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STATEMENT OF
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BEFORE THE
SUBCOMMITTEE ON SCIENCE,
RESEARCH AND TECHNOLOGY
OF THE
HOUSE COMMITTEE ON SCIENCE AND TECHNOLOGY
ON
IMPLEMENTATION OF THE SMALL BUSINESS
INNOVATION DEVELOPMENT ACT OF 1982



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Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today at your request to discuss our October 25, 1985, report on the implementation of the Small Business Innovation Development Act of 1982 (GAO/RCED-86-13). Our report, which covers fiscal years 1983 and 1984, assesses the extent to which agencies established, funded, and provided accurate information on those activities required by the law. It also assesses program coordination, monitoring, and congressional reporting activities of the Small Business Administration (SBA) and the Office of Science and Technology Policy (OSTP). We also are providing the limited amount of update information which we have at this time.

We found that agencies, for the most part, complied with the act's funding requirements, but that most did not fully adhere to the act's reporting requirements. In the area of program oversight and monitoring, we found that SBA actively pursued and fulfilled its responsibilities, while OSTP elected to limit its efforts.

I will briefly review some of the key provisions of the act, along with our findings.

SBIR PROGRAMS

The act requires each federal agency that spends more than \$100 million annually on extramural research to establish a small business innovation research program. These programs, commonly called SBIR programs, are open only to small

businesses. Agencies must spend specified percentages (up to 1.25 percent) of their extramural funds on SBIR programs and must report program and funding data annually to both SBA and OSTP.

Each agency participating in the SBIR program must follow a three-phase funding process. Each year the agency solicits project proposals and selects a limited number for Phase I funding. During this first phase, the agency awards each company limited funding (usually \$50,000 or less) over a short time (normally 6 months or less) to demonstrate the feasibility of a proposed project. The agency selects the best completed Phase I projects for Phase II, during which the agency awards additional funds (usually \$500,000 or less) over a 1 to 2-year period to carry out the principal research or R&D efforts. In the third phase, firms are expected to commercialize their new technologies through non-federal sources or, if appropriate, through traditional (non-SBIR) federal agency procurement programs. No SBIR funds may be used during the third phase.

Currently, 11 agencies meet the extramural funding criterion and have SBIR programs. Through fiscal year 1985, SBIR agencies had received over 26,000 proposed projects and made almost 3,900 SBIR awards totaling \$355 million.

Technically, compliance with the act's SBIR funding percentages must be determined using actual obligations. Most agencies, however, reported extramural figures to SBA

reflecting estimated obligations or appropriations. This was done, by and large, because estimations were more readily available than actual obligations when the agencies had to report to SBA in late December. Most agencies said that it would be difficult to report the proper figures because doing so would require extra work for budget personnel who are already busy at that time of year preparing final budget submissions to the Office of Management and Budget. Most agencies said, however, that they could report actual extramural obligations by early March, which is the normal date for reporting these and other research funding data to the National Science Foundation (NSF).

In our report we therefore recommended that SBA revise its reporting deadline to March, and that agencies report actual obligations. Most of the affected agencies agreed with these recommendations and SBA has since revised its reporting deadline to March 15. Using the actual obligation figures that agencies reported to NSF, we determined that most agencies either met or came very close to meeting their required SBIR percentages.

There remains, however, an important outstanding dispute between SBA and the Department of Defense regarding the amount of DOD's extramural research budget. SBA considered the budget to be \$17.9 billion for fiscal year 1984, while DOD contended that the proper figure was about \$2 billion less. This translated into a difference of almost \$11 million in the

required SBIR funding. The discrepancy occurred because DOD inconsistently classifies the Operational Systems Development category of its research appropriations (category 6.6) when reporting research and development budget data to SBA, NSF, and OMB. This category funds research for needed changes to weapon systems that are already operational or in production. DOD excludes the category when reporting its extramural R&D budget to SBA, but includes this same category when reporting its R&D expenditures to NSF and to OMB. SBA uses the figures reported to NSF to estimate agencies' extramural research funding.

DOD originally excluded the 6.6 category when reporting to SBA because it contended that activities in the category do not conform to the act's definition of R&D. SBA maintained that NSF's definition of R&D is the same as that in the act. In our report, we agreed that the definitions are the same and recommended that DOD report consistent figures.

Subsequently, in response to a request from the House Small Business Committee, the Comptroller General issued a legal opinion (B-209790, Feb. 21, 1986) which concluded that DOD activities conducted with 6.6 funds are within the definition of R&D specified in the Small Business Innovation Development Act. Thus, the extramural portion of such funds should be reported to SBA and included in calculating DOD's mandatory SBIR funding amount.

DOD, however, has raised some practical difficulties to including 6.6 funds in the SBIR funding base--in particular the fact that these funds are largely committed to specific weapons systems contractors and thus offer no real opportunity for small business competition.

DOD's current position is that it still will not include 6.6 funds when reporting to SBA but will explain which funds have been excluded and the basis for that exclusion. We note that H.R. 4260 would exempt the 6.6 funds.

