadvantaged people.

This report, one in a series issued pursuant to Public Law 95-507, deals with SBA's procurement program authorized by section 8(a) of the Small Business Act.

BACKGROUND ON 8(a) PROGRAM

Section 8(a) of the Small Business Act of 1953 contained the original authority for a program to help small businesses. SBA first used the 8(a) authority to support a test program initiated as a result of the 1967 civil disturbances. In 1968 SBA offered noncompetitive contracts to any small business that agreed to locate in depressed areas and hire the unemployed and underemployed. The test program was generally unsuccessful since few small businesses were willing to relocate. In 1969 SBA began operating an 8(a) program designed to channel noncompetitive contracts to disadvantaged small businesses.

SBA acts as a prime contractor for Federal departments and agencies and fulfills the prime contracts by subcontracting the work to eligible firms. The program also offers management, technical, financial, and marketing aid to firms. SBA envisioned that firms participating in the program would use the aid to develop into self-sufficient firms capable of competing in the marketplace without 8(a) support.

When Public Law 95-507 was passed, the Congress for the first time endorsed SBA's stated purpose of section 8(a) to

"(A) foster business ownership by individuals who are both socially and economically disadvantaged;

"(B) promote the competitive viability of such firms by providing such available contract, financial, technical, and management assistance as may be necessary; and

"(C) clarify and expand the program for the procurement by the United States of articles, equipment, supplies, services, materials, and construction work from small business concerns owned by socially and economically disadvantaged individuals.

Business development specialists (BDSs) usually assigned to district offices are responsible for the day-to-day monitoring of 8(a) firms and form the focal point of the program. Standard Operating Procedure (SOP) 80-05, issued in September 1979, in response to Public Law 95-507, expanded and clarified the business development function of the 8(a) program and enlarged the role of the BDS. Some of the BDS's major tasks are

--reviewing and processing initial eligibility and business plan material from new applicants, analyzing applicants' financial statements, making eligibility recommendations, and writing reports;

--servicing a portfolio of active 8(a) firms by conducting quarterly field visits and preparing reports, analyzing financial statements, resolving problems, and providing firms with management, marketing, technical, financial, and procurement aid;

--working with SBA procurement center representatives, agency procurement personnel, and contracting specialists to identify requirements suitable for firms and matching an 8(a) firm's capabilities with proposed contracts;

--determining whether proposed 8(a) firms have the financial resources necessary to perform contracts and possess the technical and management capabilities for contract performance;

--addressing industrywide problems and assessing the total effectiveness of the 8(a) program, its limitations, and any redirection needed;

--participating as a key voting member of the district committee in the required annual review of 8(a) firms to identify candidates for graduation or termination; and

--getting support for the 8(a) program from State legislatures, the private sector, and civic, trade, and business associations.

Preparing business plans

The cornerstone of the program is the business plan prepared by the 8(a) firm and approved by SBA. The plan is a comprehensive document that identifies the resources needed to become a self-sustaining profit-oriented small business. The plan enables SBA to identify the types of management assistance needed by the firm to help it overcome its business deficiencies.

--determine the adequacy of SBA's administration and monitoring of the 8(a) program;

--assess the basis and reasonableness of 8(a) program goals, the adequacy of business plan preparation, and the 8(a) program's impact on the market of nondisadvantaged small businesses; and

--identify workable alternatives for improving the program's effectiveness.

To meet these objectives, we obtained program data at SBA's central office. At SBA's Atlanta, Chicago, Philadelphia, and San Francisco district offices, we analyzed the business development files for selected 8(a) firms, assessed the amount of contract support and other financial and management services provided by SBA, and solicited comments from officials of 8(a) firms and nondisadvantaged small businesses. Chapter 4 gives further detail about the scope and methodology of our review.

Other objectives, such as assessing 8(a) eligibility and the adequacy of SBA controls over advance payments and business development expense, were initially surveyed but were not included in our review because the issues were recently reviewed by SBA's Office of Inspector General.

merely acting as a link between the Federal buying agency and the 8(a) firms.

THE HISTORY OF THE 8(a) PROGRAM-- FEW SUCCESS STORIES

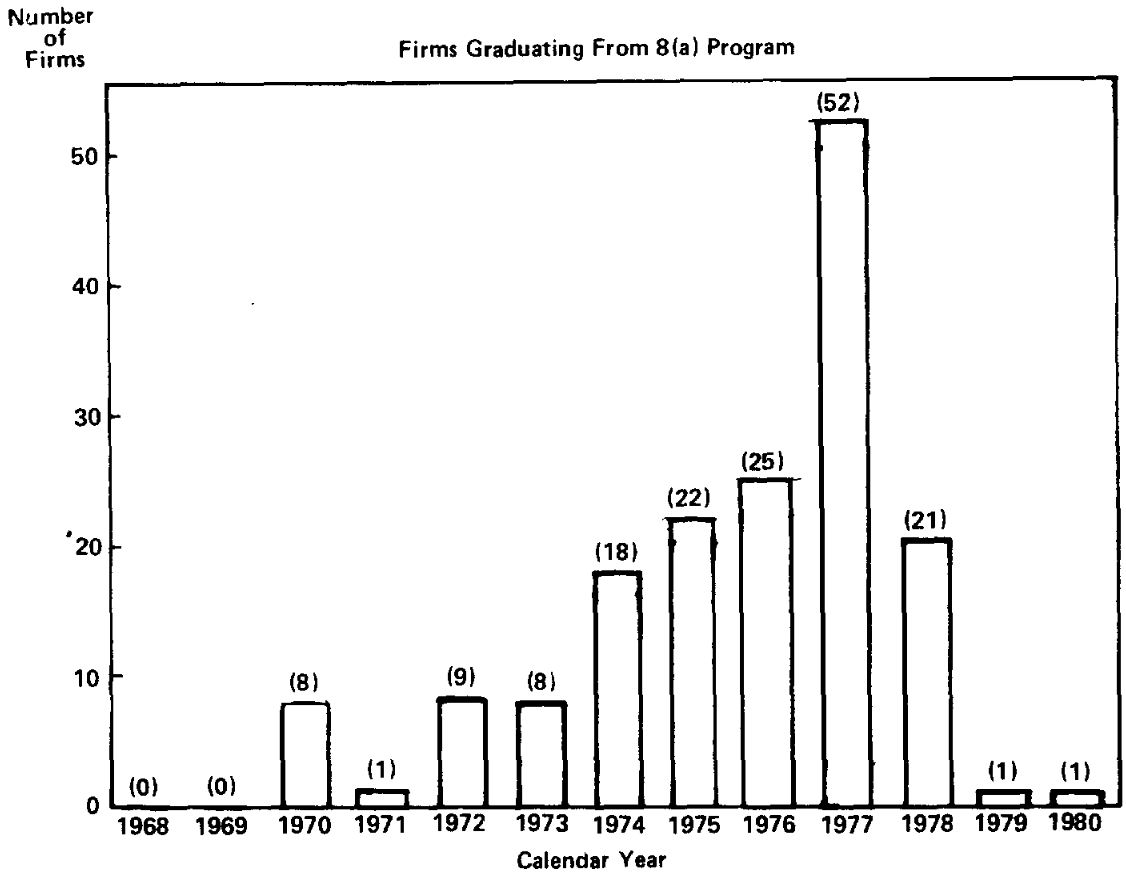
SBA has had little success in helping disadvantaged small businesses become self-sufficient without relying on 8(a) contract support. Only 166, or less than 4 percent, of the 4,598 firms admitted to the program over the years have graduated as competitive and self-sufficient businesses. The following table shows the status of the 4,598 program participants as of September 30, 1980.

Year firms admitted	Program graduate	Voluntarily withdrew (note a)	Discon- tinued	Out of business	Active	Total
1968	1	5	6	3	1	16
1969	1	3	5	9	2	20
1970	29	88	172	82	66	437
1971	50	105	285	81	163	684
1972	59	148	410	106	198	921
1973	14	74	199	45	149	481
1974	7	29	147	27	144	354
1975	3	37	76	21	187	324
1976	2	23	53	13	229	320
1977	0	4	16	2	153	175
1978	0	7	5	6	297	315
1979	0	2	0	0	279	281
1980	0	0	0	0	270	270
Total	166	525	1,374	395	2,138	4,598

a/Firms voluntarily withdrew primarily because of dissatisfaction with the 8(a) program. Some firms were not satisfied with the number of contracts provided by SBA. Other firms were unhappy with the prices negotiated on 8(a) contracts or were dissatisfied with the management assistance furnished by SBA.

An SBA headquarters official in the Eligibility Division told us that the 1,374 discontinued firms consist mostly of firms terminated because they no longer met the social or economic eligibility standards or because they did not comply with the program's reporting requirements.

The lack of program graduations was evident at the four districts visited. The following table shows the number of graduates by district through September 30, 1980.



Between January 1979 and September 1980, only two firms left the program as competitive businesses. The virtual cessation of graduating firms resulted mostly because required annual reviews were not always made. SBA procedures require that each firm's progress be reviewed annually. At these reviews, decisions are made to graduate, terminate, or retain firms. However, only 7 of 75 firms in the Chicago and Philadelphia districts analyzed by us had received an annual review since the end of 1978. In Atlanta, 17 of 30 firms requiring reviews were past due for such evaluations. Lastly, an internal SBA study noted that only 27 of 100 firms in the San Francisco district had been reviewed between January 1978 and October 1979.

For example, in the Philadelphia district, none of the 39 firms we analyzed had an annual review between November 1978 and September 1980. The Philadelphia Chief of the Office of Business Development told us that the emphasis on annual reviews lessened shortly before Public Law 95-507 was passed because SBA expected changes in 8(a) eligibility requirements. After the law's passage in October 1978, the required annual reviews still were not made because a new SOP was anticipated. But the new SOP 80-05 was not published until September 1979 and not actively implemented until January 1980. As a result, no firms in the Philadelphia district have received the required annual reviews for almost 2 years.

In our opinion, the major reason why certain firms receive the bulk of 8(a) contract dollars is to help SBA meet its contract goal. The following is an example of such a firm.

--An 8(a) firm in the Philadelphia district has been in the program more than 8 years and received $31.5 million of contract support, $75,000 in advance payments, $168,000 of business development expense, and $400,000 in SBA loans through September 1980.

The firm is one of ten 8(a) firms providing general construction services in the Philadelphia area. However, the firm received 76 percent of the total $41.7 million of 8(a) contracts for general construction.

In March 1978, the Assistant District Director told the firm to concentrate on large procurements because the firm's self-marketing resulted in the firm getting smaller projects that were within the capabilities of other general contractors unable to obtain adequate support.

On three separate occasions, the firm had been scheduled for graduation. In March 1977, because of the pending graduation, a waiver was granted to award an additional $2 million above the firm's business plan projection. The BDS stated: "This figure is based on current and anticipated requirements, and it would enable the firm to strengthen its competitive position as it enters its Post-8(a) Phase." However, the BDS told us that the firm was the only firm with a bonding capacity to handle large construction jobs. Consequently, the district decided to retain the firm since the loss of the large construction contracts would create problems in meeting the district's 8(a) contract goal.

ANALYSIS OF FIRMS IN THE FOUR DISTRICTS

We identified 75, or 28 percent, of the 267 firms in the program as of March 31, 1980, at the four districts visited whose continued participation in the 8(a) program appears questionable. Twenty-two firms obtained 8(a) contracts and generated non-8(a) sales that sometimes exceeded the firms' business plan projections. An additional 27 firms depended heavily on 8(a) sales. These firms' commercial sales were substantially lower than business plan projections. Another 26 firms had business plan projections for 8(a) contracts that did not materialize. An additional 77 firms we analyzed were not classified because files were lost or lacked significant data, firms went out of business or moved, or firms' sales patterns were too erratic.

Years in program	8(a) history: Actual contracts	8(a) history: Actual vs BP projections Initial	8(a) history: Actual vs BP projections Revised	Non-8(a) history: Actual sales	Non-8(a) history: Actual vs BP projections Initial	Non-8(a) history: Actual vs BP projections Revised
		(percent)			(percent)	
8	$ 523,910	121	84	$1,765,128	143	78
5	14,970,686	214	192	5,988,776	256	289
8	15,118,418	265	140	3,761,933	70	96
9	1,695,710	224	134	2,242,875	96	111
8	4,143,257	288	274	1,314,213	85	101
5	1,880,685	109	109	3,574,912	158	158
6	4,070,983	219	161	619,657	93	104
7	2,780,732	107	96	1,594,891	100	97
7	470,715	199	36	662,983	77	43
9	1,372,154	283	134	1,569,106	115	85
3	692,375	216	141	1,772,818	171	114
4	170,272	275	275	779,102	87	87
5	2,852,216	407	154	3,770,006	79	118
10	8,686,773	144	117	4,539,664	74	95
4	521,267	401	134	220,774	87	82
7	1,180,909	115	38	4,539,857	64	102
5	557,715	223	139	1,136,571	223	130
4	6,013,183	802	89	6,547,141	74	124
5	2,318,838	259	160	389,944	76	76
4	519,372	226	115	1,646,742	95	95
2	2,172,522	207	207	3,057,262	113	113
6	111.551	130	98	1,060,284	95	90

Sixteen of the 22 firms have been in the program 5 or more years. In addition, 10 of the 22 firms had been recommended for graduation by district officials. Records generally were not available to determine why graduation recommendations were not carried out. Two case studies illustrate typical firms falling into this category.

Firm No. 18--A Philadelphia district professional service firm

This firm entered the 8(a) program in December 1975. The firm has obtained $6,013,000 in 8(a) contracts, which represents 802 percent of the initial projection of $750,000. The $6,547,000 of non-8(a) sales represents 74 percent of the firm's initial projection of over $8.8 million.

The firm was initially rejected in November 1975 because the owner's net worth was considered excessive and because the company had already developed a commercial business. One month later, the firm got 8(a) program approval limited to 2 years. The Assistant Regional Director commented:

> "* * *this firm was recently acquired by a disadvantaged person, (therefore) a valid possibility exists that the firm cannot maintain its current position. In view of this possibility, it is believed that enrollment in the 8(a) program would assist this firm, under its present ownership, during the initial stage of development under new management."

As of September 30, 1980, the firm continues in the 8(a) program and has projected a need for $3.5 million in 8(a) contracts for fiscal years 1981 and 1982.

Firms heavily dependent on 8(a) sales

We classified 27 firms in this category because 8(a) contracts generally represented more than 50 percent and non-8(a) sales represented less than 20 percent based on either initial or revised business plan projections. Some firms in this category had non-8(a) sales higher than 20 percent but showed evidence of declining non-8(a) sales. When firms are admitted into the program, getting 8(a) contract support is intended to improve the firm's competitive status. Over time, the proportion of 8(a) contracts to total sales should decrease because firms are supposed to identify and rely to a greater degree on commercial and non-8(a) Government sales obtained competitively.

The sales history for the 27 firms is shown in the following table:

		8(a) history			Non-8(a) history		
			Actual vs BP projections			Actual vs BP projections	
Firm	Years in program	Actual contracts	Initial	Revised	Actual sales	Initial	Revised
			(percent)			(percent)	
1	3	$ 254,712	47	51	18,875	5	7
2	4	12,089,837	105	105	-0-	0	0
3	4	5,638,665	52	61	-0-	0	0
4	9	10,033,065	177	106	418,792	6	18
5	6	1,452,466	113	85	127,980	3	4
6	4	3,715,769	66	65	130	0	0
7	5	3,071,955	164	97	453,338	50	33
8	6	2,652,339	101	84	466,756	20	42
9	7	12,377,508	447	142	2,204,102	14	46
10	2	2,934,998	92	92	1,817	0	0
11	9	5,724,706	105	121	709,635	22	19
12	7	17,111,080	115	126	896,430	19	27
13	7	1,637,236	277	170	156,444	16	23
14	9	4,859,013	89	88	688,328	19	18
15	7	3,020,678	111	85	1,013,913	40	34
16	10	8,587,390	113	113	2,057,122	19	19
17	4	747,335	100	79	-0-	0	0
18	4	1,019,960	113	60	579,321	10	12
19	10	453,231	94	54	319,293	19	82
20	6	3,932,384	116	66	68,943	7	9
21	10	16,928,535	79	109	1,550,190	7	8
22	10	11,041,226	119	141	1,090,121	16	17
23	7	633,136	136	151	151,135	23	24
24	4	1,755,659	1,170	540	[illegible]4,588	34	34
25	9	12,460,932	248	229	1,044,436	31	31
26	4	254,023	170	170	104,878	20	8
27	8	1,430,159	72	89	449,222	30	46

While the lack of a commercial market was of some concern to SBA, decisions to retain the firm were made during the 1975 and 1977 annual reviews. Another possible problem was expressed by the BDS during the 1977 annual review. He wrote:

> "When [the] firm does present itself to an Agency, an Agency usually wants [the] firm but wants to go 8(a). This is penalizing the firm in its ability to acquire non-8(a) work."

