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The Office of Minority Business Enterprise (OMBE) was established to be the focus of Federal efforts to help establish and expand minority businesses. However, OMBE's management assistance program provided few benefits to the 344 minority and prospective minority businesses sampled. Only 25% of the 169 prospective businesses got enough help to start, and about 37% of the existing businesses helped were out of business or could not be located. Findings/Conclusions: The Office has emphasized quantity rather than quality assistance, causing such deficiencies as: business plans not being prepared for about two-thirds of the cases, management assistance not being given to about one-third of the cases, and cases receiving assistance getting only portions of the comprehensive program. Contractors generally do not provide assistance according to OMBE criteria and have not followed their clients' progress after initial assistance. Recommendations: The Secretary of Commerce should require the Director of OMBE to: redirect the management assistance program to encourage contractors to provide a comprehensive assistance program to only as many clients as the contractors can assist over a long-term period; require contractors to obtain periodic financial statements from their clients; require that each serious client's business weaknesses and needs be analyzed in a formal business plan; assure that contractors provide clients sufficient management assistance to meet their needs; assure that contractors follow their clients' progress frequently to evaluate growth and identify problems; restructure the time-phase plan so that primary emphasis in OMBE's evaluation process is placed on meeting program objectives and secondary emphasis placed on activity levels; direct contractors to stop abandoning clients at the first indication that clients cannot qualify for financial assistance; direct contractors to exhaust all alternatives in helping clients locate equity and other resources needed to finance

businesses; and study the possibility of freeing regional program officers from their heavy contract-administration workload. (Author/SC)

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REPORT TO THE CONGRESS

*BY THE COMPTROLLER GENERAL
OF THE UNITED STATES*

The Office Of Minority Business Enterprise Could Do More To Start And Maintain Minority Businesses

The Office of Minority Business Enterprise's management assistance program provided few benefits to the 344 minority and prospective minority businesses sampled. Only 25 of the 169 prospective businesses got enough help to start. About 37 percent of the existing businesses helped by the Office were out of business or could not be located.

To minority owners and those wanting to start businesses, the ability to get financial assistance can make the difference between success and failure. Only 47 of the 221 minority and prospective minority businesses (21 percent) got needed financial assistance.



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

B-149685

To the President of the Senate and the
Speaker of the House of Representatives

This report shows that minority and prospective minority businesses received marginal benefits from the Office of Minority Business Enterprise's management assistance program. The report contains several recommendations to improve the Office's efforts to start and maintain minority businesses.

We made our review pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67).

Copies of this report are being sent to the Acting Director, Office of Management and Budget, and to the Secretary of Commerce.

ACTING


Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

THE OFFICE OF MINORITY
BUSINESS ENTERPRISE
COULD DO MORE TO START
AND MAINTAIN MINORITY
BUSINESSES

D I G E S T

Most of the 344 minority and prospective minority businesses sampled received marginal benefits from the Office of Minority Business Enterprise's management assistance program. The program finances management assistance from private or public contractors for minority businesses.

Of 169 prospective minority business owners, only 25 received enough assistance to start new businesses. About 37 percent of the minority businesses assisted by the agency's contractors in maintaining their businesses were out of business or could not be located. Further, GAO had difficulty evaluating the quality of assistance provided because contractors' records generally did not contain enough financial data.

One factor that may cause business success is the ability to get financial assistance. Office of Minority Business Enterprise contractors helped clients meet their needs only 21 percent of the time. (See pp. 21 and 22.)

Although the program appears well designed, the Office has emphasized quantity rather than quality assistance, causing many deficiencies, including

- business plans not being prepared for about two-thirds of the cases,
- management assistance not being given to about one-third of the cases, and
- those cases receiving assistance getting only portions of the comprehensive program the Office intended. (See pp. 10, 12, and 16.)

Contractors generally are not providing assistance according to Office criteria and have not followed their clients' progress after initial assistance. (See p. 14.)

The Office does not adequately evaluate the management assistance program's effect nor does it adequately monitor contractors. As a result, data is generally unavailable. Because of this, the Office measures contractor progress and effectiveness by comparing assistance provided against preestablished goals. (See pp. 26 to 38.)

To correct these problems, the Secretary of Commerce should require the Director, Office of Minority Business Enterprise, to take several actions, as listed on pages 19, 20, 25, and 38.

The Director, Office of Minority Business Enterprise, said that although the Office has some reservations about a few findings, the report was essentially accurate, well balanced, and realistic. He added that the report's overall tenor and specifics are consistent with the Office's recent program evaluations. Together, this GAO report and the Office evaluations will help the Office improve program management. (See pp. 20, 25, 29 to 31, and 38.)

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ABBREVIATIONS

CCAC	construction-contractor assistance center
GAO	General Accounting Office
LBDO	local business-development organization
OMB	Office of Management and Budget
OMBE	Office of Minority Business Enterprise
SBA	Small Business Administration

CHAPTER 1

INTRODUCTION

Concern over the disproportionately small number of businesses owned by minorities has caused the Federal Government to emphasize assisting minorities to become business owners in recent years.

A lacking business tradition, inadequate financial and management resources, language barriers, and racial discrimination are factors that limit opportunities for minority business ownership.

OFFICE OF MINORITY BUSINESS ENTERPRISE

The Office of Minority Business Enterprise (OMBE) was established within the Department of Commerce by Executive Order 11458 (Mar. 5, 1969). OMBE was to be the focus of Federal efforts to help establish and expand minority businesses. OMBE's responsibilities at that time were to

- coordinate Federal plans, programs, and operations that affect minority business;
- stimulate State and local governments and private institutions to aid minority business growth; and
- develop and disseminate information for those who would assist or engage in minority business development.

Management assistance program

OMBE's responsibilities were significantly expanded in October 1971. Executive Order 11625 superseded the first Executive order and redefined and expanded OMBE's authority and responsibilities. The primary change authorized OMBE to provide financial assistance to public and private organizations that would render management and technical assistance to minority business enterprises.

Under this order, OMBE established a nationwide delivery system of management assistance organizations (via contractors). These contractors are to provide information on resources (such as capital, market opportunities, education, and training) and services (such as information, counseling, specialized technical aid, and loan packaging) that are

required to assist minority business. These contractors are nonprofit and most rely on OMBE for all funding.

OMBE began funding contractors in February 1972. Contracts are awarded on a direct sole-source basis; although awards are sometimes made competitively. They can be renewed upon expiration.

OMBE also enters into grant agreements with States to provide State and local OMBE investment and develop procurement opportunities.

OMBE has reported that significant gains in the national minority enterprise program have occurred because of its coordination and promotion. OMBE has also reported that its contractors have annually increased the number and value of services provided. A selection of OMBE's reported accomplishments is contained in appendix III; we discuss weaknesses in OMBE's method of judging success beginning on page 36.

