

**AUDIT OF MONITORING COMPLIANCE WITH 8(A)  
BUSINESS DEVELOPMENT REGULATIONS DURING  
8(A) BUSINESS DEVELOPMENT CONTRACT  
PERFORMANCE**

**AUDIT REPORT NO. 6-15**

**MARCH 16, 2006**

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**U.S. SMALL BUSINESS ADMINISTRATION  
OFFICE OF INSPECTOR GENERAL  
WASHINGTON, D.C. 20416**

<b>AUDIT REPORT</b>
<b>Issue Date: March 16, 2006</b>
<b>Report Number: 6-15</b>

**TO:** Anthony Martoccia  
Associate Deputy Administrator for Government  
Contracting and Business Development

Michael J. Pappas  
Associate Administrator for Field Operations

**/s/ Original Signed**

**FROM:** Robert G. Seabrooks  
Assistant Inspector General for Auditing

**SUBJECT:** Audit Of Monitoring Compliance With 8(a) Business Development  
Regulations During 8(a) Business Development Contract Performance

The Office of Inspector General (OIG) completed an audit to determine whether Federal agencies were effectively monitoring compliance with 8(a) Business Development (BD) regulations when completing 8(a) BD contracts. This audit began with a complaint about potential violations by an 8(a) BD company when completing contracts. As we were conducting our review of these violations, we expanded our review to cover SBA's and the procuring agencies' monitoring of compliance with 8(a) BD regulations during the performance of 8(a) BD contracts. This report presents the results of our audit.

### **BACKGROUND**

According to 13 Code of Federal Regulations (CFR) § 124.1, "The purpose of the 8(a) BD program is to assist eligible small disadvantaged business concerns compete in the American economy through business development." According to § 19.8 of the Federal Acquisition Regulation (FAR), "Section 8(a) of the Small Business Act (15 U.S.C. 637(a)) authorizes the Small Business Administration (SBA) to enter into all types of contracts with other agencies and let subcontracts for performing those contracts

to firms eligible for [8(a) BD] program participation.” SBA has implemented various regulations with which 8(a) BD companies must comply when performing these contracts. These regulations are cited in 13 CFR § 124, as well as FAR § 19, 42, and 52.

SBA retains the ultimate responsibility for ensuring that 8(a) BD companies comply with all applicable 8(a) BD program regulations. However, starting in 1998, SBA delegated the contract execution function to 26 procuring agencies by entering into partnership agreements/memorandums of understanding with them. The delegated authority includes ensuring compliance with FAR regulations, which includes 8(a) BD contract regulations. SBA has the authority to conduct surveillance reviews at the procuring agencies to ensure, among other things, that procuring activities have followed the proper procedures in executing 8(a) BD contracts and, if necessary, to provide suggestions, training or assistance to enable them to improve their procedures.

### **OBJECTIVES, SCOPE AND METHODOLOGY**

Our objectives were to determine whether (1) Federal agencies ensured that companies complied with 8(a) BD contracting requirements when completing 8(a) BD contracts; and (2) an 8(a) BD company complied with critical contracting requirements in completing 8(a) BD contracts.

We reviewed the Small Business Act, the FAR, the CFR, Standard Operating Procedure (SOP) 80 05 3 “8(a) Program,” and the latest partnership agreements between SBA and 26 procuring agencies to determine what responsibilities SBA and the procuring agencies have in monitoring contractor compliance with 8(a) BD regulations during contract performance. We also reviewed the FAR and the CFR to determine what SBA regulations companies must comply with when performing contracts. We interviewed SBA counsel in order to gain a better understanding of 8(a) BD regulations.

We interviewed an SBA official as well as one contracting officer and one technical representative from each of the 23 major procuring agencies (23 of the 26 agencies which have partnership agreements with SBA) to understand each agency’s internal requirements for monitoring compliance with 8(a) BD regulations. Since most agencies could not provide official listings of their employees designated for overseeing 8(a) BD contracts, we judgmentally selected representatives from each agency based on their applicable experience with these contracts.

Based on a complaint, we audited an 8(a) BD firm to determine whether it could be viewed as a potential front; i.e., a disadvantaged firm that allows a non-disadvantaged company to perform its 8(a) BD requirements. We reviewed documents relating to seven 8(a) BD contracts the company received from December 17, 2002 to May 26, 2004. The seven contracts were the seven largest dollar value 8(a) BD contracts the company received. [FOIA Ex. 7(A) and 7(D)]. We interviewed the owner and the former vice president of the company, company subcontractors, the procuring agency’s contracting officers, and SBA officials.

Audit work was conducted in Washington, D.C. from March 2005 to October 2005. The audit was conducted in accordance with generally accepted Government Auditing Standards.

