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The Honorable Sam Nunn
Chairman, Committee on Armed Services
United States Senate

The Honorable Dale L. Bumpers
Chairman, Committee on Small Business
United States Senate



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The Honorable Ronald V. Dellums
Chairman, Committee on Armed Services
House of Representatives

The Honorable John J. LaFalce
Chairman, Committee on Small Business
House of Representatives

The Miller Act (40 USC 270a, et seq.) requires federal construction contractors to provide performance and payment surety bonding. The Conference Report (H.R. Rep. No. 102-311) on the National Defense Authorization Act for Fiscal Years 1992 and 1993 (Public Law 102-190) directed the General Accounting Office to assess the Department of Defense's (DOD) implementation of a test program in which it was to award construction contracts to small and disadvantaged businesses that DOD or the Small Business Administration (SBA) exempted from the requirements of the Miller Act.

The SBA and DOD were initially directed to establish the test program in 1989, and in 1992 we reported¹ that use of the surety bond exemption authority had been quite limited through fiscal year 1991. Since that report was issued, both SBA and DOD have continued to make very little use of the exemption authority. We are providing factual

¹Small Business: Use of the Surety Bond Waiver Has Been Limited (GAO/RCED-92-166, July 7, 1992).

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information on the contracts that were exempted in fiscal years 1992 and 1993, through June of 1993. Enclosure I to this letter contains that information.

To obtain the information presented in this letter, we (1) reviewed surety bond exemption legislation, regulations, and procedures; (2) interviewed officials from SBA headquarters; the Small and Disadvantaged Business Utilization offices of the Office of the Secretary of Defense, Army, Navy, and Air Force; (3) interviewed Army contracting officers who awarded contracts utilizing DOD's exemption authority; (4) interviewed officials from associations that represent the surety industry and producers and minority contractors; and (5) obtained and analyzed DOD and SBA program data. We performed our audit work between March and June 1993.

Please contact me at (202) 512-4587 if you or your staff have any questions concerning this letter. Major contributors to this letter were Patrick S. Donahue, Assistant Director, and Charles W. Malphurs, Evaluator-in-Charge.



David E. Cooper
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BACKGROUND

Congress passed the Miller Act in 1935 in order to protect the federal government and designated persons furnishing material and labor on federal construction projects. The act presently requires federal construction contractors to provide performance and payment bonds in the case of awards exceeding \$25,000. The performance bond ensures that if the contractor does not complete the contracted work, the surety (the entity providing the bond) will either pay the costs of fulfilling the terms of the contract or a penal amount of up to 100 percent of the contract price to the government. A payment bond guarantees that employees, subcontractors, and suppliers will be paid for work performed and/or materials provided under the contract.

Section 833 of the National Defense Authorization Act for Fiscal Years 1990 and 1991 (P.L. 101-189) required DOD and the SBA to establish a test program whereby DOD would make a reasonable effort to award not less than 30 construction contracts in each fiscal year to small and disadvantaged businesses participating in SBA's 8(a) program¹ that had been granted surety bond exemptions by SBA pursuant to the administration's authority under 15 USC 636(j)(13)(D). This test program has since been extended through fiscal year 1994. Furthermore, the National Defense Authorization Act for Fiscal Years 1992 and 1993 (P.L. 102-190) authorized the Secretary of Defense to grant surety bond exemptions to 8(a) program contractors without approval by or consultation with SBA during the test program, and it retained the not fewer than 30 awards-per-year goal.

In July 1992 we issued an interim report,² as called for in the conference report on the earlier DOD authorization act. Our findings related to the first years of the test program. We found

¹To be eligible for SBA's 8(a) program, a firm must be a small business that is at least 51 percent unconditionally owned and controlled by one or more socially and economically disadvantaged individuals. Under the 8(a) program SBA, acting as a prime contractor, enters into contracts with other federal agencies and subcontracts the work to firms participating in the program. The 8(a) program is authorized in the Small Business Act, as amended.

²Small Business: Use of the Surety Bond Waiver Has Been Limited (GAO/RCED-92-166, July 7, 1992).

that DOD fell far short of the congressional goal of 30 bond waivers per year in fiscal years 1990 and 1991.

FISCAL YEAR 1992-93 PROGRAM

In fiscal years 1992 and 1993, the congressional goal calls for DOD and SBA to make a reasonable effort to exercise the bond exemption authority at least 30 times per year in awarding DOD construction contracts. During fiscal year 1992 and through June 30, 1993, DOD and SBA awarded a total of nine contracts that utilized the exemption authority. DOD awarded seven of the nine contracts utilizing its independent authority as indicated in table 1. These awards aggregated \$4.1 million. For comparison purposes, in fiscal year 1992 DOD had 1,313 sole-source procurement actions, in the range of \$25,000 to \$3 million, with 8(a) construction contractors.

Table 1: Number of DOD Awards to 8(a) Construction Contractors Granted Surety Bond Exemptions by SBA³ or DOD.

Fiscal year	Grantor	Army	Navy	Air Force	Total
1992	SBA	0	0	1	1
	DOD	3	0	0	3
1993	SBA	0	0	1	1
	DOD	4	0	0	4

In addition, we found that Army officials did not follow some of the required procedures on five of the seven contracts that utilized DOD's waiver authority. These officials did not make payments to the contractors through a special bank account on the five contracts as required by DOD regulations.⁴ These regulations

³An SBA official advised us that SBA had also granted exemptions in the case of two awards that were made by civil agencies of the federal government in 1992 and that at least one more of these was granted in 1993.

⁴Defense Federal Acquisition Regulation Supplement (DFARS 219.808-1(b)).

require contracting officers to ensure that the contractor, before award, establish a special bank account to afford payment protection to suppliers and subcontractors expected to provide materials or services. According to an Army official, the contractors' performances on the five contracts have been satisfactory and, in fact, three of these projects have been completed. However, Army officials told us it is too early to assess the performance of the contractors awarded the other two. An Army official told us that they have taken action to ensure that required procedures are followed in the future.

We interviewed DOD and military service officials with responsibility for the test program. Most of them viewed exercise of the bond exemption authority as a time-consuming administrative effort that poses increased risk and affords little, if any, benefit in assisting responsible 8(a) construction firms to meet those firms' development plans. In addition, most of the officials we spoke with believe that surety bonding requirements rarely if ever represent a significant impediment to these firms. However, the contracting officers who awarded the two contracts that were administered according to DOD's regulations believe the process involved in utilizing DOD's exemption authority is not significantly burdensome.

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