OMBE received modest funding (1 to 2 million dollars annually) during its first 2 years--when its functions were solely coordination and promotion. To implement its increased responsibility under Executive Order 11625, OMBE was given a \$40 million supplemental appropriation in December 1971. OMBE's appropriations since its beginning in 1969 through fiscal year 1976 totaled about \$248 million. Since fiscal year 1972 OMBE's annual appropriation has ranged from about \$36 million to about \$64 million.

OMBE estimates that funds obligated to management assistance contractors amounted to about \$156 million from fiscal year 1972 through fiscal year 1975. Appendix IV lists contractor types and appendix V shows funding by contractor type.

OMBE'S ORGANIZATION

OMBE began as a centralized organization in Washington, D.C. When OMBE began funding its business assistance contractors in fiscal year 1972, about 28 field representatives were placed in major cities to coordinate and monitor OMBE field activities.

In a July 30, 1973, report, OMBE reported that one of its task forces had found that OMBE contractors were not adequately monitored. As a result, after 4 years of centralization OMBE reorganized in October 1973 and established regional offices in New York City; Washington, D.C.; Atlanta;

Chicago; Dallas; and San Francisco. (App. VI shows a map of OMBE regions.) One decentralization goal was to establish closer communication, coordination, and evaluation procedures with contractors.

OTHER EVALUATIONS

The surveys and investigations staff of the House Appropriations Committee reviewed OMBE operations and presented its findings to the Committee in a March 10, 1975 report. The report comments on OMBE's management assistance program. The Office of Management and Budget (OMB), in cooperation with Commerce and the Small Business Administration (SBA), also reported on the progress of Federal minority business development programs in a March 1976 report. OMB commented on general problems with the Federal effort and on the relationship between OMBE and SBA.

CHAPTER 2

MINORITY BUSINESSES RECEIVED LITTLE

BENEFIT FROM OMBE'S MANAGEMENT ASSISTANCE

OMBE's assistance program should be improved to give minority entrepreneurs the assistance they need to start, expand, and maintain businesses. OMBE has had only limited success in assisting clients start businesses and was not very successful in helping clients maintain businesses.

Generally, OMBE's contractors did not provide the amount and frequency of management assistance needed by minority clients. The contractors generally were not familiar with their clients' indepth needs, had no plans for providing assistance, and did not keep track of clients after initial assistance was provided. The contractors argued that they generally did not have the time or resources to give clients a comprehensive assistance program because OMBE emphasized serving a large number of clients.

CONTRACTORS' RECORDS NOT ALWAYS COMPLETE

We encountered problems which limited the degree that OMBE's management assistance program could be evaluated. Contractors' record reviews coupled with contractor personnel interviews generally allowed determination of what had happened to contractors' clients in broad terms. However, the records often lacked certain specific data.

For example, contractors generally did not follow their clients' progress after initial assistance was provided and did not obtain periodic information about the clients' financial status. As a result, it could not be determined whether clients were succeeding (expanding) or whether they were failing (deteriorating).

In addition, contractor records did not always show such information as:

- What was wrong with clients' business proposals. When noted, deficiencies were often superficial. Therefore, it could not be determined if contractors had given their clients needed assistance or had made genuine attempts to help clients obtain financing needed to start, save, or expand businesses.

--The nature of clients' management weaknesses and needs or the hours of management assistance given. Therefore, what management assistance had been needed could not be compared with what had been provided. Also, the quantity of services provided could not be analyzed.

Generally, the records did not demonstrate that the contractors provided the assistance they reported to OMBE.

FEW BUSINESSES BENEFITED FROM OMBE'S PROGRAM.

OMBE has defined the problem it is trying to alleviate as follows. According to OMBE, in 1969 about 35 million Americans (17 percent of the U.S. population) were black, Spanish surnamed, Indian, Aleutian, or Asian. Yet they owned only about 4 percent of U.S. businesses and accounted for less than 1 percent of U.S. gross business receipts. OMBE has reported that equity is scarce and management capability essential to business success is frequently lacking. OMBE's philosophy is that given equal access to capital resources, management and technical assistance, procurement and market opportunities, and business education, minority businesses should have a good chance to succeed.

OMBE's contractors should provide management and technical assistance to minority business owners to help them start, maintain, and expand businesses and generally foster significant minority business success and profits.

To evaluate contractor efforts in achieving these objectives, we examined the assistance given to 376 clients selected randomly from a universe of 4,996 clients of 17 contractors. It was found that 32 individuals should not have been classified by contractors as clients or otherwise had to be deleted from our study because:

- The individuals lacked serious motives (for example, some were simply seeking information).
- The individuals had been referred to non-OMBE sources for assistance.
- The contractor could not locate the client's file.
- Contractors miscalculated the number of clients.

This chapter concerns the sample's 344 remaining clients. Of these 344 clients, 169 (49 percent) were not

in business when they approached OMBE; the remaining 175 clients (51 percent) were in business.

Contractors helped 25 (15 percent) of the 169 clients start businesses. The remaining 144 clients did not start a business while in OMBE's program. After leaving the program, 4 of the 144 clients started businesses on their own. Of these four, three clients had not been assisted; the remaining client was given management assistance. Three of the four clients were contacted and they said they had succeeded through their own efforts.

Since 175 clients were in business when they approached OMBE and another 25 clients started business with OMBE's help, 200 clients were in business at some time during this review. We examined these clients' records to determine (1) how many successfully expanded their businesses and (2) how many successfully maintained their businesses (e.g., did not go out of business).

OMBE stated that the final program test must be measured by sales, profits, and jobs created. However, the clients' business expansion could not be determined because contractors' records generally did not show clients' financial status. OMBE suggested to some contractors and required that others obtain clients' financial statements to measure financial milestones, but contractors failed to do this. (See p. 14 for further discussion.) As a result, a large gap exists in the information needed for program results evaluation.

We were able to determine the number of clients that maintained their businesses by reviewing contractor records and interviewing clients. We found that 26 of 200 clients in operation had failed; we could not locate 44 clients.

We attempted, and requested that contractors attempt, to contact the 44 clients. Since these businesses left no new telephone numbers or forwarding addresses, we assumed that they went out of business and the contractors agreed. Why the clients went out of business could not be determined.

In total, 70 (26 failures plus 44 not located) of 200 clients in operation apparently did not maintain their businesses, yielding an apparent net loss of 70 clients. 1/

1/The 70-clients figure comes from 6 of the 25 that started new businesses and 64 of the 175 that wanted to expand their businesses.