The Assistant District Director, in November 1979, suggested that the firm consider diversifying into hardware manufacturing as a vehicle for developing a commercial market. The firm did not make the transition and continues to rely solely on the 8(a) program for sales support.

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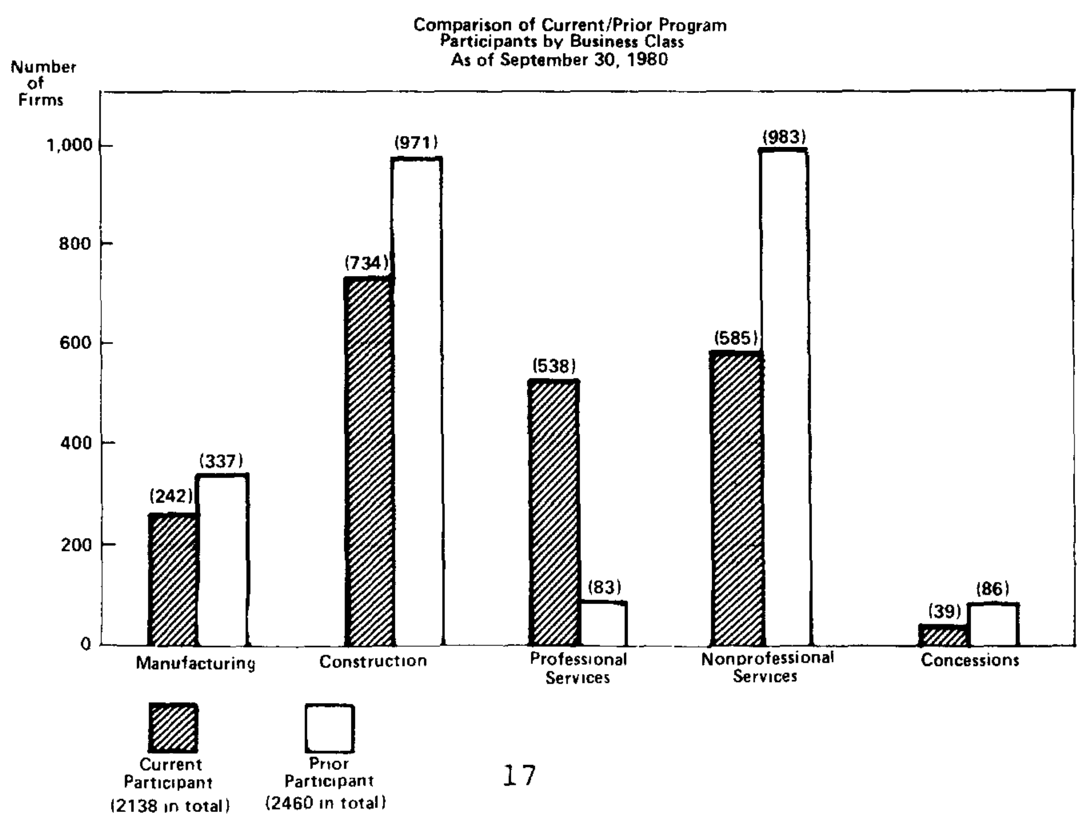
As the above cases show, some firms tend to rely on 8(a) contract support after program admission. SBA is faced with the task of continuing contract support for such firms via the artificial market of noncompetitive 8(a) contracting. The SBA headquarters Chief of the Requirements Division told us that this practice was especially true for professional service firms. He said that many of these firms claim that they do not have an available commercial market. He believes the firms should not have been accepted in the program. A Philadelphia regional official, in correspondence to SBA headquarters, noted that professional service firms had to be retained in the program because they have limited opportunities to generate commercial sales. The following chart compares current and prior firms nationwide for the five classes of businesses.



"'If he has any problems, we try to rush in and smooth them out: Make him a loan, mollify the Air Force, whatever. Our measure of success in 8(a) is supposedly viability--enough cash in the business to bond, enough knowledge to function effectively and independently and a willingness to grow in the commercial market. The shrewd companies get addicted to the program and learn to draw all their money out each year. That way they never become viable and we always have to give them more money.'"

* * * * *

"'And what happens to what was originally a sound company after a few years of this? He doesn't know the commercial business any more; all the contractors he dealt with before have moved on. He's lost the attitude, 'I have a business to build' and instead he basically reverts to a job mentality.'"

Firms getting little or no 8(a) contracts

We classified 26 firms in this category because the 8(a) contract support they received was generally less than 20 percent of the firm's business plan projections. When firms are admitted into the 8(a) program, it is expected that SBA has the available contracts and other assistance to support the firm. The sales history for the 26 firms is shown in the following table:

		8(a)history			Non-8(a) history		
			Actual vs BP projections			Actual vs BP projections	
Firm	Years in program	Actual contracts	Initial	Revised	Actual sales	Initial	Revised
			(percent)			(percent)	
1	4	$ 24,000	6	6	-	-	-
2	6	30,428	12	12	7,941	64	64
3	4	57,041	21	13	1,408,419	92	95
4	7	-0-	0	0	31,921	79	62
5	4	355,885	10	9	2,454,798	55	70
6	4	35,169	9	19	-	-	-
7	3	-0-	0	0	-	-	-
8	2	-0-	0	0	737,406	151	151
9	4	70,444	5	10	760,071	33	50
10	6	39,204	6	2	-	-	-
11	5	1,075	0.4	0.2	-	-	-
12	3	-0-	0	0	-	-	-
13	6	20,405	0.6	1	1,852,155	41	54
14	4	-0-	0	0	-	-	-
15	4	-0-	0	0	-	-	-
16	3	45,288	14	16	-	-	-
17	2	-0-	0	0	-	-	-
18	8	-0-	0	0	-	-	-
19	8	-0-	0	0	-	-	-
20	2	95,896	21	11	-0-	-0-	-0-
21	10	183,596	8	9	75,685	3	3
22	10	5,985	0.6	0.6	11,461,009	141	141
23	6	10,582	1	1	952,852	60	61
24	8	18,000	0.8	0.6	4,148,907	72	88
25	7	185,236	8	13	1,547,398	59	53
26	3	104,884	11	11	-	-	-

list" of 8(a) firms whose specialties or skills are not conducive to 8(a) procurements. He said that if the region cannot find adequate 8(a) contracts for these firms, it intends to remove them gradually.

Firms unclassifiable

A total of 77 firms, or 29 percent, of the 267 firms analyzed could not be readily classified. The business development files for most of these firms lacked so much required data that decisions could not be reached on their status. Other firms were not classified because the business development files could not be located, they had gone out of business or moved to a different SBA district, or their sales patterns were too erratic.

The following case studies illustrate firms whose status could not be classified.

A Philadelphia district professional service firm

This firm entered the program in March 1970. Between 1971 and 1978, this firm received $4 million in 8(a) contract support. In 1979 it received one contract for $19,000. However, in June 1980 it received a $9.3 million contract which was double the value of all the 8(a) contract support previously received. Interestingly, the firm's 8(a) sales projection for 1980 was $750,000. Data through 1978 shows that 8(a) sales made up 96 percent of the firm's total sales, with no commercial sales recorded for 1976-78. Between 1972 and 1975, the firm's annual commercial sales were less than $3,000. While no financial data exists beyond June 1978, we believe this trend probably has continued into 1980.

In an August 1975 financial review, SBA said that the "corporation is virtually insolvent" and that "previous experience indicates that even with 8(a) contract support they have been unable to turn this into a profitable business." In the December 1975 annual review, comments such as the following were made.

"* * *has lost all capability of getting other than 8(a) work* * *."

"* * *continuation of company depends 100 percent on SBA and the bank* * *."

SBA concluded that the "firm's inability to develop a commercial market was a major problem" and recommended that the firm "be terminated from the 8(a) program at the end of the fiscal year."

The July 1977 annual review echoes the 1975 review: "* * * unable to develop a commercial market* * *" and "* * * unless firm shows some semblance of a non-8(a) market by the end of this FY, I would recommend termination."

A Deputy Assistant Director of the Department of Commerce's Minority Business Development Agency estimates that as many as 40,000 minority firms provide goods and services required by the Government. We assume that many of these firms would welcome the opportunity to get 8(a) contracts on a noncompetitive basis and access to other Federal financial and management aid. However, the doors of the program will remain closed to these firms as long as SBA continues on its present path of not graduating competitive firms or terminating questionable firms.

A number of respondents to our notice published in the "Commerce Business Daily" in September 1980 complained about not being admitted into the 8(a) program. The rationale for using the notice to reach the small business community is explained in appendix III. Although the notice was specifically addressed to 8(a) participants and nondisadvantaged small businesses, 32 of the 224 letters received were from firms, some owned by women, claiming to be disadvantaged and seeking 8(a) admission. The following statement from the President of a Colorado firm is an example of the comments received.

> "About 2 years ago, we decided to make application to participate in the 8(a) program, which at a minimum would keep us from being frozen out of business we already had and were performing successfully. After a very frustrating 6 months of trying to correctly complete an entire application with all the documentation required, and through one appeal process, we were essentially rejected for participation in the program because of a lack of evidence that contract support would be available to us as a result of commitment to other 8(a) firms in a same or similar line of business.
>
> "To illustrate the impact of this lack of a graduation system, we wish to cite as examples four firms, that we know very well, because we have competed with them frequently over the years. They shall remain unidentified since we really do not want to pick on them specifically as there may be many more concrete examples.
>
> Firm A - Has been in the 8(a) program at least 10 years to our knowledge. Between 7/1/77 and 6/30/80, this firm was awarded 32 8(a) contracts totaling $6,554,586.
>
> Firm B - Has been in the 8(a) program at least 7 years to our knowledge. Between 7/1/77 and 6/30/80, this firm was awarded 15 8(a) contracts totaling $6,082,831.

position in the marketplace. It is not intended that 8(a) subcontracts would support a company indefinitely, but rather should serve as an adjunct to assist in its development."

Public Law 95-507, enacted in 1978, endorsed SBA's stated goal of using the program to promote the competitive viability of disadvantaged small business. The statute implied that assisted small businesses should eventually graduate from the program.

However, SBA must meet another goal that differs drastically from the goal of developing competitive 8(a) firms. In recent years, the President has established a Government-wide goal for purchasing goods and services from disadvantaged businesses. The 1980 fiscal year goal set by the President totaled $3.8 billion. Of this amount, a $1.6 billion goal was established for SBA 8(a) contracts. The remaining $2.2 billion was to come from direct prime contracts and subcontracts awarded to disadvantaged firms by Federal agencies and prime contractors.

SBA was successful in placing over $1.6 billion during fiscal year 1980, which is a 61 percent increase over SBA's accomplishment of slightly more than $1 billion during fiscal year 1979. The following chart depicts how the 8(a) contract volume has expanded since fiscal year 1969.

Closely linked to the expanding contract volume goal, SBA also had a goal to have 2,130 firms in the program by the end of fiscal year 1980. SBA met this goal by having 2,138 active firms as of September 30, 1980.

The President recently announced a fiscal year 1981 goal of $4.2 billion for contracts with disadvantaged businesses. SBA's goal for the 8(a) program was set at $1.5 billion, or about $100 million less than the 1980 goal accomplishment.

8(a) program success measured by wrong goal

The award of increasing amounts of 8(a) contracts has become the single most important measure of the 8(a) program's success. Region and district officials generally agreed that the contract volume goals are contrary to the business development objectives of the program.

Atlanta regional officials, for example, were outspoken in their criticism of the situation and said that because of contract goals, business development had to take a back seat. The Assistant Regional Administrator told us that his performance rating and future salary increases will be predicated on his ability to achieve contract volume goals. He believes his performance should be measured by the number of competitive businesses he can develop.

A San Francisco District Supervisor told us that the increasing contract volume goal means that SBA needs 8(a) firms in the program more than the firms need SBA. The Regional Administrator and District Director in Philadelphia both agreed that developing and graduating competitive firms, rather than meeting contract goals, should form the basis for assessing performance. The Chicago Assistant Regional Administrator told us that increasing contract volume goals have lessened the capability of BDS staff to service active 8(a) firms.

Lastly, the SBA headquarters Chief of the Requirements Division advised us that the present 8(a) program functions as nothing more than a "contract broker" for disadvantaged firms. He added that if SBA was truly working to develop competitive businesses, the 1980 goal for 8(a) contracts would have been $500 million rather than $1.6 billion.

MEETING THE BUSINESS DEVELOPMENT GOAL IS DIFFICULT BECAUSE OF STAFFING PROBLEMS

The limited BDS staff assigned to the 8(a) program, required to perform numerous duties including special projects, have been hindered from monitoring the business development of active 8(a) experience. The director added that most were outreach workers in other programs before becoming BDSs. Regional officials labeled the current situation of static resources as "potentially chaotic." They said that a caseload of about 10 active firms per BDS would be ideal. BDSs were only able to visit 3 of the 40 active firms during the past 6 months.

In the San Francisco district office, three BDSs were serving 114 active firms. However, two BDSs have not been trained for the position. The one trained BDS told us that 90 percent of her normal work week is devoted to processing new applications. During the past year, she has not had time to perform any field visits. She believes an ideal caseload would be about 20 active firms.

Chicago and Philadelphia regional and district officials told us that they also experienced problems, such as insufficient and poorly trained staff. They told us that required field visits were not always made and agreed that about 10 firms would be an ideal case load for a BDS. They also stressed that special projects, such as recertifying eligibility based on Public Law 95-507, take BDSs away from their normal duties. In August 1980 the Philadelphia Assistant Regional Administrator estimated that an additional 11 BDSs would be needed by his districts to handle the fiscal year 1981 workload.

Like SBA managers, BDSs are pressured to meet the 8(a) contract volume goals. Accordingly, assessing the progress of 8(a) firms and identifying their developmental needs receives a low priority. Because of the shortage of BDSs, the Philadelphia District has issued management assistance contracts for consultants to conduct field visits to evaluate 8(a) firms and identify the types of assistance needed.

To achieve the President's goal of $1.5 billion in 8(a) contracts, it is highly unlikely that the expanded developmental services envisioned under Public Law 95-507 will be provided by the understaffed and overworked BDSs during fiscal year 1981.

Interestingly, the inability of the BDSs to service the needs of the firms does not appear to cause any significant hardships to 8(a) program participants. For example, the Philadelphia District Director told us that 90 percent of the firms in his district view the program not as a business development program but more as a vehicle for getting 8(a) contracts. Our telephone survey asking officials of 8(a) firms to comment on SBA's administration generally confirmed the District Director's comment. (See app. II.) When asked to identify the most valuable type of aid that SBA could provide, the 316 responding firms answered:

b. A comparison of the 8(a) concern's business and financial profile with profiles of comparable non-8(a) small businesses in the same activity or similar business category.

c. Management capacity, and capability."

The SBA headquarters Chief of the Eligibility Division told us that applying the above criteria is entirely subjective. He added that SBA has contracted with an 8(a) consulting firm to develop more objective criteria for determining when a firm is ready to graduate from the program.

Most regional and district officials consider SBA's criteria to be both vague and subjective. For example, the San Francisco Assistant Regional Administrator said that the SBA criteria concerning the viability of 8(a) firms is so subjective that applying it to actual situations is difficult. He would define viability as enabling the disadvantaged business owner to operate his or her business and produce the same equity that his or her peers would produce in a similar small business environment.