NON SBIR GOALS

Because Congress intended that the SBIR program be a net addition to the agencies' existing small business research awards, all agencies with total research budgets exceeding \$20 million are required to set goals for awarding research funds to small businesses. These goals must at least equal the percentage of an agency's total research budget that went to small businesses the preceding year; SBIR awards cannot be counted toward meeting an agency's non-SBIR goals.

Most of the 18 agencies required to have non-SBIR goals collected and reported fiscal year 1983 and 1984 goals data to SBA. However, in both fiscal years most agencies did not provide SBA with all the data needed to properly determine goal

attainment. For example, in fiscal year 1983 some agencies reported no data at all, while others reported extramural rather than total research dollars as a base for their goals. While the quality of data improved in fiscal year 1984, the amount of total research dollars (the legislatively required basis for computing goals) that agencies reported to SBA differed from that reported in the President's budget. One reason for the inconsistency is that agencies do not normally make their budget figures final until after SBA's December reporting deadline.

We could not determine whether the agencies actually met their goals because the data reported to SBA were either inconsistent or inappropriate as a basis for judging goal attainment. We did, however, recommend that certain actions be taken in order to make goals meaningful targets. In particular, we recommended that agencies set their goals at the beginning of the fiscal year and make those goals known to program officials responsible for awarding external R&D funds. The agencies should also collect the information needed to meet SBA's reporting requirements and to determine whether they have achieved their goals by the end of the year. Fewer than half the agencies followed all of these practices. While we realize that following our recommended practices will not guarantee goals achievement, we believe that they are preferable to leaving goals achievement essentially to chance by treating it

as an after-the-fact reporting exercise, as many agencies did. As we also recommended, SBA changed its deadline so that agencies could more easily report non-SBIR goals data.

AMBIGUOUS PARTICIPATION CRITERIA

The criteria for required activities is ambiguous with regard to both the goal setting requirement and the SBIR program. It is not clear whether agencies whose research budgets had met the \$20 million criterion must continue to set goals if they drop below \$20 million in later years. This situation occurred at the Department of Housing and Urban Development, which met the criterion requiring goal setting in fiscal year 1983 but not in fiscal year 1984. As a result, HUD did not submit a 1984 annual report to SBA. Regarding the goals requirement, we recommended that when the act is considered for reauthorization, the Congress make it clear that the \$20 million criterion should be applied annually to identify those agencies that must establish goals.

After our report, the Department of the Interior dropped its SBIR program when its extramural research budget apparently fell below the required \$100 million minimum. Accordingly, Congress may want to make it clear whether the criterion for participation in the SBIR program is an annual one.

PROGRAM OVERSIGHT

The act assigns the Small Business Administration and the Office of Science and Technology Policy similar responsibilities for monitoring and reporting to Congress on the implementation of SBIR programs.

We found that SBA made extensive efforts to fulfill its responsibilities under the act. Specifically, we found that, as required, SBA issued policy directives for the conduct of the SBIR programs that complied with the act. Additionally, SBA made extensive efforts to stimulate small business participation, to coordinate agency solicitations, and to oversee and report on program implementation.

The act requires the Office of Science and Technology Policy--in consultation with an interagency group, the Federal Coordinating Council for Science, Engineering and Research--to independently survey, monitor, and report to the Congress on the implementation and operation of the SBIR programs. Although OSTP has complied with the requirements for monitoring, surveying and reporting to Congress, it purposely limited its activity and has not assessed the quality of the research as envisioned in the reports of the House and Senate Small Business Committees. Thus, the Director of OSTP has not utilized the Federal Coordinating Council for SBIR oversight and OSTP staff have conducted a very limited review of the program. OSTP has submitted annual reports to the Congress for fiscal years 1983, 1984, and 1985. The reports' conclusion that the SBIR agencies were all making "good faith" efforts to accomplish the purposes of the act were based for the most part on review of the agencies' annual reports to SBA and OSTP.

OSTP limited its activity for two reasons--a belief that the required duties are inappropriate and impractical given OSTP's mission and its limited staff resources, and a desire to avoid duplication of what OSTP believes to be adequate monitoring by SBA. Additionally, in its fiscal year 1984 report, OSTP maintained that the quality of research is assured through the competitive review procedures normally utilized by the agencies. Therefore, OSTP holds that further evaluation by OSTP is not necessary any more than it would be for other research programs of the various agencies. The reports of the authorizing committees, however, indicate that the Congress expected OSTP to concentrate on assessing research quality, while SBA would protect the interests of small businesses so that the monitoring roles of the two agencies would complement rather than duplicate each other. Therefore, in our report we recommended that OSTP monitor research quality, utilizing the Federal Coordinating Council for Science, Engineering and Research to do so.

GAO ROLE

The act requires a GAO report on the program by July 1987. Currently, GAO has underway a study of the SBIR proposal review and award process, with a report scheduled for March 1987. Also, we have sent out a questionnaire to a large sample of SBIR award recipients to obtain information on the characteristics of firms receiving awards and their experience with the program.

This information, together with the views of the agencies on the impact of SBIR on their overall research programs is scheduled to be presented in our summary report, which is scheduled for June 1987.

This concludes my statement, Mr. Chairman. I will be happy to respond to any questions.