This analysis contains an unknown degree of error primarily because assumptions were made about uncontacted clients. But it demonstrates that serious problems exist in OMBE's management assistance program. For example:

--There is a serious lack of information about what has happened to clients still in operation. As will be discussed, one reason this happens is that contractors are not following their clients' progress after initial assistance is provided.

--OMBE's assistance program does not appear to appreciably affect OMBE's program objective of closing the gap between the minority population/business ownership ratio.

PROGRAM CONCEPT

OMBE's contractors should provide clients a complete, comprehensive management and technical assistance program. The need for such a program was discussed by the President's Advisory Council for Minority Enterprise ^{1/} in June 1971; minority to nonminority business was compared in its report on the national minority enterprise program. The Council stated that:

"* * * the health of minority businesses tends to be more precarious due to extensive managerial and technical deficits characteristic of minority entrepreneurs."

The Council characterized these deficits as generally stemming from a lack of formal business training or a business tradition, undercapitalization, failure to find meaningful managerial employment, little or no money for necessary assistance, and unavailability of self-help aids for developing business skills.

OMBE responded to the needs cited in this report by designing a management assistance program to assist minority businesses with any problems their business might have. For example, its December 1972 contractor guidelines stated that:

^{1/} The Council was established by Executive Order 11458, which also established OMBE.

"OMBE's new program * * * seeks to make available locally * * * the resources--capital, market opportunities, education, training--and the assistance services--information, counseling, specialized technical aid, loan packaging, etc.--required by minority businesses."

OMBE designed its assistance program around several different types of organizations. Local business-development organizations and construction-contractor assistance centers are the primary contact for minority businesses needing assistance, and should provide a complete assistance program. Other contractors should provide specialized assistance or assist specific target groups. Appendix IV lists contractor types and describes contractor relationships in more detail.

Combined, this contractor mix is designed to provide or assist minority business with obtaining the total resources and other assistance services needed to start and expand business. The local business-development organizations and the construction-contractor assistance centers, for example, should.

- Make the program known to as many minority business owners as possible.
- Screen prospective clients to identify immediate needs.
- Prepare a business plan that analyzes the clients' immediate (within the first year) needs and long-range needs; after that, identify the assistance necessary to meet those needs, project sales and expenses, and describe markets.
- Provide management assistance in accordance with the business plan and clients' needs.
- Follow the client's progress for at least 2 years to determine whether milestones are being met and whether new assistance is needed to assure that the business remains a viable and growing enterprise.

Business plans

OMBE guidelines provide that preparing business plans should enable contractors to (1) determine whether clients' plans are feasible and (2) formulate a program to meet those

needs. OMBE stated that clients, in assembling viable businesses, might include the following in the business plans:

- Market study: Provides an analysis of sales volume and a preliminary answer to the question: Is the business feasible?
- Sales projection: Summarizes potential sales and expenses and helps determine whether profits can be achieved.
- Technical and operational plan: Sets forth a course of action for the contractor and the business.
- Financial analysis: Pulls all the above data together to answer the question: Can the business succeed financially?

If the business is determined feasible, the contractor should assist the client in assembling required resources, including, if necessary, preparation of loan packages or other financial proposals.

OMBE has not established criteria which tell contractors when clients should have business plans prepared. Each contractor must decide on its own. OMBE's guidelines state only that local business-development organizations and construction-contractor assistance centers (primary contact point) contractors:

"* * * shall * * * assist business candidates to develop and implement, as appropriate, comprehensive business plans for the creation of new business ventures or the improvement of existing businesses * * *" and
"* * * will help clients to develop their detailed business plans * * *." (Underscoring supplied.)

Other contractor types are not required to work from a business plan in providing client assistance. Presumably, clients are to be referred to local business-development organizations or construction-contractor assistance centers if clients need business plans.

Management assistance

The contractors should have the necessary technical and professional resources to provide a complete management assistance program. Assistance can include areas such as marketing, accounting, management, and finance.

Followup

OMBE considers followup extremely important. OMBE guidelines specify for some types of contractors and suggest for others that contractors obtain at least monthly business and financial information and use that information to analyze businesses' financial status and health. The contractor should determine if management assistance is needed to prevent significant problems from arising in the client's business and assure its survival and growth. OMBE's guidelines stress the need to provide continual assistance until the business can operate profitably without Federal assistance.

In a memorandum to his contractors one OMBE regional director stated:

"* * * it is imperative that the BDO [local business development organization] have a [followup] system which guarantees that the client will avoid the pitfalls and errors in judgment that normally create serious difficulties * * * for inexperienced business owners and managers."

BUSINESS PLANS USUALLY NOT PREPARED

Contractors for two-thirds of their clients did not prepare business plans and those prepared were usually incomplete, as shown below:

<u>Client objectives</u>	<u>Total</u>	<u>Plan prepared</u>	<u>Percent of prepared plans in total</u>	<u>Plan not prepared</u>
To start business	169	58	34	111
To expand business	<u>175</u>	<u>59</u>	34	<u>116</u>
Total	<u>344</u>	<u>117</u>	34	<u>227</u>

Clients that had business plans had a significantly greater chance of starting a business. Contractors prepared plans for 21 of 25 clients who started businesses (84 percent) but contractors prepared plans for only 37 of 144 perspective business owners not starting businesses (26 percent).

Business plans were not so important for 175 clients who wanted to expand their businesses. Contractors prepared plans for 41 of 111 clients still in business (38 percent)

and for 18 of 64 clients who went out of business or could not be located (28 percent). 1/ While the percentages are not high, business plans gave clients a slightly greater chance of staying in business.

We believe contractors would have better success in assisting clients if they prepared business plans that list the business' serious weaknesses and needs. Also, plans would remind contractors to follow their clients' progress.

Plans usually incomplete when prepared

Contractors prepared business plans for 117 clients. These plans were normally developed for preparation of loan application packages and were aimed at helping clients obtain financing.

Loan-package business plans accounted for 99 of 117 plans. Contractors, in developing information for loan packages, were required to assemble much of the material that would be used for a business plan. For example, banks and SBA required that loan packages generally contain some type of market study, sales projection, and financial analysis. Because these packages represented a benefit to the client, we accepted them as business plans.

The problem with these plans is that they were designed to "sell" the client by presenting the most favorable financial and business information.

However, the 99 loan-package business plans are missing an indepth analysis of management weaknesses and needs. For example, OMBE's guidelines call for complete business plans as part of the process to assemble viable businesses. SBA also greatly stresses business plans. SBA advises small businessmen to prepare and use a business plan as a profitability guide. SBA states that plans must be complete because items not planned for will create additional costs and if enough items are left out the business is headed for disaster. These incomplete plans illustrate the one-time nature of OMBE's assistance program; contractors do not seem concerned about their clients' long-term growth and success.