The San Francisco Assistant District Director agreed that there was a lack of clear rules for graduating or terminating firms from the program. She pointed out that not only does the program lack precise criteria relating to program graduation, but it also lacks rules for terminating firms that make no attempt to increase their commercial business.

The Philadelphia Assistant District Director agreed that the present criteria is useless. He told us that the criteria is so loose that a reason can always be found to retain a firm. This could encourage firms to avoid developing a commercial market to stay in the program.

SBA's Inspector General capsuled the problem of subjective program graduation criteria in the eligibility report issued in September 1979:

> "The use of subjective graduation criteria, such as they are, is understandable. No definition of "viability" is specific enough to describe precisely what ingredients are necessary to make a firm competitive, nor sufficiently comprehensive to fit the situation of all firms in all industries under all market conditions. By making the criteria subjective and elusive, the problem of precisely defining "viability" is avoided, but the problem of evaluating a firm's status fairly and objectively remains. The Agency has evaded the issue by simply postponing a decision in the graduation of 8(a) firms. SBA consequently graduates few firms, thus diminishing the possibilities of new firms entering the program."

Another problem noted was that firms commonly submitted financial data that was incomplete because it did not break out 8(a) and non-8(a) sales separately. For example, a general construction contractor in the Philadelphia district received 8(a) contracts totaling $31.5 million and has been in the program for 8 years. The firm did not submit yearly financial statements for 2 years and failed to break out 8(a) and non-8(a) sales separately on the financial statements submitted for the other 6 years. In Atlanta, a construction firm has been in the program since 1976. The firm received $809,000 of 8(a) contracts and has submitted financial statements for the past 4 years. However, the statements did not break out 8(a) and non-8(a) sales separately; thus, we were unable to determine the firm's success in developing a non-8(a) sales market.

Like financial data, business plans are often lacking considerable information and are not always updated. The Assistant Regional Administrator in Philadelphia told us that the business plan has become a paperwork nightmare. However, he believes that business plan data is essential for SBA to properly assess firms. He said that BDSs have been unable to update business plans because special projects take up their time. A Philadelphia district BDS told us that he does not concern himself with whether firms may be getting more 8(a) contract support than was projected in the business plan. He added that each firm's capacity somewhat assures a built-in control against the firm receiving unlimited 8(a) contracts.

The SBA headquarters Chief of the Requirements Division told us that revising business plan projections upward is a common occurrence. It usually results because buying agencies offer larger contracts than the 8(a) firm had anticipated when projections were prepared.

The following is an example describing the problems with preparing and maintaining business plans.

--A manufacturing firm in the Philadelphia district has been in the program more than 10 years. The business plan projections have consistently requested increasing levels of 8(a) support rather than the opposite. For example, in fiscal year 1973 the firm requested $600,000 of 8(a) support, which represented 32 percent of projected total sales. The latest approved projection requested 8(a) support of $7.8 million for fiscal year 1978. This represented 72 percent of projected total sales. In February 1980 the firm submitted a revised business plan projection requesting $55 million in fiscal year 1981, which represented 92 percent of total sales. The district office did not approve the latest revision. Despite the wide variations in requested support, the firm actually received contracts totaling $3.2 million through September 30, 1980.

Criticism, much of it justified, about SBA's ineffective administration and the meager results of the program has come from many sources. The problems that plague the program have been known for years and yet corrective action has not been taken. Without such action, the expanded business development of 8(a) firms envisioned in Public Law 95-507 will be hard to achieve.

Difficult decisions are needed on the future direction of the 8(a) program. The merits of a properly administered and structured program to help disadvantaged businesses gain a toe-hold in the competitive marketplace cannot be emphasized enough. However, such a program should be structured so that the opportunity to participate is distributed more equitably over a larger universe of disadvantaged firms. Further, the program's credibility must be accepted by both the disadvantaged and nondisadvantaged small business communities. This acceptance will occur if SBA can demonstrate that program participants will not remain indefinitely.

The recent passage of Public Law 96-481 was a step in the right direction. However, so long as the criteria for graduation remains vague, SBA will be faced with the problem of constantly negotiating new graduation dates for the majority of 8(a) firms. Too many factors, mainly subjective, hinder SBA's ability to assess a firm's competitiveness. Further, the benefits of staying in the program could encourage firms to avoid the commercial market and thus extend program dependency.

SBA has contracted out to develop more objective graduation criteria. However, we doubt whether such criteria will increase graduation rates because of the many problems discussed in this report. We believe SBA, Federal buying agencies, and 8(a) firms have no incentive to change the status quo.

In our opinion, redirection of the program is needed to improve the Government's overall effectiveness in helping disadvantaged businesses become competitive. Several alternatives are being proposed. We think a two-tier program combining 8(a) participation with a disadvantaged small business set-aside program or a separate disadvantaged small business set-aside program appear to have some potential for improving the program's overall effectiveness. However, there may be other ways to change the program. In addition, operating a disadvantaged small business set-aside program has not been tested.

MATTERS FOR CONSIDERATION BY THE SENATE SELECT AND HOUSE COMMITTEES ON SMALL BUSINESS

If the committees decide that the program should be changed, several alternatives are available, depending on whether business development or contract placement is to receive emphasis as the

Establish a two-tier program

This alternative assumes that contract placement becomes a short-range goal and business development becomes a long-range goal. Under this alternative, a two-tier program would be established that would include a disadvantaged small business set-aside program as an adjunct to the 8(a) program.

In the first tier, disadvantaged firms would enter the 8(a) program with specific limitations imposed. These limitations could be based on time periods or specified dollar amounts of 8(a) contract support. The agreed-upon limitation could be standard or different for all firms, depending on the type of industry, product, or service, or agreed upon on a firm-by-firm basis when firms enter the program.

Once a firm reaches the limit, it completes the 8(a) program and moves to the second-tier. The firm would then compete with other eligible businesses under a disadvantaged small business set-aside program. The program could operate similar to but apart from the Small Business Set-Aside Program, wherein Federal buying agencies would identify items or services within the capabilities of disadvantaged firms. Potential procurements could consist of partial set-asides for items or services historically provided by big business and total set-asides for items or services provided by the general small-business community. In cases where only one company responds to a disadvantaged set-aside solicitation, negotiation on a sole-source basis could be pursued. Solicitations could be announced, for instance, in minority trade publications and the "Commerce Business Daily" to alert the disadvantaged small business community of upcoming contracting opportunities.

SBA would be responsible for certifying the eligibility of disadvantaged businesses to participate in the set-aside program. SBA would also provide marketing, technical, and management aid to those firms that request such services. Lastly, SBA would determine when disadvantaged small businesses are ready to move from the limited competition of the set-aside program to full competition in the economic mainstream.

This alternative allows 8(a) firms to make a transition on a phased basis into the competitive market while providing the opportunity for other disadvantaged firms to participate.

Replace the 8(a) program

This alternative assumes that the problems in the 8(a) program are so serious that the present program should be replaced. A disadvantaged small business set-aside program would become the major vehicle for awarding contracts and would operate as described under the third alternative.

SBA also did not believe that our last three alternatives for restructuring the 8(a) program were appropriate. It stated that alternative number two would deny disadvantaged firms entry to the program and cause the arbitrary selection of participants for program removal. Alternative number three was considered impractical because more staff would be needed to manage a more complicated program. Lastly, SBA expressed concern about whether Federal buying agencies had the willingness to carry out and assure the success of alternative number four.

We do not agree with SBA regarding alternative number two. As noted on page 11 of this report, our analysis identified 75 firms whose continued participation appears questionable. Also, many of the 77 firms that we categorized as unclassifiable could be terminated for not complying with reporting requirements. Thus, about 57 percent of the 267 firms analyzed are potential candidates for program removal. A smaller number of firms at any one time could enable BDSs to develop and graduate successful firms. The turnover of firms would then allow new entries an opportunity to participate in the program. A scaled down program is needed if the business development thrust of Public Law 95-507 is to be achieved.

We continue to believe that alternative number three offers the potential to improve the Government's overall effectiveness in meeting the needs of disadvantaged firms. The two-tier program envisioned by us should not be any more sophisticated than the present 8(a) program. The first-tier program could be a contract placement program of smaller size than the current 8(a) program, requiring less SBA staff investment. The mechanism for the second-tier program is already in place if features of the current Small Business Set-aside Program are followed. Procurement officers located at Federal buying agencies could be charged with carrying out a disadvantaged small business set-aside program. This program could consist of a portion of the current 8(a) program contract volume as well as direct prime contracting with disadvantaged firms.

Although an initial SBA staff investment would be required to establish an approved list of disadvantaged firms eligible to participate in the second-tier program, limited staff should be needed to control additions and deletions during subsequent years. Finally, the monitoring effort to identify graduation candidates for full-scale competition might be limited to those firms that demonstrate success performing in the second-tier disadvantaged small business set-aside program.

We do not share SBA's concerns about alternative number four. The recent substantial increase in yearly Government contracting with disadvantaged firms demonstrates that Federal buying agencies are agressively carrying out the President's mandate. In our opinion, an independent disadvantaged small business set-aside program could work if the administration continues its commitment

CHAPTER 3

8(a) FIRMS HAVE BENEFITED

BUT OTHER SMALL BUSINESSES ARE CONCERNED

ABOUT THE PROGRAM'S IMPACT

Despite its problems, the 8(a) program can take credit for some benefits. Many firms were established by disadvantaged persons so they could enter the 8(a) program, and some of these firms' business operations continue to rely on the program. About 43 percent of the firms we analyzed in four SBA districts were classified as still in need of 8(a) contracts.

Other program benefits, not easily measurable, have also resulted. Officials of many 8(a) firms provided us with information on the merits of the program. They commented that the program has increased sales or income, allowed employment expansion, and provided valuable experience and exposure to managing a business. Lastly, several 8(a) owners believed that being certified as 8(a) helped them penetrate the commercial market.

On the other hand, some nondisadvantaged small business owners believe they have suffered from the effects of the program. SBA, driven by its goal to award an increasing volume of 8(a) contracts, does not always follow its policy to assess and document the potential impact of taking contracts away from the nondisadvantaged small business community.

Nondisadvantaged small business owners told us of instances where the 8(a) program contributed to reduced or lost opportunities for Government work. Other small business owners raised questions about the size of 8(a) firms, the length of time the firms remain in the program, the 8(a) firms' technical abilities, SBA's administration of the program, and the higher prices paid by the Government to contract with 8(a) firms.

The 8(a) program does not yet appear to have caused widespread injury to significant numbers of small businesses, but they could be adversely impacted in the future. The Government's commitment to the disadvantaged small business community is an increasing share of Federal contracts. If small businesses rather than big businesses continue to bear a disproportionate share of supporting the 8(a) program, then problems are inevitable. A number of small businessmen told us that the growing commitment to disadvantaged businesses is threatening their ability to survive.

was based on past work experience, solid trade supplies, and bank credit references. Prior to the illness of the firm's owner, the firm received $475,000 in 8(a) contracts, which represented 63 percent of 8(a) support projected in the firm's business plan. Since April 1980, it has received $153,000 in additional 8(a) contracts.

--A professional service firm in the Chicago district has been in the program since May 1977. The firm's total sales from 1977 through March 31, 1980, were $128,000, or about 22 percent of the total projected. About 58 percent of the $128,000 represented 8(a) sales. The proportion of 8(a) sales increased from 40 percent in 1977 to 75 percent in 1979 but decreased to 47 percent during the quarter ended March 31, 1980. In this latter period, non-8(a) sales were $10,500 or about $3,000 more than in the entire year of 1979. In March 1980, the District Review and Evaluation Committee recommended a 2-year extension in the program with increased 8(a) support. The Committee noted that the firm had competed for and won an SBA contract to conduct training. Contract files contained two commendations for contract performance, and the firm was believed to have strong management and growth potential. Also in March 1980, the Chicago region retained a consulting firm to help the firm to determine potential markets tailored to the firm's speciality.

Participants views of the 8(a) program

In our telephone survey, we asked officials of 8(a) firms whether they were generally satisfied or dissatisfied with their participation in the 8(a) program. More than 57 percent, or 180 of the 316 respondents, indicated satisfaction with the program. Of the participants who responded favorably, 110 commented on their experiences in the 8(a) program. Some of their comments follow.

The president of a construction firm in California:

> "Without 8(a), we would close-up shop."

The president of a nonprofessional service firm in South Carolina:

> "Company has been growing, if not for 8(a), we never could."

The president of a construction firm in Illinois:

"Through the SBA program we have been given the opportunity to perform certain jobs that I am sure we could not have received without their help. We proudly point to the fact that we are now constructing a building from the ground up and we doubt if we could have otherwise had this opportunity.

"Through these opportunities afforded us through the SBA program we have been able to; (1) increase our staff, (2) gain experience on more complicated jobs, (3) gain experience on more diversified jobs and (4) develop an experience record which should help us gain work from other customers.

"We feel that the program is extremely beneficia to the disadvantaged company and pray that the program will continue."

From a manufacturing firm in California:

"Prior to receiving the 8(a) certification in June 1978, we contemplated filing for bankrup at the advice of our CPA and attorney. However, after being certified as an 8(a) firm and consid able assistance from the SBA, we increased our gross sales approximately 80 percent. Our year to date gross sales have already surpassed our 1979 sales and should be a profitable year.

"The growth of our firm, and the fact we are still in business, can be attributed to the SBA 8(a) Program.

"We are confident that with the continuing support from the SBA and the 8(a) Program, we will become a viable company, and in all probability, will be able to compete with other small businesses."

BIG BUSINESS IS VIRTUALLY UNAFFECTED BY 8(a) PROGRAM INCREASES

Procurements from disadvantaged businesses are a ver part of total Federal purchasing. Total Federal procurem fiscal year 1980 amounted to $91.1 billion, while contrac to disadvantaged-owned firms were only $3 billion, or abo percent of the total.

"Taking contracts from the small business community when such contracts represent a traditionally significant part of the Federal purchase dollar to small business, is not the intent of the 8(a) program. Instead, we firmly believe that a conscious and deliberate effort by the Government to decrease the share of the Federal procurement budget spent with large business concerns, is the fundamental prerequisite for both increasing awards to small business and for securing an increase in the number and quality of contracts selected for the 8(a) program. It is the committee's further belief that SBA should attempt to obtain, insofar as practical, a selection of contract requirements which will result in a broad geographic dispersal of work so that the program will have a more representative base for proper evaluation.

"The SBA is strongly urged to conduct its programs guided by these principles and not to engage in practices which merely result in shifting contracts between the small and small minority business community, while large business continues to maintain its disproportionate share of the Federal procurement dollar."

SBA's POLICY ON ADVERSE IMPACT NOT FULLY IMPLEMENTED

The policy

As far back as 1973, SBA has had a policy that the 8(a) program should not cause injury to other nondisadvantaged small businesses. Although not specifically required by Public Law 95-507, SBA's proposed rules to implement the Minority Small Business and Capital Ownership Development Program stated, in part:

"It is the policy of SBA that any assistance made available pursuant to section 8(a) shall be made available after a determination has been made by SBA that no small business, having relied upon Federal purchasing of the item for a significant part of its business during the preceding year, will suffer excessive hardship because of the removal of the procurement from competition."

This policy was not incorporated in the final rules and regulations on the 8(a) program. However, it was included in SBA's SOP 80-05, which requires that an impact assessment be made before awarding any 8(a) contract. The impact statement should determine whether the proposed procurement been funded and it was awarded to an 8(a) firm. A nondisadvantaged firm has taken legal action and the case is in litigation.

Another problem is that SBA has not defined what constitutes a significant impact; various SBA offices interprete it differently. For example, a BDS in Philadelphia believes a significant impact occurs if a proposed 8(a) contract represents more than 20 percent of another firm's prior year sales. In San Francisco, officials said that a significant impact may range from 20 to 50 percent of the firm's sales, varying with the size of the firm. Basically, judging the severity of the impact is left to the discretion of the BDS, and little guidance exists to aid in this determination.

A BDS in Atlanta told us that whenever a procurement requirement is reserved for an 8(a) firm, a small nondisadvantaged firm suffers some impact, but no guidance exists to define if the impact is major. The Atlanta BDS stated that region IV officials believe accepting contracts representing 10 percent or less of a small, nondisadvantaged firm's business volume will not adversely impact the firm, but accepting contracts representing 30 percent or more of the firm's business volume will have an adverse impact. However, the BDS must make judgment decisions when the contract represents between 10 and 30 percent of the nondisadvantaged firm's business.