## AUDIT RESULTS

### **Finding 1: Neither SBA nor Procuring Agencies Ensured that 8(a) BD Companies Complied with Applicable Regulations when Completing 8(a) BD Contracts**

While SBA delegated 8(a) BD contract execution authority to 26 procuring agencies, there's no evidence to support that SBA performed any surveillance reviews to ensure that these agencies effectively monitored companies for compliance with 8(a) BD regulations when they completed 8(a) BD contracts. Neither SBA nor procuring agencies monitored these contracts during contract execution to ensure companies were complying with these regulations. Procuring agencies did not establish guidelines or procedures to monitor adherence to these regulations after contract award. As a result, companies could violate 8(a) BD regulations and government officials would be unaware of the violations. Our review showed that a company appears to have violated various significant regulations on various 8(a) BD contracts, and neither the procuring agency nor SBA was aware of the apparent violations.

Though SBA delegated 8(a) BD contract execution authority to 26 procuring agencies, SBA did not ensure that procuring agencies monitored whether companies complied with 8(a) BD regulations when completing 8(a) BD contracts. It does not appear that SBA performed any surveillance reviews to determine, in part, whether procuring agencies were ensuring compliance with these regulations. Further, neither SBA nor procuring agencies monitored whether the companies complied with these regulations when completing contracts. None of the 23 procuring agencies that we contacted had procedures or other guidance that would detect if companies were not complying with these regulations. SBA does not directly monitor individual 8(a) BD contracts. While SBA could get involved in these issues if notified by the procuring agency, this has not occurred.

As the prime contractor, SBA has ultimate responsibility for ensuring that companies comply with 8(a) BD regulations. Each participation agreement states that:

SBA only delegates the authority to sign contracts on its behalf. SBA remains the prime contractor on all 8(a) BD contracts . . . and shall retain the responsibility for compliance with all applicable provisions of 13 C.F.R. Part 124 . . . .

According to each partnership agreement, the procuring agency “shall retain responsibility for compliance with all applicable provisions of the FAR and any (agency) regulations . . . .” The FAR includes the 8(a) BD regulations which

8(a) BD companies must comply with when completing 8(a) BD contracts. The partnership agreements do not provide any details on how the procuring agencies should ensure the 8(a) BD companies are in compliance. Neither the procuring agencies nor SBA have developed and distributed guidance on what the procuring agencies should be reviewing and how they should be monitoring.

According to each partnership agreement, SBA “shall retain the right to perform on-site contract surveillance reviews . . .” at the procuring agencies. According to SOP 80 05 3, “the Assistant District Director for 8(a) BD (ADD/8(a)BD) is responsible for selecting procuring activities to review in locations covered by his or her District Office (DO).” According to SOP 80 05 3, the Assistant District Director for 8(a) BD performs the 8(a) review, the District Director signs the final report from this review and the District Office sends a copy to the Assistant Administrator for the Office of Program Review within the 8(a) BD program.

SBA will conduct reviews at the procuring agencies to ensure, among other things, that procuring activities have followed the proper procedures in executing 8(a) contracts. The SOP stipulates that SBA has the authority to take back this delegated authority if the agency routinely abuses the authority of the partnership agreement. The partnership agreements, however, do not state any specific reasons why SBA may terminate the agreement and take back the delegated authority.

The partnership agreements do not specifically detail all the parts of the FAR dealing with 8(a) BD contract requirements that should be followed. Contracting Officers and their technical representatives only know that they are responsible for all FAR stipulations. Notwithstanding this stipulation, none of the 8(a) contracts we reviewed had been monitored. While the participation agreements state that SBA delegates contract execution to the procuring agencies, it does not specifically state that the procuring agencies are responsible for enforcing the 8(a) BD regulations, allowing for possible misinterpretation of SBA’s meaning. Since SBA believes that it has delegated its authority to monitor company compliance with all contract and FAR requirements, including Limitation on Subcontracting, on individual contracts to the procuring agencies, it does not monitor company compliance on individual contracts.

It does not appear that SBA conducted any surveillance reviews to determine whether procuring agencies are effectively monitoring for 8(a) BD regulation compliance. Neither the 8(a) BD program nor the Office of Field Operations could identify any completed surveillance reviews. The Deputy Associate Deputy Administrator for Government Contracting and Business Development could not explain why these reviews had not been conducted. Officials in the Office of Field Operations stated that they will take appropriate action to ensure that the reviews are done.

Since Federal officials were not monitoring 8(a) BD companies’ compliance with 8(a) BD regulations, companies could violate these regulations and government officials would be unaware of the violations. When companies violate these regulations, it

undermines the integrity of the 8(a) BD program and hinders the company from ultimately being able to compete in the mainstream of the American economy.