1/The analysis in this paragraph does not include six clients who started businesses and subsequently went out of business or could not be located.

The 18 remaining plans generally met OMBE's guidelines for business plans, although 6 were obviously slanted toward special-purpose analysis such as feasibility marketing and site selection studies. Only two plans seemed complete enough to meet the spirit and intent of SBA's criteria.

These inadequacies in the business-planning process caused contractors' records to not contain complete or consistent information about their clients' management weaknesses or needs. As a result, the relationship between the management assistance needed and that which was given could not be analyzed.

MANAGEMENT ASSISTANCE NOT GIVEN TO ALL CLIENTS

Contractors did not give management assistance to 127 of 344 (37 percent) clients; assistance was given to 217 (63 percent) clients. Clients that received management assistance were more likely to start or stay in business than clients that did not.

For new businesses, contractors assisted 15 (60 percent) of 25 clients that were successful in starting businesses, but only 69 (48 percent) of 144 clients who attempted but did not start businesses. Thus, clients who received management assistance had a slightly greater chance of starting businesses.

For existing businesses, contractors assisted 87 (78 percent) of 111 clients who had and were able to maintain their businesses but only 46 (72 percent) of 64 clients that failed or could not be located. While the difference is small, it still indicates that improvement in assisting clients might increase the clients' ability to stay in business.

We also determined how many types of management assistance had been given to each client and whether the assistance had been concentrated at initial contact.

As discussed earlier, contractors usually did not record the number of hours of management assistance that had been provided to clients or what had transpired when assistance was given. Documentation was usually only an OMBE reporting form noting the type of assistance. As a result, the amount of assistance provided per client could not be determined.

The types of assistance given each client and whether assistance was given for a short period or continuously

over a longer period could not be determined. Clients were generally given only one or two types of assistance. Assistance was concentrated around initial contact between contractor and client and very little followup assistance was provided.

Only a few types of assistance provided

Contractors should be able to provide a wide range of management assistance to meet client needs. However, as shown below most clients were given only one or two types of assistance.

<u>Client status</u>	<u>Total</u>	<u>One type</u>	<u>Two types</u>	<u>Three types</u>	<u>Four or more types</u>
New business	84	50	15	13	6
Existing business	<u>133</u>	<u>75</u>	<u>35</u>	<u>11</u>	<u>12</u>
Total	<u>217</u>	<u>125</u>	<u>50</u>	<u>24</u>	<u>18</u>

Appendix VII shows the frequency of each type of assistance given.

Of the 217 clients given management assistance, 125 (58 percent) were given only one type of assistance. Such a narrow range of assistance does not coincide with OMBE's announced intention of providing clients a complete, comprehensive management assistance program. This narrowness of assistance may be one reason why the management assistance that was given was not enough to help clients start or stay in business.

Assistance not given on a continuing basis

OMBE stated that continuous management assistance should be made available to clients to assure that their businesses remain viable and growing enterprises. We analyzed the number of months between the time persons first became clients and the last date they had received management assistance. This data was available for 117 of 133 clients in business given management assistance.

Assistance to 34 (29 percent) of 117 clients was completed in the same month they became clients. Assistance to 12 others was completed by the end of their second month and to 11 more within 3 months. Thus, these contractors apparently considered that 57 clients (about one-half of

the 117 clients) could operate profitably without special assistance within 3 months after they became clients. Another 24 clients received all their management assistance within 6 months after becoming clients.

CLIENTS' PROGRESS NOT FOLLOWED

After providing initial assistance, contactors did not normally follow their clients' progress and clients were usually left on their own. We believe contractors need to utilize systematic procedures for determining when their clients are encountering severe problems.

Contractors attempted to follow only 21 of the 200 clients in business. These attempts were sporadic and generally did not result in any followup assistance. Only 1 of the 21 attempted contacts was directed toward the 70 clients that had failed or could not be located. Obviously, many of these clients encountered severe business problems that led to their failure. Without following clients' progress, it is doubtful that contractors would be aware that these businesses were troubled and needed assistance.

Financial statements not obtained

Contractors could follow clients' progress by obtaining periodic financial statements. Statement analysis would show general business trends and financial progress and might warn of business problems.

OMBE's guidelines state that local business-development organizations should obtain the necessary business and financial information to determine the business health from each client at least once a month. Construction-contractor assistance centers are also required to obtain annual financial statements for clients assisted in starting, saving, or expanding a business in order to evaluate the clients' effectiveness. However, only 4 of 344 files contained statements showing clients' progress.

Contractors apparently were not seriously trying to obtain periodic financial statements. Contractor officials said that it was very difficult to obtain statements because:

- Contractors do not have the leverage to require clients to submit statements.

- Clients are often incapable of preparing such statements or do not have the time or motivation to do so.
- Clients hesitate to prepare statements for fear they will disclose discrepancies in their tax returns.

However, 57 of the 118 clients contacted were asked whether they had prepared financial statements. Fifty-three said they did; four said they had not. The clients with statements generally appeared willing to provide them to contractors.

We found no evidence that contractors were seriously trying to persuade clients to submit statements. For example, there was no documentation to indicate that contractors were even requesting that clients submit statements.

OMBE has not clearly defined which clients should be tracked

One reason contractors were not following up on more clients is that OMBE's guidelines on followup are not clear. The guidelines state that "Once a business opens * * * continuous management assistance will be made available to the client * * * ." (Underscoring supplied.)

This criterion can be interpreted in several ways:

- All clients should be tracked, since contractors should try to assist clients wanting to both start and expand businesses. Under this interpretation contractors should have followed up on all 344 clients.
- Only clients in business should be tracked. Under this interpretation contractors would have followed the progress of 200 clients. 1/
- Only clients who received two or more types of management assistance should be tracked. Under this interpretation 92 clients should have been tracked.

1/The 175 clients in business and the 25 that started businesses.

Contractors attempted to follow the progress of only 21 clients (6, 10, and 23 percent of the totals above, respectively). To improve contractor performance, OMBE should

--reemphasize the importance of followup and

--define clearly which clients are to be followed up.

OMBE STRESSES ACTIVITY RATHER THAN PERFORMANCE

OMBE's contractors did not provide clients a comprehensive assistance program because contractors were devoting most of their resources to meeting OMBE's quantitative performance goals. In general, OMBE did not give its contractors the proper incentives to prepare business plans, provide comprehensive management assistance, and follow client progress.

OMBE requires that its contractors prepare time-phase plans to forecast, among other items:

--Client and business totals--the number of clients to be interviewed and assisted.

--Loan packages--the number of business loans to be packaged.

--Financial resource development--the number of loans to be applied for and obtained for clients.

--Management services and technical assistance--the number of clients to be assisted and the amount of assistance to be provided.