In the Chicago district, informal criteria for measuring impact is applied. If a proposed contract represents less than 10 percent of the annual sales of the small, nondisadvantaged business, it is accepted. Further study is undertaken when the contract represents between 11 and 15 percent of annual sales. A contract is not accepted by the district when it represents over 15 percent of annual sales.

A third problem is inadequate documentation, which could lead to mistaken impact assessments. Some BDSs rely on information provided by the procuring agency when completing the impact statement. We noted cases where information was inaccurate but BDSs made no effort to verify it through followup with the agency or by contacting the affected nondisadvantaged firm.

For example, the SOP forbids selecting a requirement for an 8(a) contract if it has been previously offered by public solicitation under a small business set-aside. However, we found one case where bids were issued and opened and a nondisadvantaged firm was the low bidder on the item. An official of the firm told us that the requirement was withdrawn and given to an 8(a) firm several weeks after the bids were opened. The BDS who completed the impact statement said that she relies on what the agency tells her and they told her that the requirement had not been previously bid.

of specific contracts to the 8(a) program had hurt their businesses. At least 10 other small firms believed the 8(a) program had reduced the number of Federal contracts available for competition, but they could not describe the impact in terms of sales or employment.

We contacted the 12 firms who mentioned specific contracts and found that in 9 cases the firms had been injured but were able to recover in the private sector market. However, SBA never contacted 10 of the firms to discuss the effect of reserving contracts for the program.

Each of the businesses we contacted supported the idea of the 8(a) program but feared for their own survival if they continue to lose contracts to the program. Officials of associations representing manufacturing, construction, and service firms expressed similar views.

Results of notice in
"Commerce Business Daily"

In response to the notice published in the "Commerce Business Daily", we received 84 letters from nondisadvantaged firms; 72 of these respondents believed that the 8(a) program had affected their businesses, either directly or indirectly. These firms overwhelmingly believed the 8(a) program caused reduced sales and lower employment and denied them an opportunity to bid on Government contracts. Other less frequently mentioned concerns were that

--some 8(a) firms have exceeded the size standard and are no longer small businesses,

--some 8(a) firms have stayed in the program too long,

--some 8(a) firms get higher prices than if the items had been competitively bid, and

--some 8(a) firms are not technically qualified and have to subcontract the work to non-8(a) firms.

Several nondisadvantaged firms also complained about the Federal agencies taking part in the 8(a) program. They questioned SBA's administration of the program and Federal buying agencies' preference for the easier method of contracting sole-source with 8(a) firms, rather than competitively.

A sample of the comments from nondisadvantaged firms follow.

--A management consulting firm in the Washington, D.C., area employs 17 people and averages $800,000 in annual sales. Historically, the Government market accounted for about 60 percent of its yearly sales. The firm's president said

However, SBA must do a better job of identifying potential contracts traditionally performed by big businesses that are within the capability of 8(a) firms. Historically, small rather than big business has borne a disproportionate share of the burden of supporting the 8(a) program. As the Government increases its emphasis on distributing a share of Federal procurements to disadvantaged small businesses, SBA must prevent widespread injury to the nondisadvantaged small business community.

SBA, preoccupied with its 8(a) contract goals, has neglected its policy of assessing the potential impact of reserving requirements for 8(a) firms that were previously provided by other small businesses. Also, SBA district offices are using different criteria to assess impact, making it difficult to measure the program's effect on other small firms. Because impact assessments are afforded low priority by SBA, affected small businesses are sometimes not contacted and the files lack documentation to support impact decisions.

To fulfill its role as the advocate of small business, SBA must protect the interests of both disadvantaged and nondisadvantaged firms.

RECOMMENDATIONS TO THE SBA ADMINISTRATOR

We recommend that the SBA Administrator:

--Provide standardized criteria for determining adverse impact so that SBA regions and districts make proper determinations.

--Revise the SOP to require that sufficient documentation supporting the impact determinations be included in the file. At a minimum, records of contacts with the Federal procuring agency and the small business affected, as well as financial and sales information used in reaching an impact decision, should be documented.

--Require SBA program personnel to fully implement the adverse impact policy aimed at protecting the rights of small businesses. The policy should be formally incorporated into SBA regulations as an indication of SBA's resolve to protect small businesses.

--Direct SBA personnel, in cooperation with Federal procuring agencies, to identify items that 8(a) firms can provide that have been traditionally furnished by big business.

CHAPTER 4

SCOPE AND METHODOLOGY

OF THE REVIEW

Detailed work on this review was conducted at the SBA Atlanta, Chicago, Philadelphia, and San Francisco region and district offices. Work was also performed at the SBA central office in Washington, D.C.

We interviewed SBA officials responsible for the Minority Small Business and Capital Ownership Development Program. These included the Associate Administrator and his assistants in the central office, Assistant Regional Administrators, District and Deputy District Directors, and various regional and district BDSs.

We reviewed SBA's policies, regulations, and procedures dealing with the 8(a) program. We also reviewed the reports issued by different organizations that have studied the 8(a) program over the past 6 years (see app. I).

The four district offices managed 267, or about 14 percent, of the 1,937 8(a) firms in the program nationwide, as of our cutoff date of March 31, 1980. The mix of 8(a) firms in the four districts reviewed was quite similar to the business mix of firms in the program nationwide, as depicted in the chart on page 56.

Preliminary meetings were held with the Associate Administrator of the Business Development Division and several of his assistants to consider our selection of district offices for detailed review. These officials agreed that the results of our evaluation at these four district offices should be representative of the other 54 districts with firms participating in the program. In essence, the officials conceded that the conditions found in the four district offices would exist, to a lesser or greater degree, at the other SBA district offices.

We analyzed the business development files of 195 firms in the four districts that were accepted into the 8(a) program before April 1, 1978. The 72 firms accepted susequently were not reviewed. We decided that less than 2 years was not long enough to demonstrate progress towards developing a commercial market without 8(a) contract support.

The analysis of the 195 firms included reviewing business plans, sales projections, financial statements, management assistance reports, and miscellaneous correspondence. We visited a few 8(a) firms to confirm assessments made at the district level.

The data yielded by the analysis was used to classify the firms as appropriate or inappropriate for continued participation in the 8(a) program. We had to patch together the information for a number of firms because records were poorly maintained. The missing data was so significant in certain instances that the records could not be audited and these firms were categorized as unclassifiable.

A universe of 418 active 8(a) firms was surveyed using a telephone questionnaire. The universe consisted of all active firms in SBA's Atlanta, Chicago, Philadelphia, and San Francisco district offices. Another 173 firms were randomly selected from the remaining nationwide portfolio.

Usable responses were obtained from 316 of the 418 firms surveyed. (See app. II.) The remaining 102 firms were not interviewed primarily because (1) phones were disconnected or businesses were no longer at that phone location, (2) firms were contacted but refused to be interviewed, or (3) firms had gone out of business. Probably, some firms not contacted would have called SBA's assistance inadequate, since business operations had ceased.

The survey results provided some insight into the experiences of 8(a) participants and their satisfaction with SBA's services and identified the kinds of SBA support that 8(a) firms want. In parts of the report, we merely state the absolute results of our sample in raw numbers and percentages, which provide a reasonable but not statistical estimate of the nationwide portfolio of 8(a) firms.

We published a notice in the "Commerce Business Daily" to solicit input from other 8(a) firms and nondisadvantaged small businesses. (See app. III.) The notice was intended to reach the small business community to identify 8(a) program benefits and possible adverse effects. We received 224 responses. We did not try to verify the validity of the comments in these responses.

SBA provided us with a magnetic tape listing the total contract and participant history of the 8(a) program from 1968 through September 1980. Using the SBA tape, our technical assistance group ran a series of computer programs that yielded various statistics on program activity by business class of 8(a) firms, active and nonactive firms, year of program admission, and location of 8(a) firms by region. In addition, statistics were developed identifying 8(a) firms that received substantial contract support and 8(a) firms that received minimal contract support.

The reliability of the computer data was not tested because many of the contract files had been retired and time did not permit retrieving these files. However, we used other means to

PRIOR REPORTS AND STUDIES

OF THE 8(a) PROGRAM

The following are summaries or excerpts from reports and studies of the 8(a) program highlighting various problems, including the contradicting goals and lack of staff to effectively administer the program. 1/

1. GAO report entitled "Questionable Effectiveness of the 8(a) Procurement Program" 2/ (GGD-75-57, Apr. 16, 1975)

--Sponsors exercising too much control over 8(a) firms.

--Questionable eligibility criteria for 8(a) program admission.

--Measuring 8(a) success based on contracts awarded not a valid measure.

--Management assistance not provided to 8(a) firms.

We recommended that SBA establish realistic 8(a) goals to include the number of successful program completions, reconsider maintaining 1,500 active firms in the 8(a) program, and evaluate each firm's need for management assistance and provide such assistance.

2. Interagency Report and Recommendations on the Section 8(a) Program. (January 1978) 8(a) Review Board composed of representatives from SBA; the Departments of Defense, Commerce, Transportation, and Energy; Office of Management and Budget; National Aeronautics and Space Administration; and General Services Administration.

The report's principle conclusion was that:

> "The business development goal of the 8(a) program has not been adequately supported by the necessary personnel resources and agency commitment that would allow reasonable expectations of program success."

1/See chapter 1 for additional information on these evaluations.

2/We issued two other reports related to the 8(a) program: a February 1978 report entitled "Ways to Increase the Number, Type, and Timeliness of 8(a) Procurement Contracts" (CED-78-48, Feb. 1, 1978) and a March 1978 report entitled "An Analysis of How Eligibility Criteria are Applied for Participation in the 8(a) Program" (CED-78-92, Mar. 31, 1978).

large number of variables made it impractical to develop objective criteria. Further, the Inspector General noted that the problem of negative motivation prevalent in the 8(a) program would still remain, even assuming objective criteria was developed. He concluded that SBA does not and will not have the resources for developing the capability to adequately monitor business development.

The Inspector General recommended that SBA develop procedures for measuring the full extent of contract assistance a firm can expect from the 8(a) program to determine objectively when the firm should be graduated from the program. SBA did not concur with this recommendation.

5. The 8(a) Program: Management Issues and Recommendations (August 1980). A paper prepared by an SBA headquarters official in the Office of Policy Analysis and Review.

The paper discusses the impediments to a successful 8(a) program and possible alternatives available. The paper details the

--confused results of the 8(a) program caused by measuring performance based on contracts awarded each year,

--strong disincentives that discourage 8(a) firms from leaving the program, and

--lack of SBA staff as a factor causing other disadvantaged firms to be denied entry into the 8(a) program.

The paper proposes several legislative initiatives that include: (1) limiting the period of time or dollar amount of assistance to each 8(a) firm, (2) proposing that contracts be bid competitively between 8(a) firms and included in small business set-asides, and (3) proposing that SBA not serve as the prime contractor but as a link between 8(a) firms and Federal procuring agencies for eligibility checks, negotiation, and marketing assistance.

6. Hearings Held by Senate and House committees

The 8(a) program's problems have been the subject of numerous hearings held by the Senate Select Committee on Small Business, the House Budget Committee, and the Subcommittee on General Oversight and Minority Enterprise, House Small Business Committee. In September 1980 the Subcommittee on Limitations of Contractual and Delegated Authority, Senate Committee on the Judiciary, held a hearing on abuses connected with the 8(a) program. Essentially, SBA's Inspector General testified that many of the problems identified in the September 1979 report on the eligibility review of 1,505 firms remain uncorrected.

SELECTED RESPONSES BY OFFICIALS OF 8(a) FIRMS TO

GAO QUESTIONNAIRE ABOUT SBA's 8(a) ADMINISTRATION

The following are selected questions and the answers furnished by officials of the 316 responding firms.

1. Are you aware of Public Law 95-507, which was passed in October 1978 and gave new emphasis to the 8(a) program?

	Number	Percent
1. Yes	241	76
2. No	74	24
3. Did not answer	1	0

2. Have you ever received any 8(a) contracts?

	Number	Percent
1. Yes	291	92
2. No	25	8

3. Would you say you received most of your 8(a) contracts through self-marketing or through SBA?

	Number	Percent
1. Self-marketing	120	41
2. SBA	110	38
3. Both equally	62	21

4. Have you been satisfied with the contract support provided?

	Number	Percent
1. Satisfied	116	40
2. Neutral	11	4
3. Dissatisfied	164	56

8. Would you say you have been generally satisfied or dissatisfied with your firm's participation in the 8(a) program?

	Number	Percent
1. Satisfied	180	57
2. Neutral	34	11
3. Dissatisfied	101	32

Note: Numbers do not always account for 316 responses because 8(a) officials did not answer all questions, or answered questions not applicable.

injured your business in terms of sales volume and/or level of employment, please contact GAO with specific information that demonstrates the extent of the program's impact."

We viewed the notice as a medium to reach both segments of the small business community likely to be affected by the 8(a) program. We believed the notice offered:

--A chance for us to augment the information obtained through our telephone survey of 8(a) participants. It provided a forum for other 8(a) firms not contacted in our survey to comment on the program.

--An opportunity to reach the nondisadvantaged small business community to determine if, in fact, the impact of the 8(a) program is isolated or widespread.

As intended, the notice drew responses from both segments of small business. The following is a breakdown of the 224 replies received based on respondent type:

--Eighty-one letters were from officials of 8(a) firms and 76 of these believe the 8(a) program had been beneficial. (These letters are discussed in ch. 3.)

--Eighty-four letters were from officials of non-8(a) small firms and 72 of these provided specific or general concerns about the 8(a) program's impact on their business. (These letters are discussed in ch. 3.)

--Thirty-two letters were from firms claiming disadvantaged status and seeking 8(a) certification. (These letters are discussed in ch. 2.)

--Twenty-two letters were received that were not specifically related to the 8(a) program.

--Five letters were received from minority associations endorsing the merits of the 8(a) program.

Note: A number of responses required followup by us either because the respondent requested a reply or because we wanted to obtain additional data or specifics concerning the letters' content. However, in no case, did we verify the data.

SMALL BUSINESS ADMINISTRATION
COMMENTS TO GAO DRAFT REPORT ENTITLED
"SBA'S 8(a) PROCUREMENT PROGRAM--A
PROMISE UNFULFILLED"

GENERAL STATEMENT:

While it is clear from a program point of view that the proposed report contains statements which tend to distort the reader's understanding of what the 8(a) Program is, and what the real areas of difficulty are, it is the intent of these comments to offer constructive responses in anticipation that they may be included by GAO in the final report.

We would also like to point out that there has been definite progress demonstrated in the 8(a) Program since the enactment of Public Law 95-507, which the report does not mention, such as:

1. Centralized authority has provided more consistent review and decision making in the eligibility process as well as in the program completion and termination processes.

2. The quality of the portfolio has increased significantly. Firms are now stronger financially and managerially. Problems concerning ownership and control have also been reduced significantly.

3. Approximately 100 firms have been recommended for program completion during the past year.

4. An automated data system which will streamline our information retrieval capability is being developed. This ADP system will enhance significantly program management capability.

GOAL SETTING:

Goal setting as required by P.L. 95-507 does not compete with business development or the development of viable businesses. Company business plans establish annual dollar requirements of procurement support compatible with the resources of each company. The sum total of all company business plans should be the annual 8(a) Program goal to be negotiated with each of the Federal agencies. Once the negotiated goal has been finalized, it gives the SBA and Federal agencies an objective for attainment and support. Without this type of objective, it is doubtful that sufficient incentive and attention would be given to the 8(a) Program.

ALTERNATIVE RECOMMENDATIONS

The number 3 alternative recommended by GAO is impractical without additional personnel and other financial resources. It has been continuously reported that there are insufficient resources to perfect management of the 8(a) Program as presently constituted. To

3. Submission of Financial Data from 8(a) Firms

Without ADP capability for analyzing this data, existing manpower resources would be strained beyond capacity. It would, therefore, be extremely helpful if GAO would assist SBA in articulating the urgent need for adequate manpower resources and ADP equipment which would provide field as well as Central Office staff with the capability to increase the efficiency and effectiveness of 8(a) Program administration.