At one of the reviewed 23 procuring agencies, we assessed whether a company was complying with 8(a) BD regulations when completing 8(a) BD contracts. The company appeared to have violated significant regulations on all seven contracts we reviewed. [FOIA Ex. 7(A) and 7(D)]. The 13 contracts had a combined value of \$2 million. Specifically:

- It appears that the company subcontracted out 100 percent of the work on all 13 contracts. This violates the regulations which require the company to perform at least 15 percent of each contract's labor costs with its own employees.
- On some of these contracts, the company appears to have been unduly dependent on the subcontractors as the company could not perform essential portions of the contract with its own employees, e.g., electrical work on an electrical contract. As such, it would not have provided significant resources and experience to the contract. Nor did the company have a joint venture agreement on any of these contracts. Companies must have a joint venture agreement approved by SBA when working closely together to complete an 8(a) BD contract. SBA cannot approve the joint venture agreement if the 8(a) BD company cannot provide sufficient evidence that it will contribute significant resources and experience to complete its portion of the contract.
- The company appears to have falsified payroll records it submitted to the procuring agency in connection with six contracts. The submitted payroll included individuals who were also included as employees on sub-contractors payrolls, [FOIA Ex. 7(D)].
- The company did not meet the requirements to perform out of state contracts, in violation of Section 8(a) (11) of the Small Business Act (15 U.S.C. § 637(a) (11)) which provides that, to the maximum extent practicable, 8(a) BD construction requirements should be awarded within the county or State where the work is to be performed.

Since the agency did not monitor this company for compliance with 8(a) BD regulations, it did not detect any of these possible violations. [FOIA Ex. 7(A)].

SBA was not aware that the 23 major procuring agencies failed to monitor 8(a) BD compliance and in fact, that they had no requirements for such monitoring. Due to the lack of monitoring, there was little likelihood that the procuring agencies would know if companies were out of compliance so that they could take appropriate action. As a result, the integrity of the 8(a) BD program may be compromised.

## **Recommendations**

We recommend that the Associate Deputy Administrator for Government Contracting and Business Development:

- 1A. Revise the partnership agreements so that procuring agencies are specifically required to (1) monitor 8(a) BD companies compliance with specified contract and FAR requirements, and 8(a) BD regulations, (2) inform contracting officers and technical representatives of their responsibilities concerning 8(a) compliance, and (3) acknowledge that SBA can take back the delegated authority if it does not adequately monitor 8(a) BD company compliance with 8(a) BD regulations.

We recommend that the Associate Administrator for Field Operations:

- 1B. Ensure that surveillance reviews of procuring agencies are conducted on a regular basis. These surveillance reviews should ensure that procuring agencies are effectively monitoring for and enforcing compliance with specified 8(a) BD regulations on the contracts they administer.

## **SBA MANAGEMENT'S COMMENTS**

The Associate Deputy Administrator for Government Contracting and Business Development and Associate Administrator for Field Operations stated that they agreed with the recommendations in the report (See Attachments 1 and 2).

\* \* \* \* \*

The findings included in this report are the conclusions of the Office of Inspector General's Auditing Division. The findings and recommendations are subject to review, management decision, and corrective action by your office in accordance with existing Agency procedures for audit follow-up and resolution.

Please provide us your management decision for each recommendation within 30 days. Your management decisions should be recorded on the attached SBA Forms 1824, "Recommendation Action Sheet," and show either your proposed corrective action and target date for completion, or explanation of your disagreement with our recommendations.

Should you or your staff have any questions, please contact Robert G. Hultberg, Director, Business Development Programs Group at (202) 205-[FOIA Ex. 2].

Attachments

Attachment 1



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

DATE: March 10, 2006

TO: Robert Scabrooks  
Assistant Inspector General for Auditing

THRU: Sheila D. Thomas  
Acting Associate Administrator for Business Development

FROM: Anthony Martoccia ] FOIA EX 6  
Associate Deputy Administrator for  
Government Contracting and Business Development

SUBJECT: Response to Draft Audit Of Monitoring Compliance With 8(a)  
Regulations During 8(a) BD Contract Performance

CC: Calvin Jenkins, Deputy Associate Deputy Administrator, GC/BD

The Office of Government Contracting and Business Development have reviewed the draft audit entitled "Audit Of Monitoring Compliance With 8(a) Regulations During 8(a) BD Contract Performance and acknowledge the suggested revisions that has been incorporated into this draft audit.

At this time, the Office of Government Contracting and Business Development agrees with the draft audit findings and recommendations and have no further comments.

Thank you for your support.

Attachment 2



U.S. SMALL BUSINESS ADMINISTRATION  
WASHINGTON, D.C. 20415

DATE: March 14, 2006

FROM: Michael J. Pappas [FOIA Ex 6] ]  
 Associate Administrator  
 Office of Field Operations

TO: Robert G. Scabrooks  
 Assistant Inspector General for Auditing

SUBJECT: Audit Of Monitoring Compliance With 8(a) BD Regulations During 8(a)  
 BD Contract Performance

The Office of Field Operations (OFO) does not dispute the findings in your draft report "Audit Of Monitoring Compliance With 8(a) BD Regulations During 8(a) BD Contract Performance". We have reviewed the document and met with OIG staff to discuss the report. OFO agrees that our office will be responsible for taking such action to ensure the reviews are conducted on a regular basis as recommended in the draft audit report dated February 23, 2006.

Any questions may be directed to Stephen Umberger, Field Operations Specialist via e-mail, or by phone at (202) 205-4 [FOIA Ex 2]

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