--Procurement assistance--the number of bids to be submitted and contracts to be obtained for clients.

--Education and training--the number of training courses and seminars to be provided to clients.

OMBE places primary emphasis on contractors' production levels--the number of clients assisted and the amount of financial assistance obtained--when contracts are being renewed. For example, OMBE has previously expected that most contractors would help clients obtain loans and contracts in an amount totaling 10 times the contractors' contract amounts. OMBE still considers return on investment to be a major factor in evaluating contractors. Evaluation

criteria and regional office goals focus on comparing financial aid obtained for clients with the contractors' funding levels.

OMBE requires that contractors annually prepare overall performance evaluation reports which are to contain, among other items, a comparison of actual performance with the forecasted quantitative performance goals in the time-phase plan. Contractors are given considerable latitude in preparing the annual report and they normally limit reporting to those quantitative goals met. They usually report the number of clients assisted and the amount of financial assistance obtained because OMBE uses these measures in reporting its own accomplishments.

OMBE measures each contractor's success in meeting its goals during the annual refunding (contract renewal) process. Since most contractors are totally funded by OMBE, refunding is paramount.

Sixteen of the 17 contractors visited said that they did not have the time or staff to assist each client fully. They said that they geared their programs to solving specific problems rather than providing comprehensive assistance.

For example, one local business-development organization official said that comprehensive long-term business plans are not prepared for clients because his organization is concerned only with the economic short run. He said that the organization's overall goal is to achieve short-term (annual) objectives specified in the time-phase plan and that his organization is not concerned with long-term successes.

Another contractor, also a local business-development organization, was having trouble meeting goals in the time-phase plan. A contractor official said that OMBE would have to increase his contract's funding level so that additional staff could be hired if the time-phase plan goals were to be met.

A director from a third contractor, another local business-development organization, said that OMBE should direct its contractors to concentrate more on the quality of service provided to clients and less on quantity. He said the needs assessment function, the management assistance, and followup services all need to be intensified, but more staff is needed to do this, especially if the number of clients to be assisted remains at past or current levels.

An official from a fourth contractor said current staffing levels are adequate; however, less attention should be directed toward generating numbers of clients assisted and more concern should be placed on service quality.

An OMBE regional director stated that:

- Contractors were concentrating on areas that weighed heavily in evaluations.
- Contractor failure to prepare comprehensive business plans and provide followup management assistance is a significant weakness since both are necessary for business success.
- A continuing relationship between contractor and client should be established and help should be provided as long as it is needed.
- A monthly reporting system will be used in his region that will focus more on OMBE's overall objective of preserving, expanding, and strengthening minority business.

These comments indicate that contractors know they are spreading their resources too thin but they feel constrained to do so if they are to meet OMBE's expectations and obtain refunding. OMBE's method of setting goals and evaluating performance is at odds with its objective of providing clients a comprehensive assistance program to meet all their needs.

CONCLUSIONS

OMBE's management assistance program has not been carried out in accordance with OMBE's program objectives. More needs to be done to help clients start new businesses and maintain existing businesses. There is a serious lack of information about the financial status of clients in business; this deficiency can be traced to the contractor's failure to obtain periodic financial statements.

OMBE's program design--to assess each client's needs in depth, to provide a comprehensive management assistance program to meet those needs, and follow the client's progress and provide followup assistance when needed--appears to be designed well.

However, contractors were generally not providing clients assistance in accordance with OMBE's criteria. Needs were not analyzed in depth; management assistance was often limited to one or two types and generally was not given after the initial contact period, and very few attempts were made to follow clients' progress.

Contractors should restructure their programs to develop a manageable group of clients and work with those clients until success occurs or until it is obvious that the clients represent hopeless cases. Contractors should be encouraged to accept only as many clients as they can reasonably expect to assist on a long-term period, given contractors' resources. New clients should be a mixture of those in business and those starting new businesses.

To give contractors the incentive to reach such goals and provide such services, OMBE should restructure the time-phase plan. The first and highest priority should be to start, expand, and maintain businesses, and activity levels should play a secondary role. OMBE would have to be prepared to accept lower activity levels with the view that improvements would be made in the number of businesses started and maintained.

RECOMMENDATIONS

We recommend that the Secretary of Commerce require the Director of OMBE to:

- Redirect the management assistance program to encourage contractors to provide a comprehensive assistance program to only as many clients as contractors can assist over a long-term period. Contractors must be convinced that the long-term objective of making minority business more successful is more important than the short-term objective of assisting a large number of clients.
- Require contractors to obtain periodic financial statements from their clients and if necessary make eligibility for participation in OMBE's program contingent on providing such statements.
- Require that each serious client's business weaknesses and needs be analyzed in a formal business plan.

- Assure that contractors provide clients sufficient management assistance to meet their needs. Contractors should provide followup assistance when needed.
- Assure that contractors follow their clients' progress frequently to evaluate growth and identify problems. Clients' financial statements, discussed in the second recommendation, would be an important tool in such a monitoring process. OMBE should also specify in its contractor guidelines criteria for determining which clients are to be monitored.
- Restructure the time-phase plan so that primary emphasis in OMBE's evaluation process is placed on meeting program objectives and secondary emphasis placed on activity levels.

OMBE concurred with our recommendations. It agreed that criteria should be established to call for the preparation of business plans for each client. It acknowledged that plans development would produce a greater number of continuing clients so that each contractor would reach a limit in its ability to accept new clients in a short time.

OMBE agreed with our position that continued assistance must be given if OMBE's services are to have a meaningful effect. It stated that:

"* * * There must be, however, a clear understanding by the Congress and within the Executive of the constraints placed on the eventual availability of OMBE services to new entrants. To put it simply: within existing and anticipated resources, we cannot have it both ways. OMBE can provide longer-range continuing assistance, or it can increase the number of its clients. We have chosen the first course. Thus, OMBE's FY 1978 Budget Request, submitted to the Congress in January, 1977, calls for a sharp reduction in the number of minority firms to receive OMBE assistance in FY 1978."

After we had received its formal comments, OMBE advised us that the Congress did not address OMBE's proposed reduction in the number of minority firms in the appropriation hearings. OMBE's appropriation was approved on August 2, 1977.

CHAPTER 3

FINANCIAL ASSISTANCE--A CONTINUING PROBLEM

Financing was the most important factor influencing clients' success in starting or maintaining a business. More needs to be done to assist clients in acquiring equity and experience so that they can qualify for financing. Beyond that, the problems seem to be beyond OMBE's control.

FINANCIAL ASSISTANCE NEEDS OFTEN NOT MET

A greater number of clients did not start or maintain businesses primarily because they could not qualify for financing. Although to a degree this problem is beyond OMBE's control, OMBE could do more to help clients obtain financing.