4. Impact Studies

SBA and specifically the program managers of the 8(a) Program are certainly concerned that accurate impact assessments are performed. However, it must be clearly understood that there is a significant difference between the allegation of negative impact and the fact.

While we cannot claim a perfect or error-free record where impact assessments are concerned, our record, nevertheless, is a good one. More standardization in the performance of impact studies is viewed as a constructive recommendation and should lead to consistency. On the other hand, it must be realized that negative impact allegations are one way of thwarting the capability of the program to assist 8(a) firms and the extent to which these allegations have no merit, 8(a) firms themselves experience negative impact.

CONCLUSION:

We conclude by pointing out that much of the content of the proposed report can be helpful in improving the performance of the 8(a) Program. However, an adequate description of the need for, and the environment in, which the program operates is missing. Without this basis from which performance evaluation can be measured, the report in our opinion lacks the necessary cohesion and structure for developing logical conclusions or inferences.

For example, the report states that since inception, 50 firms have received 30% or $1.3 billion of contract assistance. The implication is that something is wrong with that fact. However, no analysis accompanies that statement which demonstrates that something is wrong. When simple breakdown of the $1.3 billion to 50 firms over 13 years is performed, each firm received an average of $2,000,000 in contract support each year. The net value of each firm, assuming a 10 percent profit before taxes, and a 5% profit after taxes approximates $100,000 per year on the average. The 50 firms would have received a total benefit of $65,000,000 (5,000,000 x 13 years) and the Federal government received $1,235,000,000 in goods and/or services and federal income taxes.

Request for copies of GAO reports should be sent to:

U.S. General Accounting Office
Document Handling and Information
Services Facility
P.O. Box 6015
Gaithersburg, Md. 20760

Telephone (202) 275-6241

The first five copies of individual reports are free of charge. Additional copies of bound audit reports are $3.25 each. Additional copies of unbound report (i.e., letter reports) and most other publications are $1.00 each. There will be a 25% discount on all orders for 100 or more copies mailed to a single address. Sales orders must be prepaid on a cash, check, or money order basis. Check should be made out to the "Superintendent of Documents".

This too, is not a complete or rigorous analysis, but it does present a clearer picture from which the reader of the proposed report could draw some conclusions.

In addition, we have administratively corrected many of the expressed concerns during and subsequent to the GAO review. The changes have not come as fast as we would have liked.

We strongly feel that we have made the proper adjustments to the 8(a) business development program, corrected what needed to be done and that we are now headed in the proper direction.

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structure a more complicated, sophisticated program such as the two tier approach would require additional resources which everyone knows will not be made available.

Alternative 2 compounds the problem of denying a number of socially and economically disadvantaged firms an opportunity for program participation by placing a moratorium on new entries into the program or the arbitrary selection of program participants for removal from the program.

The success of alternative 4 is dependent upon the willingness of procuring agencies to reserve procurement opportunities for ultimate award to socially and economically disadvantaged concerns. We do not believe that the individual agencies of the federal structure presently have the empathy and willingness to manage such a program successfully.

In our opinion, alternative 1 is the most appropriate as a continuing process of improvement has been underway with limited resources since the enactment of P.L. 95-507. With the availability of additional resources, we are convinced that much of the criticism can be overcome.

RECOMMENDATIONS:

On the whole, the recommendations to the Administrator on p. 58 and p. 79 are constructive. They also address problems that are not new to us since we have been addressing many of these problems for quite some time. There are some for which we do feel elaboration is required. They are:

1. "Take Action to Fill BDS Vacancies"

We have been making every attempt possible to improve resources through BDS staffing but it must be remembered that a Federal hiring freeze has been in effect most of the period of time since P.L. 95-507 was enacted. In addition, much of the unfavorable publicity, most of it unfounded, which the program has received since 1977, has made many people less willing to work in a program where constant criticism by GAO, the Press, and others creates an environment in which one's efforts cannot receive favorable consideration no matter how noteworthy they may be.

2. Financial Training for BDS's

Many BDS's now have financial analysis capability. However, the inadequate staffing in most field offices is probably the primary cause for analysis problems, not an extreme lack of BDS's with financial analysis capability.

U.S. GOVERNMENT
SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

FEB 23 1981

Mr. Henry Eschwege
Director
Community and Economic Development
Division
United States General Accounting Office
Washington, D. C. 20548

Dear Mr. Eschwege:

This is in response to your letter of January 19, 1981, addressed to the then Administrator A. Vernon Weaver requesting his comments on your draft report entitled, "SBA's 8(a) Procurement Program--A Promise Unfulfilled."

Enclosed are our comments as requested for your consideration in the preparation of the final report.

If you have any questions or need additional information, please advise.

Sincerely,

Carl Ellison

Carl Ellison
Acting Associate Administrator
for Minority Small Business
and Capital Ownership Development

Enclosure

RESPONSES TO NOTICE PUBLISHED IN

"COMMERCE BUSINESS DAILY"

The "Commerce Business Daily" is a Federal procurement publication prepared by the Department of Commerce. The "Commerce Business Daily," published every weekday, tells subscribers what the Government is buying and selling. It lists Government procurement invitations, contract awards, subcontracting leads, sales of surplus property, and foreign business opportunities.

As of September 1980, the "Commerce Business Daily" was being sent to 29,302 subscribers, as follows:

	Number of Subscribers
Companies	19,163
Individuals	6,969
Government agencies	1,260
Research centers	691
Educational organizations	542
Libraries	358
Energy and environmental organizations	319
Total	29,302

At our request, the Department of Commerce published the following notice in the "Commerce Business Daily:"

"BUSINESS NEWS

ATTENTION: 8(A) PARTICIPANTS AND NON-DISADVANTAGED SMALL BUSINESSES

As required by Public Law 95-507, the U.S. General Accounting Office (GAO) is currently reviewing SBA's procurement program to aid small and disadvantaged businesses known as the 8(a) program. This review will assess the extent to which participants have benefited from the program and the extent to which non-disadvantaged small firms have been affected by the program. To assist in this study, GAO is seeking input from the small business community. If you have participated in the 8(a) program and believe that it has improved your ability to compete in the marketplace without 8(a) assistance, please contact GAO with specific information that demonstrates how your firm has progressed. Likewise, if you are a non-disadvantaged small firm and believe that the 8(a) program has

5. Have you ever received the following assistance?

	Advance Payment		BDE		SBA Loans	
	Number	Percent	Number	Percent	Number	Percent
1. Yes	57	18	50	16	130	41
2. No	259	82	265	84	186	59

	Technical Help		Marketing Help		Management Help	
	Number	Percent	Number	Percent	Number	Percent
1. Yes	106	34	96	30	135	43
2. No	208	66	220	70	180	57

6. Were you satisfied with the assistance provided?

	Advance Payments		BDE		SBA Loans	
	Number	Percent	Number	Percent	Number	Percen
1. Satisfied	37	65	36	73	86	68
2. Neutral	4	7	1	2	12	9
3. Dissatisfied	16	28	12	25	29	23

	Technical Help		Marketing Help		Management Hel	
	Number	Percent	Number	Percent	Number	Percent
1. Satisfied	70	69	52	57	76	57
2. Neutral	7	7	15	16	14	10
3. Dissatisfied	25	24	25	27	44	33

7. If not received, do you need this assistance?

	Advance Payments		BDE		SBA Loans	
	Number	Percent	Number	Percent	Number	Percent
1. Yes	104	41	103	39	60	32
2. No	152	59	160	61	129	68

	Technical Help		Marketing Help		Management Help	
	Number	Percent	Number	Percent	Number	Percent
1. Yes	39	19	66	30	48	27
2. No	170	81	155	70	132	73

Chapter 2 of this report discusses the same types of problem described in these prior reports and studies. Essentially, the problems noted by us and others continue and corrective action ha not been taken.

The review board recognized contract placement and business development as 8(a) program goals. The board came up with 51 separate recommendations to SBA centered around the need for additional personnel and resources and significant organizational changes to introduce a true business development effort in the program.

3. GAO report entitled "Efforts to Improve Management of the SBA Have Been Unsatisfactory--More Aggressive Action Needed" (CED 79-104, Aug. 21, 1979)

The report dealt with following up on our recommendations from prior reports on SBA. We reported that management assistance delivered under the 8(a) program needs improvement. The report noted that 52 percent of firms interviewed had not received management assistance, although a number of firms had requested such assistance.

4. SBA Inspector General Report of Audit on Eligibility Review of 8(a) firms (Sept. 27, 1979) 1/

--SBA criteria regarding ownership and control are inadequate.

--Eligibility criteria for determining social and economic disadvantage status are inadequate.

--More objective procedures for 8(a) firm graduation should be established.

--Termination action needed for firms out of business, in failing financial condition, and recommended for termination.

The SBA auditors reviewed 1,505 firms and raised questions about the status of 323 firms. These firms appeared to be headed by disadvantaged individuals who did not actually control or manage the firms' day-to-day operations or whose status as socially or economically disadvantaged individuals was doubtful.

The report also raised several significant issues concerning the 8(a) program criteria for graduation, which the Inspector General called subjective and elusive. He questioned whether the

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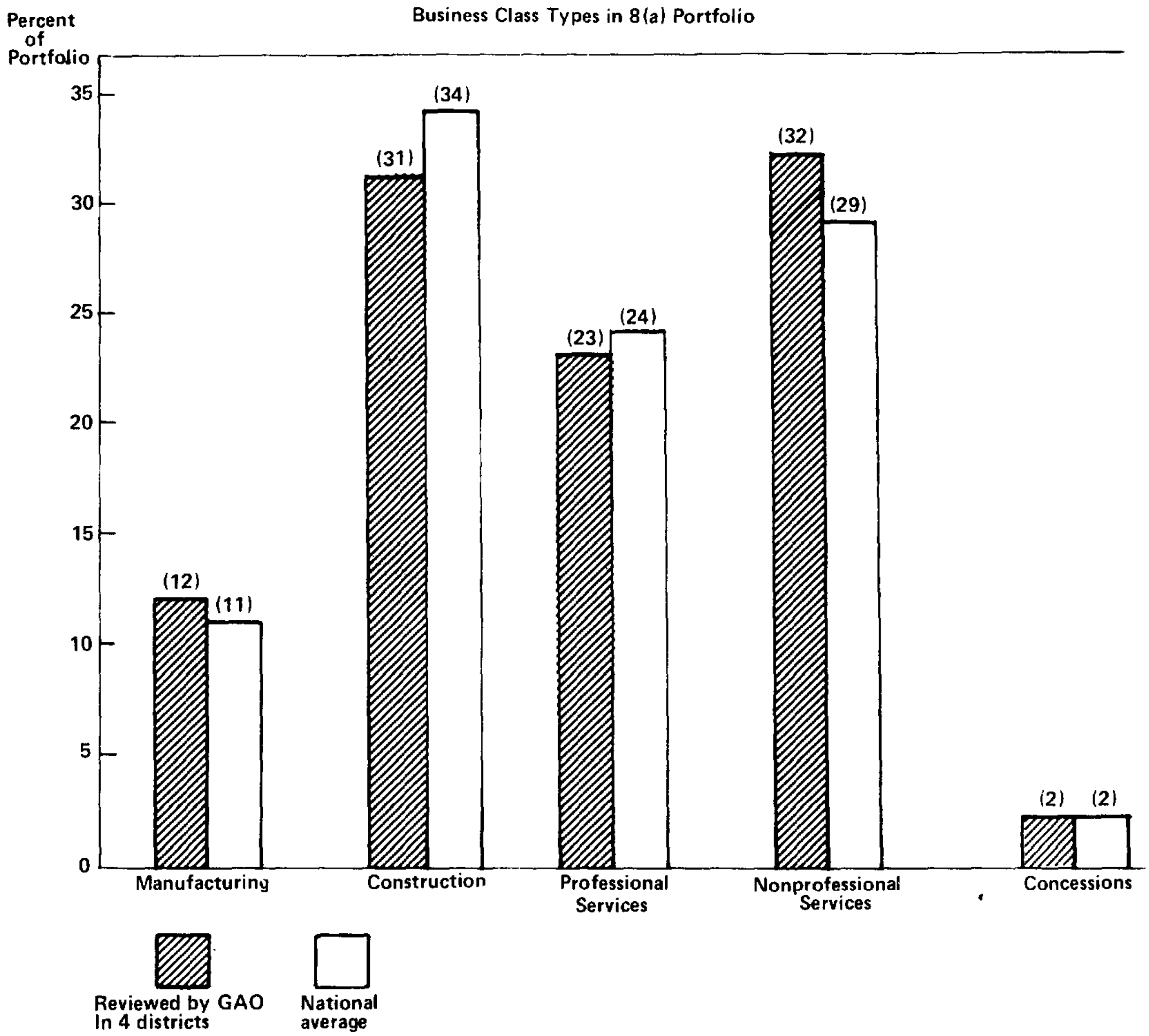
1/SBA's Inspector General also issued two other reports in 1979: a January report that identified problems in SBA's use of and control over business development expense furnished to 8(a) firms and an April report describing SBA's improper management of advance payments to 8(a) firms, resulting in misused and uncollectable advance payments.

satisfy ourselves about the adequacy of the computer data. An SBA headquarters official in the Office of Data Management told us that the computer files are fairly accurate regarding the contract data. He added that the total amount of $5.5 billion may be slightly understated. The differences, which amounted to less than 1 percent, occurred because contracts awarded near the close of fiscal year 1980 were not promptly entered in the computer system. In addition, SBA district officials who were furnished with information about 139 of the 195 firms analyzed did not question the accuracy of computer-generated statistics on the 8(a) contract volume. For these reasons, the computer-generated data has been deemed creditable for purposes of this report.


Business Class Types in 8(a) Portfolio
Percent of Portfolio
35
30
25
20
15
10
5
0
(12)
(11)
(31)
(34)
(23)
(24)
(32)
(29)
(2)
(2)
Manufacturing
Construction
Professional Services
Nonprofessional Services
Concessions
Reviewed by GAO In 4 districts
National average

SBA COMMENTS AND OUR EVALUATION

SBA agreed that more standardization in performing impact studies was a constructive recommendation that should lead to consistency. However, SBA stated that its record on impact assessments was a good one and that negative allegations are one way of thwarting the program's ability to aid 8(a) firms.

We continue to believe that an evenhanded approach to contracting with disadvantaged firms is necessary so that the concerns of nondisadvantaged firms about the program's future impact do not materialize. Therefore, compliance by SBA with its policy and procedures becomes an absolute prerequisite.

that he has lost the opportunity to bid on several contracts. As a result, he has had to lay off five employees. He said that the 8(a) program had seriously impaired his firm's ability to obtain Government contracts. In an attempt to mitigate the impact, the firm is now serving as a subcontractor to an 8(a) firm. This arrangement, according to the official, increased costs to the Government as the 8(a) contract was awarded for $70,000 while his firm could have done the job alone for $40,000. The firm's president told us that the company has been sold to a larger business because of cashflow problems created by a lack of contracting opportunities largely due to the 8(a) program. The larger firm has also been affected by the program but because of its size has been able to survive.

--A professional service firm in the Midwest was similarly affected. The firm had performed on a contract since 1978 and had expected that the contract would be renewed. However, it was informed that the contract was reserved for an 8(a) firm. According to the firm's president, the contract represented about 35 percent of the firm's average annual sales. After this significant loss in sales, 15-20 workers were laid off. The president said that he does not expect a short-term recovery from the adverse impact. Interestingly, SBA never contacted him to discuss impact and has not responded to his inquiries on the subject.

--A southern manufacturer told us that he had been hurt when a substantial contract was awarded to an 8(a) firm. However, he was able to recover by turning to other markets. He noted that this sort of sequence may cause a ripple effect. As he turns to other markets, smaller firms with less experience lose some of their business.

CONCLUSIONS

Admittedly, the 8(a) program's task to develop competitive disadvantaged firms is a difficult one. These firms fail at a rate three times higher than other small businesses.