While contractors' files did not contain indepth information about client needs, we were generally able to determine when clients needed loans or other financial assistance. About 60 percent of the clients sampled needed financial assistance, but contractors were able to assist the clients only 21 percent of the time, as follows:

Minority Entrepreneurs'

Financial Needs

<u>Client objectives</u>	<u>Total</u>	<u>Needed financing</u>	<u>Loans obtained</u>	<u>Percent of financing obtained</u>
Start business	169	125	17	14
Expand or stay in business	<u>175</u>	<u>96</u>	<u>30</u>	31
Total	<u>344</u>	<u>221</u>	<u>47</u>	21

Contractors' low success rate in helping clients meet financial needs directly affected clients' ability to start businesses. Clients who had their financial needs met had a much better chance of starting businesses; 17 of 25 clients that succeeded in starting businesses needed loans, and all 17 had that need met. Of 144 clients who did not succeed in starting businesses, 108 needed loans--104 did not have their needs met, 3 did not accept their loans once they had been approved, and 1 had a loan pending at the time of our review.

A similar pattern was evident for those clients wanting to stay in business or expand. Of the 111 clients still operating, 62 needed loans and 28 had that need met. Of the 70 clients that failed or could not be located, 34 needed loans but only 2 had that need met.

OMBE's contractors help clients prepare financial application packages (loan packages) and also help them negotiate with lenders.

Contractors helped prepare loan packages for 94 of 221 clients needing financial assistance. Financial institutions approved 51 of the 94 loan packages and rejected 43.

The fact that loan proposals weren't prepared or were rejected when prepared generally indicates that something was wrong with clients' business proposals. Contractors' records did not always show what these deficiencies were, and when they did deficiencies were often superficial. For example, some files contain only statements that the client did not provide data.

Private financial institutions and Federal agencies with financial assistance programs such as SBA (a source of financing for many minority businesses) have certain minimum requirements for obtaining a loan. These requirements are to protect the financial institution by providing reasonable assurance that the borrower will be able to repay the loan. Private lenders (such as banks) typically require that borrowers have a certain amount of equity or collateral. SBA normally requires that participants in its financial program offer security to assure repayment. Lenders also usually require that the borrower have experience and/or expertise in the proposed business.

OMBE has no control over these requirements and cannot require lenders to waive them. OMBE cannot lend money directly but must work through lenders such as SBA and banks.

MORE COULD BE DONE TO ASSIST CLIENTS

OMBE has stated that limiting assistance only to clients with a high potential to succeed in business violates the program's obligation to the Congress and the minority constituency.

Therefore, contractors were not justified in abandoning so many potential business owners. An unknown number of

these clients probably had hopelessly optimistic proposals and could never be competent managers. Many, on the other hand, seemed to need only a few vital resources to be business owners. At the same time they also seemed to possess one vital resource--the desire to start or save a business.

What is needed is increased contractor effort to provide an innovative management and technical assistance program to help clients identify ways of obtaining needed equity and experience. Such efforts might show that:

- Clients did not accurately calculate equity or left out assets that could be properly counted. This could easily occur when clients do not prepare financial statements.
- Clients did not actually need a loan as large as originally proposed.
- A savings program could be instituted, or venture capital solicited, to obtain needed equity.
- Clients could be assisted in obtaining training or employment that would provide any necessary experience and technical expertise.

More direct action must be taken for clients in business who needed loans to survive. For example, contractors must understand clients' problems as early as possible; this involves tracking clients' progress. (Contractors are not doing this--see p. 14.)

LACK OF EQUITY IS A MAJOR PROBLEM

OMBE has reported that one of the largest problems for any new business owner is to find and tap capital sources to establish and operate their business. OMBE went on to say that:

"[The client] must obtain both an adequate amount and a proper mix of equity capital, debt capital and credit. To obtain debt capital--that is, to borrow money--he must have in hand sufficient assets to secure a loan. To accumulate those assets, he requires equity or seed capital--investments in his business. To balance his cash flow during periods when his obligations exceed his receipts, he also needs credit."

Lenders consider both the cost of administering minority business investments and the risk of early loss to be very high, according to OMBE. "Traditionally, they have refused to provide more than a minimum amount of capital, and then only on a short-term, secured basis."

Further, OMBE reported that very little Federal money can be used directly for equity investment. A vehicle with great potential--because it involves pooling of public and private funds--is SBA's 301(d) small business investment company program, designed to provide risk capital and/or long-term subordinated loans to minority firms in return for an equity interest.

In a report to the Congress ^{1/} we said that as of June 30, 1974, 67 301(d) small business investment companies had funds totaling \$42 million, but their investments in minority small businesses totaled only \$17 million (about 33 percent of available funds). Further, equity investments accounted for only 19 percent of total funds available for investment.

In its study of the national minority enterprise program, OMB concluded that the effectiveness of the 301(d) program in providing equity capital needs improvement. OMB recommended that SBA analyze alternative means of improving the program to make more equity capital available to minority firms.

CONCLUSIONS

One primary factor influencing minority business success or failure is financial assistance. If these businesses have their financial needs met the chances of success are great; if not, their chances are poor.

In certain respects, helping clients obtain financing is beyond OMBE's control. However, contractors are too quick to abandon clients when clients apparently cannot qualify for financial assistance. Much more can be done to help clients obtain necessary qualifications.

^{1/}"A Look at How the Small Business Administration Investment Company Program for Assisting Disadvantaged Businessmen Is Working," October 8, 1975, GGD-75-76.

RECOMMENDATION

We recommend that the Secretary of Commerce require the Director of OMBE to direct its contractors to stop abandoning clients at first indication that clients cannot qualify for financial assistance. Instead, OMBE should direct contractors to exhaust all alternatives (such as those listed on p. 23) in helping clients locate equity and other resources needed to finance businesses.

OMBE concurred with our recommendation.

CHAPTER 4

OTHER OBSERVATIONS

In administering its management assistance program, OMBE does not adequately

- evaluate the program's impact on stated objectives,
- monitor contractors' day-to-day performance, and
- report accomplishments.

OMBE IS NOT EVALUATING PROGRAM EFFECTIVENESS

OMBE uses a management-by-objectives system initiated in fiscal year 1974. Under this system OMBE established three major objectives to improve program effectiveness and ultimately provide more substantive assistance to minority businesses:

1. Increase successful minority business ownership by improving OMBE-assisted firms' ability to grow and establish 1,000 additional minority-owned firms with good survival and growth potential either by creating new enterprises or purchasing existing firms.
2. Effectively coordinate and reconcile the goals and budgets of SBA and OMBE to promote and improve services to minority individuals and firms disadvantaged by economic and social conditions.
3. Improve the OMBE program by augmenting a comprehensive network of business-assistance organizations.

One component of the management-by-objectives system is the performance management system, which was designed to provide periodic and timely information on progress toward defined objectives compared to money spent. In an internal report dated December 10, 1975, OMBE reported that some indicators studied in 1971 (when the system was being developed) were gross sales, profits, jobs generated, tax revenues generated, reductions in transfer payments, failure rate data, and a number of standard business ratios. OMBE hoped that this data would help track business success or failure.

However, OMBE reported that it found that it was not practical to collect the data described above in a comprehensive and usable manner because, among other reasons, clients would not give such information to contractors.

OMBE reported that as a result of these problems it fell back on more input-oriented measures that--within the state of the existing art--could be quantified and collected. OMBE reported that it is currently using such measures as loans, contracts, clients assisted, and specific assistance furnished.

OMBE reported that these measures focus primarily on input, not output. OMBE managers can use these measures to evaluate administrative and operational efficiency but the measures are of little value in determining program impact.

OMBE concluded that it did not have a formal evaluation system and did not conduct regular program evaluations of any kind. The report stated that as a result OMBE may know how well a particular project is doing but often cannot determine how well the overall program is doing.

OMBE proposed a new system to give its management staff and project leadership an orderly system for, among other purposes, making decisions on effectiveness on the basis of program and project impact. Under this new system the primary performance measure will be gross business receipts (gross sales). Other measures in the new system are

- numbers of businesses,
- failure rate of businesses,
- trend data on profits and business ratios, and
- procurement awards/contracts obtained as a result of OMBE assistance.

Gross receipts and failure data will be obtained from Dun and Bradstreet for every OMBE-assisted firm. OMBE stated that it would not be possible, with current resources, to obtain reliable profit trend data from all OMBE-assisted businesses. Therefore, OMBE plans to obtain such information on a random-sample basis from a limited number of contractors, provided that the data is submitted to OMBE in aggregate form without mentioning client names.

The use of gross-receipts data to analyze clients' progress can be misleading and can disguise serious problems. A client's gross receipts might increase in a given period and give the impression that the client's business is improving while in reality the client's net income could be decreasing and the business failing. Problems might not be apparent to OMBE until substantial time had elapsed and the client's business had deteriorated past help.

A better measure of client progress would be profits-- OMBE had considered profits as a measure in its old system. The Secretary of Commerce, in a statement given to the Senate Appropriations Subcommittee in October 1971, stated that OMBE is responsible for the long-term effort to develop profitable minority-owned businesses and that: "Profit is what minority business development is all about."

Further, OMBE instructed local business-development organizations and construction-contractor assistance centers to obtain clients' financial information and use it to evaluate clients' progress. As discussed in chapter 2, contractors did not obtain statements.

In its new system, OMBE plans to use profit trend data, apparently to supplement gross-receipts data. OMBE plans to obtain this data from clients on a random-sample basis without identifying clients by name.

As discussed, OMBE abandoned its earlier system because it assumed that clients would not provide financial information. OMBE specified the following reasons for its position:

- To burden contractors with data-gathering efforts during their early development stage was not feasible.
- Small firms traditionally are reluctant to surrender detailed fiscal data to a Federal agency.
- OMBE's contractors had not yet demonstrated their credibility and thus it was difficult to ask clients for financial information.
- Other Federal agencies had not been able to collect data in the depth proposed by OMBE.

These reasons are no longer pertinent; OMBE's contractors should have established their credibility by now. Further,

provide financial statements to contractors. Also, a substantial amount of financial data is already available through other Federal agencies.

OMBE said that it did not have the resources to obtain reliable profit data from such sources as independent certified audit reports and the Internal Revenue Service. It further said that even SBA has had difficulty in securing financial data from its clients.

In a previous review of SBA's 7(a) business loan program, SBA concurred with our recommendation to require the submission to SBA of financial statements by borrowers of both guaranteed and direct loans. ^{1/} It should be noted also that SBA requires the regular submission of financial statements and that it sometimes requires quarterly statements if a loan is to assist a new business. The Farmers Home Administration also requires that loan applicants submit financial statements in its programs.

Although OMBE is correct that no other Federal agency that gives technical assistance to businesses requires the regular submission of profit data, a substantial number of OMBE clients use SBA and other Federal programs that already require the submission of financial data.

Regarding the paperwork problem OMBE cited, no additional burden would be placed on minority businesses since financial statements are prepared anyway since they are generally an important part of the records of most businesses. Furthermore, as stated above a substantial number of OMBE's clients already prepare statements in fulfilling other Federal programs' requirements.

We do not believe the statements OMBE cited from the Senate Select Committee on Small Business report are applicable to the issue since these statements and others in the report address the pros and cons of using net income and business receipts in various statistical analyses of industries. There is no place in the report where the committee said that gross receipts data should be used to analyze the individual business entities' progress and development.

In its March 1976 report on Federal minority-business development programs, OMB also reported that current knowledge of program effects is not adequate to permit the most effective management of the minority enterprise programs. OMB recommended that the Commerce Department and SBA jointly

^{1/}Report to the Congress, "The Small Business Administration Needs to Improve Its 7(a) Loan Program," (GGD-76-24, Feb. 23, 1976).

clients interviewed in our sample that had prepared financial statements appeared willing to give the statements to OMBE. OMBE should make more efforts to obtain clients' financial data, specifically profit data, and use that data to evaluate program effect.

Commenting on our position, OMBE agreed that a gross receipts measure by itself can mislead in certain cases and it would be preferable to use net income. In addition to the reasons mentioned on page 28, OMBE maintains that there are other practical difficulties for using net profits:

- It is virtually impossible to obtain reliable profit data from clients on a regular and ongoing basis.
- No other Federal agency that provides technical assistance to businesses requires the regular submission of profit data.
- Both the Congress and the administration are committed to reducing the paperwork and reporting burden levied on small businesses by the Federal Government.
- The Senate Select Committee on Small Business stated that:

"A composite figure of net income is not as good a measure of outputs for classification within an industry division as is business receipts."

It stated further that:

"Business receipts income is a more reliable classifier of the size and the contribution (to the economy) of an individual business enterprise than net income. This assumption seems to hold whether comparisons are made on a year-to-year basis or on relative standings within its industry divisions at a given point in time."

We continue to believe that profit trend data is the best means of measurement and that OMBE should reassess its position on some of the practical difficulties in using net-profit data. Again we cite the fact that several of the minority businesses contacted generally appeared willing to

- establish useful, quantifiable objectives for the Federal minority enterprise effort;
- improve the knowledge of the most important factors in minority firms' success and, where feasible, measure the effect of Federal assistance on those factors; and
- establish a comprehensive system for evaluating the effect of Federal assistance.