Despite the considerable problems noted by us and others, the 8(a) program has provided some benefits. It spurred the formation of disadvantaged firms that would not have otherwise been established. Many firms continue in business because of 8(a) program support. SBA has helped some firms to increase sales and income, resolve bonding problems, and improve credit capabilities. Participants also gained valuable experience in managing a business. Several firms believed that being certified as 8(a) helped in getting commercial work as well.

In another case, a BDS accepted the procuring agency's statement that a proposed requirement was for a new item that had never been purchased before. He later learned that the item had been supplied for several years by three small firms. One of the firms claimed adverse impact. However, our followup contact with the firm did not substantiate the claim.

The format of SBA's impact statement does not provide for the necessary analysis, and the SOP gives no guidance in this are The statement is basically a checklist addressing the four conditions listed in the SOP. This statement is simply inadequate according to a Philadelphia regional official. He told us that to determine the effect on an existing contractor, one should contact the firm, or at least obtain a "Dun & Bradstreet" report for it. This data is needed if the potential 8(a) contract is to be compared with the firm's total sales. Most of the files we reviewed contained the basic impact statements but included no supporting documentation.

Only Atlanta, among the four districts visited, obtain adequate documentation on the potential impact of proposed contracts reserved for 8(a) firms. The Atlanta district requires procuring agencies to provide estimates of the contract cost and the name of the previous supplier of the item. The BDS then sends a form letter to that firm requesting financial and sales data and a listing of all its contracts along with the dollar amount of each contract. The firm must also send in data about its size.

The BDS reviews the firm's sales data for the complete fiscal year to consider the contract's potential impact. Using information provided, the BDS determines if region IV's acceptance of the contract would adversely impact the nondisadvantaged small firm.

ADVERSE IMPACT NOT YET WIDESPREAD

Despite the weakness of SBA's procedures for avoiding adverse effect on other small firms, we did not find widespread injury caused by the 8(a) program. We did find several cases where small businesses claimed to have lost contracts to the program.

We tried to obtain a universe of small businesses that deal with the Government. Our plan was to statistically sample the universe and use a telephone questionnaire to solicit comments about the 8(a) program. However, we were unable to develop a suitable universe because records maintained by Federal procurement agencies did not contain necessary identifying data.

When these efforts failed, we examined congressional and SBA records of firms complaining about the 8(a) program. This search identified 12 nondisadvantaged small firms claiming that the loss

--is excessive in relation to the total purchases of like or similar products or services procured by the Federal Government,

--has been offered previously by public solicitation under a small business set aside,

--could reasonably be expected to be awarded to a disadvantaged firm--under conventional procurement procedure, and

--will cause any other small business concern to suffer major hardship if the award is made to SBA pursuant to section 8(a).

Proposed procurements should not be considered for 8(a) contracts when SBA concludes that one or more of the above conditions exist.

<u>The problems</u>

SBA's policy on adverse impact has not been fully implemented because

--SBA staff do not give priority attention to the policy,

--criteria to determine what constitutes adverse impact have not been defined, and

--complete and sufficient data is not always obtained to verify and document the adverse impact.

The SBA chief of the Requirements Division told us that 8(a) program staff have no incentive to conduct a thorough impact study. The emphasis on the number and dollar volume of 8(a) contracts awarded causes SBA to accept contracts with little or no review of the possible adverse impact on nondisadvantaged firms. However, he said that SBA must do more to assure that its impact policy is enforced.

For example, SBA reserved 28 of 37 construction requirements offered by the Corps of Engineers for the 8(a) program during fiscal year 1980 in the Huntington, West Virginia, and Pittsburgh, Pennsylvania, areas. Nondisadvantaged firms in these areas indicated that removing this large a portion of the work would have a devastating effect. SBA officials agreed. The chief of the Office of Business Development in the Philadelphia region said that when the office reserved the projects, it was unaware that the projects represented such a large portion of the procurement in the area. Even after it realized this, it did not change its original decision because it anticipated that not all of the projects would actually be funded. In our opinion, if some projects are not authorized, the potential effect on nondisadvantaged firms could be even greater. So far, only one project has

When viewed from this perspective, it seems that minority contract set asides for disadvantaged firms could have little, if any, impact on the Federal marketplace. However, an SBA headquarters official in the office of procurement assistance told us that contracts reserved for disadvantaged firms are generally for items or services historically furnished by small business. While the commitment to contracting with disadvantaged firms is growing, the total amount of Federal contracts set aside for small business participation is expected to drop significantly during fiscal year 1981, as shown by the following table.

FY	(A) Total Federal procurement	(B) Small business awards	(C) Percent of col. A	(D) Disadvantaged business awards	(E) Percent of col. A	(F) Percent of col. B
	---(billions)---			(billions)		
1979	$91.7	$20.6	22.5	$2.5	2.7	12.1
1980	91.1	21.5	23.6	3.0	3.3	14.0
1981 (note a)	95.3	17.3	18.2	4.2	4.4	24.3

a/Goals for 1981.

The total Federal procurement goal for fiscal year 1981 is expected to be $4.2 billion higher than 1980. However, the small business goal is expected to be $4.2 billion lower. An SBA headquarters official in the Procurement Assistance Division told us that a number of important procurements for small businesses are being frozen for fiscal year 1981. For example, the General Services Administration is not buying any furniture for the Government this year. These procurements usually would have been set aside for small businesses.

Big business, which accounts for the majority of Federal procurement dollars, generally has not borne a proportionate share of giving up items or services for 8(a) contracts. If this trend continues, greater impact on the small business sector will be inevitable. The SBA headquarters Chief of the Requirements Division said that agency contracting officers have used big business on a sole-source basis for years. SBA must put more emphasis on Federal buying agencies to break out portions of large procurements from big business to lessen the impact of the 8(a) program on small firms.

The failure to get big business to absorb a share of the contracting goals for disadvantaged firms has also concerned the Congress. The September 1980 Congressional Conference report on H.R. 5612 noted the following:

"A wonderful program. Has opened many doors for firm especially in waiving of bonding requirements."

The president of a nonprofessional service firm in California:

"Went from unemployment at $75 per week to president of a firm employing 80 people including many minorities. I am chairman of our association of 8(a) contractors."

The president of a nonprofessional service firm in Illinois:

"I could not survive without the 8(a) program. Competition is tough in the janitorial business. I have provided jobs for many minorities."

Additional comments were received as a result of our notice published in the "Commerce Business Daily." Officials of 8(a) firms sent 81 letters in response to the notice. Of these, 76 respondents commented favorably about participating in the 8(a) program and cited the following benefits most frequently.

--Resulted in increased sales and income.

--Allowed the hiring and upgrading of employees.

--Provided an opportunity to learn management techniques and contracting procedures.

--Helped firms to compete in the non-8(a) market.

--Improved the firm's credit and bonding capabilities.

--Enabled the firm to stay in business.

Comments from two of these letters follow.

From a construction firm in Michigan:

"I am a participant in the SBA 8(a) program and can definitely state that the program has been extremely helpful to me. Although all of our contracts have not been profitable, the degree of profitability has been greater then it would have been on a competitive basis. My bonding company is more eager to bond SBA contracts as opposed to others since there is less risk of having a job going into default.

SOME DISADVANTAGED FIRMS HELPED BY THE 8(a) PROGRAM

The 8(a) program is faced with a difficult task--developing disadvantaged firms to the point of self-sufficiency. An SBA headquarters official in the Industry Analysis Division told us that about 50 percent of all small businesses discontinue within 2 years of beginning operations. The failure rate for disadvantaged small firms is even higher. A study of the Minority Business Development Agency's client firms and a control group of nondisadvantaged businesses indicated that client firms fail at a rate three times higher than nondisadvantaged firms. Another study commissioned by the Commerce Department reported that most disadvantaged entrepreneurs are first-generation managers who usually lack adequate capital and access to marketing possibilities.

However, the program has benefited some disadvantaged firms. Any firms that received 8(a) contracts have to some degree been helped by the program. More than 84 percent of the 2,138 active 8(a) firms received at least one contract. Our analysis at the four districts identified 115 firms that received moderate 8(a) contract support, reported some non-8(a) sales, and appeared to need more SBA aid. Also, officials of 8(a) firms who responded to our telephone survey and notice published in the "Commerce Business Daily" provided comments on positive aspects of the 8(a) program, including specific examples.

8(a) firms with moderate 8(a) contracts and non-8(a) sales

We classified 115 firms, or 43 percent of the 267 firms analyzed at the four districts, as businesses that appear to need more contract support. Seventy-two of these firms have been in the program for less than 2 years. We assumed that a period of less than 2 years did not permit enough time for an 8(a) firm to show progress or achieve a competitive status.

A number of firms that were in the program for more than 2 years also appeared in need of additional 8(a) contract support because SBA was only moderately successful in meeting the projected 8(a) contract support. Following are two examples of 8(a) firms that need more 8(a) contract support.

--A Philadelphia District general construction firm entered the 8(a) program in September 1976 because the residential housing market was in decline. From mid-1978 until March 1980, the firm's owner was seriously ill. The business was inactive during his illness. In April 1980, the firm began operations again. A management study done for SBA recommended that this firm should be supported in its return to the construction industry. The recommendation to share Government procurements with disadvantaged firms. We also believe that this alternative should result in less staff requirements since SBA would be totally removed from the procurement process.

SBA also concluded that the report lacks the necessary cohesion and structure for developing logical conclusions or inferences. It cited the 50 firms that received the bulk of the contract assistance and questioned why no analysis accompanies out statement of this fact to demonstrate that something is wrong. SBA calculated a breakdown that determines that the 50 firms received an average of $2 million in contract support each year.

We question SBA's logic. The 8(a) program is designed to aid disadvantaged small businesses. We saw no reason for further analysis when slightly more than 1 percent of the participating firms received $1.7 billion, or 31 percent, of the $5.5 billion in total contracts. Like SBA, we also made a breakdown based on the year the firm was admitted into the program rather than the standard 13-year period SBA used for all 50 firms. Our analysis showed that the 50 firms received an average of $4.6 million in contract support each year.

SBA noted that, on the whole, the recommendations to the SBA Administrator were constructive, but elaborated on several. SBA stated that BDS vacancies cannot be filled until the hiring freeze is lifted and the 8(a) program environment becomes more favorable. SBA also believed that most BDSs now possess financial analysis capability and said that automated data processing capability was needed to properly analyze submitted financial data.

Our recommendation to fill BDS vacancies was made before the Federal hiring freeze was imposed. We have revised our recommendation to recognize that SBA cannot take hiring actions until the freeze is lifted.

We continue to believe that many BDSs need financial training. As noted on pages 27 and 28 of this report, several SBA regional and district officials confirmed the need for training. While an automated data processing capability may enhance SBA's administration of the program, 8(a) firms should be directed to immediately comply with SBA's requirement for the submission of financial statements. This data is needed for BDSs to assess the status of 8(a) firms.

Disadvantaged firms would deal directly with the Federal purchasing agencies and SBA would no longer function as the prime contractor. This alternative should save administrative and personnel costs since SBA would be removed from the procurement process. It would also open up the prior sole-source 8(a) procurement market to all disadvantaged firms. SBA would continue to certify disadvantaged firms' eligibility and would provide technical, management, marketing, and negotiating aid to those firms that request such services.

RECOMMENDATIONS TO THE SBA ADMINISTRATOR

Pending any action on the part of the committees to change or continue the program, SBA needs to immediately strengthen how it manages the program. Accordingly, we recommend that the SBA Administrator:

--Take action to fill BDS vacancies so that the 8(a) program operates at full staffing strength as soon as the presidentally imposed hiring freeze is lifted.

--Provide BDSs with adequate training, especially in understanding financial statements, so that the status of 8(a) firms can be assessed.

--Direct participating 8(a) firms to submit accurate and timely business plan projections and financial statements as required by SBA's standard operating procedures.

--Assure that participating 8(a) firms submit financial statements that break out 8(a) and non-8(a) sales so that progress can be measured.

--Remove inappropriate 8(a) firms by assuring that the graduation criteria being developed is aggressively implemented and termination requirements set forth in SBA's procedures are followed.

SBA COMMENTS AND OUR EVALUATION

SBA commented that some progress has been made in improving the 8(a) program and that our first alternative has merit. (See app. IV.) SBA also agreed with us that business plan projections should be used as the basis for establishing an 8(a) contract volume goal but disagreed that the contract volume goal competed with the goal of developing self-sufficient disadvantaged businesses. We do not agree with SBA and neither do many SBA regional and district officials who believe that the contract volume goal has impeded business development of 8(a) firms.

program's primary goal. We are not proposing that Government contract support to disadvantaged firms be diminished by adopting any of these alternatives. Instead, the President's contracting goal could be redistributed depending on the alternative chosen. We suggest that the two committees could further build on the recently enacted legislation by considering the following alternatives, some of which restructure the 8(a) program:

--Continue the present 8(a) program.

--Reduce the size of the present 8(a) program.

--Establish a two-tier program.

--Replace the 8(a) program.

Continue the present 8(a) program

This alternative assumes that retaining the present 8(a) program is desirable if actions are taken to minimize its problems. We believe that contract placement would continue to be the primary goal and business development would be given a low priority by selecting this alternative.

Reduce the size of the present 8(a) program

This alternative assumes that business development rather than contract placement becomes the primary goal. Questionable firms like the ones identified in this report could be removed from the program.

The scaled-down program could include only those firms that (1) want and need the development services available from SBA, (2) provide services or products that the Government purchases, and (3) are in industries that have a commercial market available. The limited SBA staff would have more time to oversee the participating firms' developmental needs. Further, this proposal would not impose stringent contract volume goals on SBA. Rather, the contract goal could be satisfied mainly by direct contracting and subcontracting with disadvantaged firms. Accurate business plan projections of needed 8(a) contract support would be used as a basis for the yearly volume of SBA's contract placements.

A recommendation to limit the number of firms in the 8(a) portfolio was included in our 1975 report entitled "Questionable Effectiveness of the 8(a) Procurement Program" (GGD-75-57). SBA agreed with this recommendation, and the number of firms was reduced through 1977. However, the number of firms in the program has grown since then and is now at its highest level.

RECENT 8(a) LEGISLATION

Public Law 96-481, enacted October 21, 1980, amended section 8(a) of the Small Business Act. It requires SBA to negotiate graduation dates with existing 8(a) firms and new applicants accepted into the program. In effect, the new law establishes a mutually agreed upon period of time for SBA to help a firm to develop the ability to compete. The time period can be revised if conditions warrant. In addition, the new law transferred responsibility for program implementation from the Associate Administrator for Minority Small Business and Capitol Ownership Development back to the SBA Administrator.

CONCLUSIONS

The 8(a) program has fallen short of its goal to develop competitive, disadvantaged-owned businesses. Few firms have used the program as a springboard to business self-sufficiency. During its 12-year history, the program has served as a haven for a chosen few firms that receive substantial sole source contracts and have no incentive to leave the program. In addition, many firms do not need the management, marketing, and technical aid offered by SBA and are only interested in receiving 8(a) contracts.

Some firms have not built up a commercial market or claim to have no commercial market to penetrate, and self-sufficiency may never be possible for them. Such firms should be removed from the program. We question whether several firms, in the program for years that have not received 8(a) contract support, should continue in the program.

A number of disadvantaged firms have been denied access to the 8(a) program because SBA has not removed questionable firms from the program. Some disadvantaged firms were rejected since SBA only had sufficient contract support for active 8(a) firms with the same or similar capabilities as the rejected firms.

SBA's main concern has been in achieving 8(a) contract volume goals imposed by the President, which has become the driving force behind the 8(a) program and competes with and clouds the program's true purpose--developing independent disadvantaged entrepreneurs. Essentially, SBA has acted mainly as a contract broker between Federal procurement agencies and 8(a) firms.

Other problems--insufficient program staff, vague and subjective graduation criteria, and substantial missing and incomplete data--further hamper the 8(a) program's effectiveness. The limited and overworked BDSs find it difficult to even assess the status of many 8(a) firms let alone identify their management and technical assistance needs.

The Inspector General further stated that SBA would find it difficult to develop objective program graduation criteria. We agree with SBA's Inspector General that any new criteria having viability as a basis for graduation face the same pitfalls as the existing vague and subjective criteria.

Missing Financial Statements and Business Plan Data

SOP 80-05 also includes a definition of program completion, as follows:

> "An 8(a) concern's substantial achievements of the objectives of the 8(a) program, including but not limited to the achievement of the goals as set forth in its approved business plan and the attainment of demonstrated ability to compete in the marketplace without 8(a) assistance."

Each 8(a) firm is required to have an approved business plan with yearly projections of needed 8(a) contracts and non-8(a) sales. Essentially, the business plans are intended to diagram the path to business independence. Firms are also required to submit quarterly and annual financial statements in sufficient detail to measure the firm's sales performance and progress. Financial statements that depict actual 8(a) and non-8(a) sales performance are intended to help SBA measure how well firms have developed their commercial market.

However, BDSs cannot even begin to assess the progress of many 8(a) firms because significant information is missing. At three of the four districts visited, 111 of 164 files analyzed had at least 1 year of financial data missing. Eighty-six files also had at least 1 year of business plan projections missing.

We queried 119 firms in San Francisco and Philadelphia in an effort to get more accurate sales and financial information. Only 37 of the 119 firms responded and 8 of these submitted incomplete data.

One of these firms, a construction company in the Philadelphia district, entered the program in June 1971. It received 21 contracts for about $3.6 million of 8(a) support. However, during its 9 years of program participation, the firm submitted only one financial statement covering a 6-month period. The firm did not answer our request for financial data.

In the San Francisco district, one firm received nine contracts totaling $699,793 of 8(a) support. It has been in the program for 8 years but has not submitted financial data for the past 3 years. The statements submitted only accounted for $381,173 of the $699,793 of 8(a) contracts. The firm did not respond to our request for the missing data.

Type of Assistance	Number of Responses	Percent
Getting contracts	235	74.4
Financial aid	19	6.0
Management aid	11	3.5
Marketing aid	6	1.9
Technical aid	3	0.9
Other	36	11.4
Cannot say	6	1.9
Total	316	100.0

In addition, more than half of the 316 respondents did not need management, technical, or marketing aid or were dissatisfied with the aid rendered by SBA.

OTHER FACTORS HAMPERING THE 8(a) PROGRAM'S EFFECTIVENESS

Two other factors--inadequate program graduation criteria and missing business plan and financial statement data--also inhibit SBA's effective administration of the program. When linked to the major problem of competing goals and insufficient staff, these factors further handicap SBA's efforts to develop 8(a) firms capable of competing without 8(a) assistance.

Inadequate Graduation Criteria

SOP 80-05 includes the following description of the criteria for program completion:

> "In determining whether a concern has substantially achieved its approved business development objectives and has attained the ability to compete in the marketplace without 8(a) assistance, the following factors, among others, shall be considered:
>
> a. Positive overall financial trends of the concern including but not limited to:
>
> (1) Profitability.
>
> (2) Level of non-8(a) sales.
>
> (3) Net worth, financial ratios, working capital, capitalization, access to credit and capital.
>
> (4) Ability to obtain bonding.

firms. The following table provides a comparative analysis of BDS workload by region in terms of number of firms between 1977 and 1980.

Region	12/31/77 No. of firms	12/31/77 No. of BDSs	12/31/77 Average firms per BDS	9/30/80 (note a) No. of firms	9/30/80 (note a) No. of BDSs	9/30/80 (note a) Average firms per BDS
I	67	4	17.0	97	10	9.7
II	129	5	26.0	168	8	21.0
III	348	8	43.5	551	24	23.0
IV	121	7	17.0	177	18	9.8
V	175	9	19.4	209	21	10.0
VI	196	11	17.8	245	15	16.3
VII	61	8	7.6	85	1	85.0
VIII	75	2	37.5	128	9	14.2
IX	219	5	43.8	313	10	31.3
X	91	5	18.2	165	10	16.5
Total	1,482	64	23.2	2,138	126	17.0

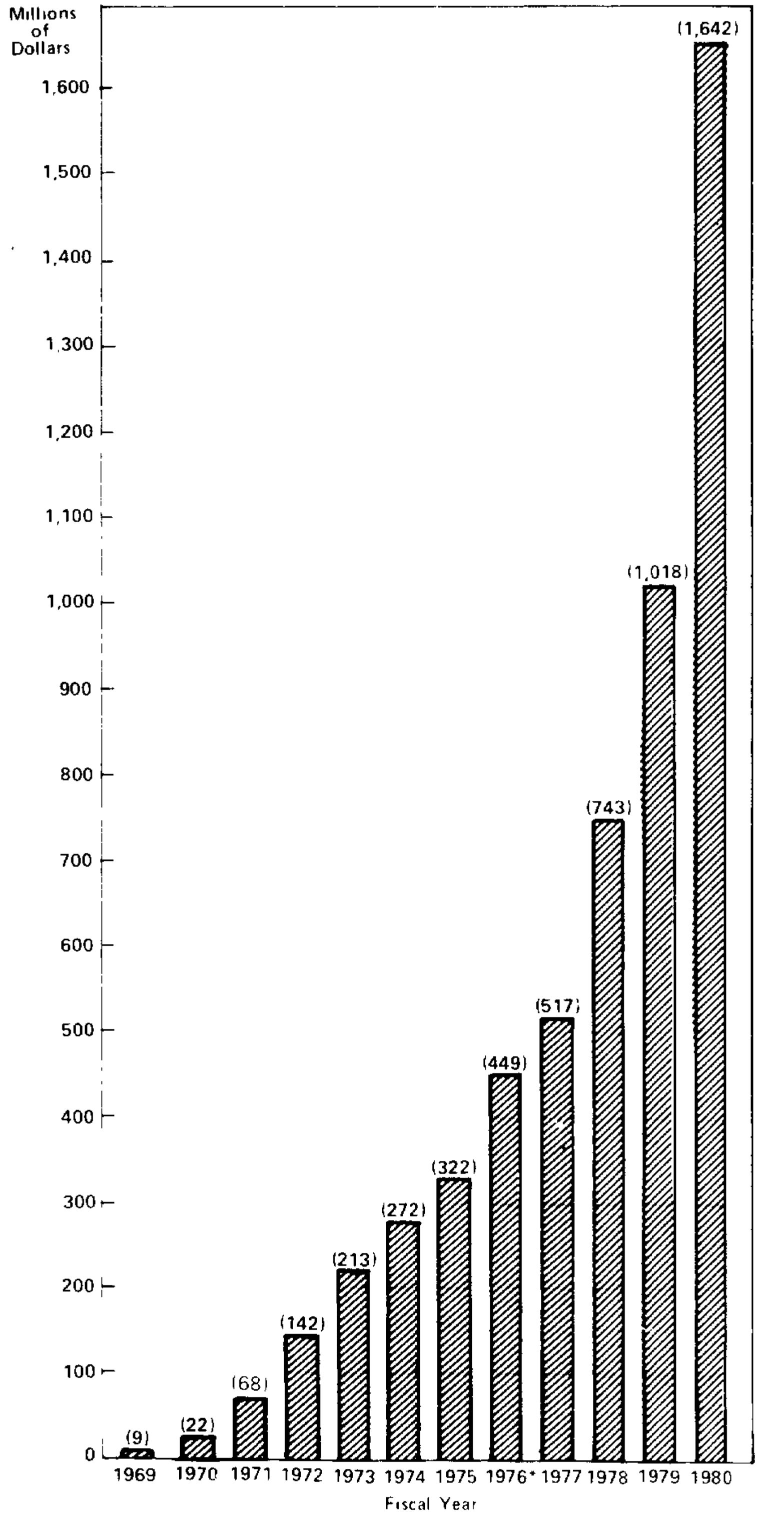
a/Nationwide, an additional 31 vacancies for BDS positions remain.

The majority of the increase, from 64 to 126 BDSs, resulted from the transfer of SBA personnel from the Procurement Assistance Division to the Office of Minority Small Business and Capital Ownership Development to absorb the added functions required when Public Law 95-507 was passed. Part of the added functions was handling the 8(a) contract workload, which dramatically increased. In fiscal year 1977, $517 million was awarded, representing 2,771 contracts, whereas $1.6 billion, representing 5,086 contracts, was awarded in fiscal year 1980.

An SBA work standards study done in 1975 determined that 8 to 10 firms was considered the ‑al number of active firms for servicing by a BDS. In theory, ‑c Law 95-507 gave increased impetus to the business development function of the program. It increased the duties of the BDS to develop 8(a) firms. The Philadelphia district Chief of Management Assistance told us that the new law has made the BDS the main link in assuring that the management and technical needs of active 8(a) firms are served.

In reality, BDSs do not have enough time to do all the tasks required of them. For example, in the Atlanta District, two BDSs were trying to serve 40 active 8(a) firms. The Assistant District Director told us that staffing is so inadequate that the situation has become ridiculous. The Atlanta Regional Director indicated that many BDSs in region IV are weak in business development skills and lack contracting and financial

Total Dollar Value
of 8(a) Contracts Placed



*15 Month fiscal year includes transition quarter

Firm C - Has been in the 8(a) program at least 5 years to our knowledge. Between 7/1/77 and 6/30/80, this firm was awarded 12 8(a) contracts totaling $6,299,523.

Firm D - Has been in the the 8(a) program at least 10 years to our knowledge. Between 7/1/77 and 6/30/80, this firm was awarded 24 8(a) contracts totaling $5,636,835.

"The above figures do not include contracts achieved competitively, and also only cover a 3-year period. In our opinion, with considerable experience in this general business line, these firms should be able to compete successfully in the marketplace by now or they never will be able to. We feel that they should have been 'graduated' by SBA, and in at least two cases, several years ago."

Fourteen of the 32 respondents seeking access to the program voiced a common concern. Paraphrased, they said that the first question asked by Federal agencies approached regarding contracting opportunities is: "Are you an 8(a) certified firm?" One respondent described the problem as a "Catch-22" situation. While the Federal agency wants the firm to be 8(a) certified, SBA tells the firm that contracting commitments from the agency must first be obtained before SBA will approve its application.

COMPETING GOALS DRIVE THE PROGRAM

Two conflicting goals--developing competitive disadvantaged businesses and increasing the volume of 8(a) contracts--compete with each other to drive the 8(a) program in opposite directions and hamper the program's effectiveness.

Since 1969 SBA envisioned that disadvantaged firms would use 8(a) contract support and other aid to develop into competitive firms. It was never intended that disadvantaged firms remain in the program indefinitely. Rather, it was expected that such firms would gradually rely less on 8(a) contract support and build up sales in the commercial sector until judged viable and self-sufficient.

As far back as September 1973, the SBA Administrator, appearing before the House Select Committee on Small Business stated:

"The Section 8(a) authority is utilized together with other available agency resources, to strengthen and upgrade these small business concerns. It is intended that through the assistance of program resources these concerns will enhance their opportunity to achieve a competitive and profitable

We asked the firm to submit the missing financial data from June 1978 to the present. However, the firm did not respond. While we categorized this firm as not classifiable because of the missing data, every indication is that the firm relies almost solely on 8(a) contract support.

A Chicago district construction firm

This firm, established in 1975, entered the 8(a) program in May 1977. SBA records show the firm received about $111,000 in 8(a) contracts. However, financial statements from the firm for 1977, 1978, and 1979 identified only $17,000 as 8(a) sales. Apparently the firm failed to break out 8(a) and non-8(a) sales on two of its financial statements.

The firm has fared well commercially, doing about $1 million in non-8(a) sales. The firm's net income increased from $36,000 in 1977 to $71,000 in 1979. Because of the incomplete financial data, we were unable to determine the full scope of the firm's development and called it "not classifiable."

DOORS TO THE 8(a) PROGRAM CLOSED FOR OTHER DISADVANTAGED FIRMS

Many disadvantaged firms have been denied an opportunity to participate in the program because SBA has not taken graduation or termination action on 8(a) firms whose continued participation is questionable.

Since Public Law 95-507 was passed, about 879 firms have been processed to SBA's central office for admittance to the program. About 396, or 45 percent, were not approved, mostly because SBA did not have potential contracts to support the firms' specialties or skills. However, an SBA headquarters official in the Eligibility Division told us that some applications were rejected because 8(a) contract support was only enough to satisfy the needs of active 8(a) firms having a similar capability.

We noted such a situation in the San Francisco district. A landscaping firm's application was denied because the central office indicated no support was available. Our analysis disclosed that there were three landscaping firms in the district's portfolio. These firms had received 15 contracts totaling more than $1.5 million. All three firms had been in the program over 6 years. We were unable to determine the status of the three firms because of missing data. However, the award of $1.5 million confirms that landscaping contracts were available and these types of contracts are normally renewed. Potentially, if any of the three firms had been removed, the new applicant probably could have been approved for the 8(a) program. In our opinion, rejected firms will continue to be shut out unless there is program turnover.

Nineteen of the 26 firms have been in the program 4 or more years. SBA had experienced difficulty in identifying potential contracts for a few of these firms and had questioned whether these firms should have been admitted to the program. The following case study illustrates a typical firm falling in this category.

Firm No. 24--A Chicago district professional firm

A professional services firm in the Chicago district has been in the portfolio since April 1972. In that time, SBA obtained only one 8(a) contract for the firm with a potential value of $150,000. About $3.2 million in 8(a) sales had been projected.

Financial data available for 1973-79 shows that total sales were $4.2 million of which only $18,000 was attributable to the 8(a) contract. The $18,000 reflected only partial realization of the 8(a) contract for $150,000 because the procuring agency discontinued the contract in view of the precarious financial condition of the firm. The firm had been terminated from the program between April 1975 and February 1976. It was reinstated only after the $150,000 contract opportunity was located.

Additional 8(a) support seems equally unlikely at the present time. In February 1980, district personnel concluded that

> "the possibility that the firm should not be in the portfolio due to the absence of a sufficient amount of 8(a) contracts in its highly technical area must be considered."

In the record of that visit, SBA personnel noted that efforts to generate potential 8(a) contracts for the firm have not materialized and that the success of any new marketing effort "over the same territory" would be dubious. District personnel told us that the firm had not been marketed properly in the past and that a limited Government market is available through two Federal agencies. However, one of those agencies had discontinued the sole 8(a) contract that had been obtained for the firm.

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Nationwide, about 21 percent of the 1,589 firms in the program on January 1, 1979, and still active on September 30, 1980, did not receive a single 8(a) contract during that period. Some firms provide services or products which are provided by a number of 8(a) firms. Possibly, the available contract support may not be sufficient to sustain the number of firms having similar capabilities. In addition, SBA may not be equitably distributing procurements across the firms.

Other firms appear to make products or have skills that are not suited to what the Government purchases. The Atlanta Assistant Regional Administrator told us that his region has a "hit

All business classes except professional services have more prior 8(a) participants than active ones. Statistically, professional service firms represent 25 percent of active firms but only about 3 percent of prior participants. Of the 166 firms that graduated as self-sufficient businesses, only 2 were professional service firms.

In some cases, the failure to develop a commercial market is not entirely the fault of the 8(a) firms. For example, a San Francisco district supervisor told us that often firms get so many 8(a) contracts in relation to the firm's capacity that the firms do not have the time to seek out commercial business. An SBA District Director, quoted in a recent business magazine, offered a hypothetical case that illustrates the above problem.

> "'We can take a good business and ruin it with the 8(a) program,' he contends. 'For instance, let's take a $100,000-a-year sheet-metal company that joins 8(a). We'll work up a business plan for him, find him a requirement, make his bid for him, help him negotiate a contract, get his finances and get him into business. Unfortunately, we rarely are able to get contracts from the procuring agencies that are suited to the contractor's capabilities.
>
> "'More often than not, we find a $250,000 sheet-metal goods contract for him. He's not going to turn it down, even though all his people are presently working as hard as they can to turn out $100,000 worth of work. If he attempts to keep his commercial work, he'll have to bring in two and a half times his current staff, train them and be trained himself in the heretofore unknown world of government contracting, with its auditors, inspectors, paperwork and requirements. We might give him $100,000 for a piece of equipment--say a big pc r-driven sheet-metal break. I don't know how many ye someone in the sheet-metal business would have work to save enough profit to buy something like t t.
>
> "'So here he is with a big computerized power break, two and a half times as many people, ten times as many people wandering in and out of his office from the Government and ten times as much paperwork.'"
>
> * * * * *
>
> "'What he does is drop the commercial work, on which he's only making 3 or 4 percent profit, and concentrate on the government work with its 15 to 20 percent profit.

Eighteen of the 27 firms have been in the program 5 or more years. In addition, 14 of the firms were either directed by SBA to do a better job of developing a commercial market or were recommended for termination because they failed to make measurable progress towards increasing their reliance on commercial sales. Records generally were not available to determine why termination recommendations were not carried out. Two case studies illustrate typical firms falling into this category.

Firm No. 4--A San Francisco district nonprofessional service firm

This firm entered the program in 1971. Since joining, its reported annual sales have been almost exclusively from 8(a) contracts, which totaled over $10 million.

The firm's reported annual 8(a) sales since 1972 increased from $111,000 to more than $2 million in 1979. The firm's reported non-8(a) annual sales peaked at $277,000 in 1973 and have steadily declined to just $3,300 in 1979. During this same period, the reported annual income ranged from $13,000 to about $330,000. The firm's net worth was more than $600,000 as of March 31, 1980.

The firm received two SBA loans totaling $165,000, advance payments of $150,000, and business development expense of $16,806.

SBA notified the firm in 1977 that it would be considered for termination unless its non-8(a) sales increased by at least 25 percent of its 1976 8(a) sales. We calculated that this would amount to an increase of $279,000 for non-8(a) sales. The firm, however, did not even come close to meeting this goal at anytime from 1977 to March 31, 1980. The highest reported annual non-8(a) sales figure was approximately $46,700 in 1977. SBA records did not contain any indication of follow-up actions regarding its proposal to terminate the firm.

Firm No. 20--A Philadelphia district professional service firm

This firm entered the program in April 1974 and has relied almost solely on 8(a) contracts for its support. Based on available sales records, the firm reported $69,000 in commercial work obtained before 1977. In contrast, the firm received $3.9 million in 8(a) contracts. Initially, the firm projected that 76 percent of its total sales would be 8(a) contracts. Subsequent revisions have increased 8(a) projections to 89 percent of total sales, indicating an increasing reliance on the 8(a) program.

During a discussion we had with the firm's president, he indicated that although he at one time tried to obtain commercial work, he generally met with no success. He believes that without the 8(a) program he would not be able to survive.

One year later the district obtained a waiver to the $175,000 original projected support for fiscal year 1977 on the grounds that it would be within policy to build sizeable work backlogs for a firm nearing program graduation.

During the 1977 annual review, it was decided to keep the firm because its financial condition was not considered good. Interestingly, the BDS wrote after visiting the firm:

> "I am pleased to report that the firm not only has sustained its previous business, but has met all of its 1976 8(a) Business Plan objectives. The firm is thriving and should be a candidate for 8(a) program completion."

By May 1977 the firm had already exceeded its fiscal year 1977 support level of $700,000 with even more requirements coming available. Further, follow-on awards to existing contracts during fiscal year 1978 would assure that the requested support for that year would be met, thus necessitating increases to the approved fiscal years 1977 and 1978 support levels.

The BDS recommended graduation for the firm during the 1978 annual review. However, the firm was retained, apparently because of a worsening financial picture. No annual reviews of this firm were done since the May 1978 review. However, the firm averaged total sales of about $3 million annually for 1979 and 1980, split equally between 8(a) and commercial sales. The latest projections show total sales increasing to $4.2 million by 1983, with the ratio of 8(a) to commercial work again about equal.

Firm No. 2--An Atlanta district nonprofessional service firm

This firm was approved for the 8(a) program in June 1975. Since program admission, this firm had received a total of $15 million in 8(a) contracts, or 192 percent of its revised business plan goals. The firm also had non-8(a) sales of about $6 million, which surpassed its $2.1 million goal. In addition, this firm received $1,375,000 in advance payments and $126,945 in business development expense.

In December 1979, a BDS recommended

> "* * *that the firm be retained in the 8(a) program for 1 more year (FY 80) because it appears that he would * * * have substantially achieved the objectives of the 8(a) program, including but not limited to, the achievement of goals set forth in * * * the business plan * * * and the attainment of demonstrated ability to compete in the marketplace without assistance from 8(a)."

We also identified 115 firms that were moderately successful in meeting 8(a) and non-8(a) business plan projections and appear to need additional SBA aid. The following table provides a district-by-district breakdown.

Category	District office Atlanta	Chicago	Phila.	S.F.	Total
Firms with substantial 8(a) contracts and non-8(a) sales	2	4	5	11	22
Firms with heavy 8(a) contracts	3	7	4	13	27
Firms with moderate 8(a) contracts and non-8(a) sales (note a)	24	19	25	47	115
Firms receiving little 8(a) contract support	2	6	10	8	26
Firms unclassifiable	9	14	19	35	77
Total	40	50	63	114	267

a/These firms will be discussed in chapter 3.

Firms with substantial 8(a) and non-8(a) Sales

We classified 22 firms in this category because they generally received more than 100 percent of 8(a) contracts and generated more than 75 percent of non-8(a) sales based on either initial or revised business plan projections. SBA's ability to provide 8(a) contracts and a firm's success in developing commercial sales in accordance with business plan projections is one of the measures used to identify graduation candidates. The sales history for the 22 firms is shown in the following table:

BULK OF CONTRACT DOLLARS
GO TO A HANDFUL OF FIRMS

A small group of 8(a) firms, some of them competitive, have received the bulk of SBA's 8(a) contract dollars. About $1.7 billion, or 31 percent, of the $5.5 billion of 8(a) contracts went to 50 active firms. They included businesses engaged in construction, manufacturing, professional and non-professional services and represented about 1 percent of the total 4,598 program participants. Over three-fifths of the firms have been in the program between 7 and 11 years.

Contract support for the 50 firms ranged from a high of $126 million to a low of $15.7 million and averaged $34.5 million per firm. Curiously, these 50 active firms have received almost five times as much contract assistance as the 166 firms that have graduated from the 8(a) program as competitive businesses.

Overall, the 2,138 firms still active in the program have received $4.6 billion, or 84 percent, of the $5.5 billion in 8(a) contract support.

A Philadelphia district BDS characterized the situation as "the rich get richer and the poor get poorer." He told us that the district began each year with the objective of distributing 8(a) contracts equitably across the firms. But inevitably, firms that were aggressive self-marketers complained when the district decided to give procurements that these firms identified to a different 8(a) firm. The district then relented, and the contracts went to the firms that did the self-marketing.

The SBA headquarters Chief of the Requirements Division told us that poor management by SBA results in 8(a) firms being helped unevenly. He said that numerous instances exist of certain firms receiving multimillion dollar contracts year after year while other firms having similar capabilities receive nothing. He offered several other explanantions for this situation:

--8(a) firms have strong political connections that they are quick to use if any of their contracts are in jeopardy.

--Federal procurement agencies prefer to stick with the same 8(a) firms.

--Federal procurement agencies believe adding quantities to existing 8(a) contracts is easier than negotiating new contracts with other 8(a) firms.

District	Total participants	Number of graduates
Atlanta	177	4
Chicago	195	8
Philadelphia	108	2
San Francisco	278	4

Region and district officials pinpointed several common reasons for the low number of graduates:

--Lack of incentive for firms to leave the program since the contracts are noncompetitive.

--Lengthy administrative process to get central office approval for graduation.

--Right of appeal available to 8(a) firms to protest the graduation action.

The Atlanta Assistant Regional Administrator told us that, in the rare cases when his region decided to graduate a firm, it often enticed the firm to leave without protesting the action or pursuing the extensive appeals process. Candidates were offered a "graduation gift" in the form of a large contract to soften the impact of leaving the program.

The San Francisco Assistant Regional Administrator told us that a past Regional Administrator had an unwritten policy that no firms were to be graduated from the program while he was in office. The Assistant District Director in Chicago told us that graduation action is generally not taken unless the firm voluntarily signs a completion agreement.

In recent years, SBA's track record for graduating competitive firms has worsened. Despite providing an increasing volume of 8(a) contracts, the rate of graduations went down. The following chart shows the number of yearly graduations nationwide.

CHAPTER 2

BUSINESS DEVELOPMENT OR CONTRACT BROKERING--

WHAT SHOULD THE 8(a) GOAL BE?

The major goal of the 8(a) program--developing competitive disadvantaged small businesses--has still not been reached. Success stories are rare. Only 4 percent of the firms admitted over the years have graduated from the program as self-sufficient businesses. Interestingly, many firms in the program are concerned with getting more noncompetitive 8(a) contracts and do not need or were dissatisfied with SBA's management, marketing, and technical aid.

The program has done too much for too few for too long. About $1.7 billion, or 31 percent, of the total 8(a) contract support has gone to 50 active firms. Three-fifths of these firms have been in the program between 7 and 11 years and seem to have no incentive to leave the program's umbrella.

A number of other firms should be terminated from the program because they claim to have no commercial market or have failed to develop one. We question whether some firms, which have been in the program for several years and have received little or no 8(a) contract support, should continue to participate in the program.

Since passage of Public Law 95-507, about 400 disadvantaged small business applicants have been rejected for the program. Many of these firms have been denied an opportunity to participate in the 8(a) program because graduation or termination action is not being taken to remove questionable firms from the program.

The limited program achievements have resulted because SBA is pursuing two competing goals: maintaining the volume of 8(a) contracts and developing competitive disadvantaged businesses. SBA and the Federal procuring agencies must meet annual goals imposed by the President aimed at increasing the dollar volume of 8(a) contracts. Thus, SBA is reluctant to graduate firms from the program--especially firms that get large contracts--since doing so would be counterproductive to the goal of increasing the 8(a) contract volume.

Other problems hamper the program's effectiveness. Because of insufficient staff, the program is poorly monitored. A lack of specific and objective criteria makes it difficult to determine a firm's business development status and many firms have not submitted required financial statements and business plans. Without adequate criteria and with significant information missing, the limited SBA program personnel find it difficult to even start to assess whether many firms are making progress. In our opinion, SBA has assigned a low priority to business development and instead functions much like a contract broker

Each firm submits a business plan projecting, usually on a 3-year basis, the amount of 8(a) contract support and the growth in commercial and other Government business (referred to as non-8(a) sales) needed to reach self-sufficiency. Over time, the plan should reflect a reduced dependence on 8(a) contract support and increased reliance on non-8(a) sales. The plan may be revised when circumstances change.

Depending on the type of business, the plan can require profile data on the firm's product line or service, market area and competitors, pricing policies, production capabilities, work force composition, past financial performance, and completed and ongoing work. The plan must also project expected operating performance for the next 3 years and estimated cash-flow needs for the next 12 months.

PRIOR STUDIES OF THE 8(a) PROGRAM REPORTED MANY PROBLEMS

The 8(a) program has been evaluated several times over the past 6 years. Reports have been issued by us, SBA's Inspector General, and SBA internal organizations and hearings have been held by congressional committees. (App. I summarizes the major issues and recommendations from some of these evaluations.) These studies criticized how SBA administers the program and pointed to the program's meager achievements. Deficiencies mentioned included

--questionable eligibility of disadvantaged persons;

--inadequate management assistance provided to 8(a) firms;

--insufficient staff for program monitoring;

--a low graduation rate of 8(a) firms as competitive businesses; and

--a disproportionate emphasis on the volume of 8(a) contracts instead of business development.

In short, the reasons why the program is ineffective have long been known to Congress, SBA, and to other outside organizations. Despite the criticism, adequate corrective action has not been taken and the problems continue.

OBJECTIVES, SCOPE, AND METHODOLOGY

In accordance with our mandate under Public Law 95-507 and a result of subsequent meetings with the Senate Select and use Committees on Small Business, the principal objectives of is review were to

The law established the Minority Small Business and Capital Ownership Development Program and vested primary responsibility for the 8(a) program in the Associate Administrator for Minority Small Business and Capitol Ownership Development. 1/

The law also revised the eligibility criteria for 8(a) participation by limiting aid to firms owned or controlled by both socially and economically disadvantaged persons. It requires SBA to determine that potential 8(a) contracts and other aid to support a firm are available before admitting the firm to the program. The law further specifies that, with such aid, a participating firm must have reasonable prospects for success in competing in the private sector.

The law implies that 8(a) firms would eventually complete the program. In this connection, House Conference Report No. 95-1914 on the bill that eventually became Public Law 95-507 reports the conferees' agreement:

> "That no one be found eligible * * * unless the SBA determines that it has the requisite contract, financial, and management assistance to promote the competitive viability of the firm within a reasonable period of time and that with such assistance, the firm does have the potential to successfully complete the program."

Size of program activity

As of September 30, 1980, 4,598 firms have participated in the program; 2,138 of these firms remain active. SBA has awarded 27,276 contracts totaling about $5.5 billion to 8(a) firms during the more than 12-year operation of the program. These firms have also received $220 million in advance payments to fund cash-flow problems. An additional $73 million of business development expense was provided to subsidize price differentials and purchase capital equipment.

How the program is administered

To aid the estimated 11 million small businesses in the United States, SBA administers a variety of programs, including the 8(a) program, through a central office, 10 regional offices, and 82 district and branch offices.

1/Public Law 96-481, enacted on October 21, 1980, transferred primary responsibility for the 8(a) program back to the Administrator, SBA.

ABBREVIATIONS

BDS	business development specialist
GAO	General Accounting Office
SBA	Small Business Administration
SOP	standard operating procedure

Recent legislation made some changes to the 8(a) program and now requires that a graduation date must be negotiated with existing firms and with firms newly accepted into the program. The legislation establishes a mutually agreed upon period of time for SBA to help a firm. The time period can be revised if conditions warrant. This is a step in the right direction. However, GAO believes problems will continue so long as the criteria for graduation remains vague. Too many factors hinder SBA's ability to assess a firm's status. SBA will be faced with the dilemma of constantly negotiating new dates for most 8(a) firms judged as not yet competitive.

GAO thinks that a two-tier program combining 8(a) participation with a disadvantaged small business set-aside program or a separate disadvantaged small business set-aside program appear to have some potential for changing the program's direction and improving its effectiveness.

MATTERS FOR CONSIDERATION BY THE SENATE SELECT AND HOUSE COMMITTEES ON SMALL BUSINESS

Should the committees decide to change the program, GAO proposes several alternatives:

--Continue the present 8(a) program, which assumes that its effectiveness can be improved if corrective actions are taken.

--Reduce the size of the present 8(a) program, which would free up limited staff to provide better services to a smaller number of firms who want and need business development.

--Establish a two-tier program that would set a fixed limitation for firms to participate in the 8(a) program before moving to a second-tier program. During the second stage, firms would compete with other disadvantaged businesses under a disadvantaged small business set-aside program.

GAO questions whether 75, or 28 percent, of the 267 firms analyzed in the four SBA districts should continue in the program. For example, 27 firms received heavy 8(a) contract support but have not built up non-8(a) sales, despite business plan projections to the contrary. (See pp. 11 to 20.)

Most firms view the program as an end in itself. Almost 75 percent of the 316 responding 8(a) firm officials indicated that they were mainly interested in getting more contracts. In addition, more than half of the 316 respondents were dissatisfied with or did not need SBA's management, technical, and marketing aid. (See pp. 29 and 30.)

GAO believes that many 8(a) firms have received all that SBA has to offer and have had ample time to develop. Because SBA is not graduating or terminating these firms, other disadvantaged firms have been denied entry into the program. Almost 400 firms applied but were rejected since legislation was passed. Most firms were rejected because additional 8(a) contracts were not available. Removing inappropriate 8(a) firms from the program would give other disadvantaged firms an opportunity to participate. (See pp. 22 to 24.)

RIGHTS OF OTHER SMALL BUSINESSES MUST BE SAFEGUARDED

SBA's required assessments of whether 8(a) contract awards will have an impact on other small businesses were not always made or, in some cases, were superficial. SBA districts were using different criteria to measure whether other small businesses were harmed by the program.

As the Government increases contracting with disadvantaged businesses, the rights of other small firms must be safeguarded. SBA, as well as Federal procurement agencies, should also do more to get big businesses to assume a share of the 8(a) burden, thus minimizing the impact on small businesses. (See pp. 45 to 52.)