Objectives and measures of this effort should include profit trend data as a primary measure.

Special OMBE effort to evaluate its program

OMBE contracted with ABT Associates, Inc., Cambridge, Massachusetts, to design and implement an evaluation methodology to

- assess the effectiveness of local business-development and construction-contractor assistance center programs and
- suggest changes in policy or administrative approach that might improve program performance.

The study was conducted in three phases:

Phase I--Developed measurement technique and program model.

Phase II--Tested this technique and model using four local business-development organizations in New England. Cost of phases I and II: about \$100,000.

Phase III--Expanded model to measure the effect of the two contractor types nationally. Cost of phase III: about \$185,000.

ABT reported that the two programs demonstrate that costs to support the minority-owned firms are exceeded by their benefits to society. The contractor went on to say that the two contractor types can affect modest short-term improvements in minority business growth and stability, largely through loan packaging and comprehensive support centered on package and procurement.

While this study provides significant information on the activities of the two contractor types, it contains weaknesses that affect the validity of ABT's conclusions.

One of the most serious weaknesses had to do with nonresponse by sample clients. ABT originally intended to survey 690 clients but was able to interview only 447 clients (65 percent of the original sample). According to ABT,

"The businesses were sampled with replacement; if a business could not be surveyed, a firm in the same sector in the same organization was selected randomly from a replacement list."

ABT reported that 243 clients had not been surveyed because they

- could not be located,
- had refused to respond,
- had failed or were not operating,
- had just started or had never existed, or
- had sold their businesses.

ABT replaced 176 clients in its sample and eventually surveyed 623 clients. ABT concluded that this replacement process may have caused a modest upward bias in the operating characteristics of the firms surveyed.

This high nonresponse rate, coupled with ABT's replacement method, actually caused an upward bias that could be substantial. By not sampling clients that had failed, would not respond, and so on, ABT overloaded its sample with successful operating businesses owned by persons who are probably satisfied with the program.

It also appears that ABT omitted significant costs in computing the benefit/cost ratio. In allocating headquarters costs to regional offices, costs for national programs, an advisory council, and program research and development totaling \$1,871,820 (about 31 percent of headquarters costs) were not allocated to the regional offices.

It doesn't appear logical to exclude such costs. For example, why is program research and development less

directly related to the contractors' support than public and congressional affairs, a cost that was allocated?

In addition, in calculating the benefit/cost ratio, it appears that costs are included only for those firms that were successfully assisted. Costs associated with unsuccessful firms, firms excluded from the universe, and costs described above do not appear in the denominator of the benefit/cost ratio.

In summary, the major faults with the ABT study are the high nonresponse rate and the failure to include all costs in the denominator of the benefit/cost ratio calculation. The benefit/cost ratios are probably overstated and this indicates that the two programs may not have a positive benefit/cost ratio. As a result, it appears that the study did not provide OMBE with accurate information about program results.

Neither OMBE nor ABT agreed with our conclusions. Their specific comments are contained in appendixes I and II. However, ABT admits that the conclusion reached in its report, which states without qualification that costs to assist minority firms are exceeded by their benefits to society, is not clearly supported by its analysis.

CONTRACTORS NOT ADEQUATELY MONITORED

OMBE regional offices, and more specifically, project officers are responsible for monitoring contractor performance. OMBE's project officers are responsible for assessing contractor performance and verifying the quality and quantity of assistance provided to clients. The project officers should

- evaluate contractors' narrative reports,
- make onsite visits to contractors, and
- contact clients to verify contractor assistance.

Narrative reports not evaluated

Contractors should submit quarterly narrative reports showing total clients assisted, management assistance provided, loans obtained, new businesses started, and any other items that reflect progress or accomplishments. This data is the same that is put into the performance management system. OMBE's regional offices use the reports to evaluate day-to-day progress and to make annual refunding decisions.

One measure that OMBE often reports and emphasizes is the number of clients enrolled in the program and the number visited. Significant differences exist between these reports and our client count at four contractors. Contractors' narrative reports showed 3,054 clients had been in contractor programs at the time of our review; our count, however, showed that only 1,617 clients were in their programs--a difference of 1,437 clients. These kinds of errors might have materially affected OMBE's perception of contractor performance.

These differences were undetected because project officers did not adequately review the narrative reports and verify them against contractors' records. Written evaluations were usually not prepared, or when prepared were only letters to contractors acknowledging receipt of the report and discussing the extent that the contractor had met its goals in the time-phase plan.

Project officers stated that their primary objective was to generally gage contractors' progress and determine if the time-phase plan goals were being met. A regional project officer said that he did not verify reported data and four others said that they did but could not document their efforts.

Regional offices not visiting contractors

OMBE's regional project officers should visit contractors and contact clients to increase OMBE's knowledge about performance. Contractor visits allow project officers to (1) get a firsthand impression of contractor operations, (2) review contractor records, and (3) give contractors needed information or assistance. OMBE's guidelines do not specify how often visits should be made or what is to take place during the visit. One OMBE regional director said visits should be made at least monthly for most contractors.

For the most part, we could not determine how many or how often monitoring visits were made, because site visit reports were available in only one of the four OMBE regional field offices visited.

These reports, prepared for five randomly selected contractors for the period from June 1974 through June 1975, showed that only 11 monitoring visits had been made; frequency per contractor ranged from 0 to 5 visits.

Project officers would have made 65 visits if they visited each contractor once a month. While we are not necessarily advocating such frequent visits, the frequency shown above is too low to allow project officers to

adequately evaluate contractors' performance and provide assistance.

Clients not contacted

OMBE project officers are required to contact clients to verify contractor reports and records. OMBE guidelines allow each region to determine how this function will be carried out. Only one region had specific guidelines on contacting clients--requiring project officers to sample 10 percent (a minimum of 12) of their clients per month. The project officer is to make at least five onsite visits per month.

The office did not achieve the client-sampling requirements. We examined records prepared by three project officers for a 13-month period and one officer for a 10-month period, covering visits made to five randomly selected contractors. However, we could not determine whether the requirements had been met for 11 of the 49 months involved; sampling requirements were met for only 13 of the remaining 38 months. The regional office's deputy director attributed the sampling shortfall to a lack of emphasis on monitoring and the difficulty project officers had in contacting sample clients.

This last point is particularly bothersome. The fact that clients cannot be contacted is a danger signal indicating that the client's business may have failed or may be failing. This should cause the evaluator to review the contractor program closely to determine if the contractor was (1) aware of the client's plight and (2) had done everything possible to help the client overcome the problems. This might have alerted the project officers to the weaknesses discussed in chapter 2.

Regional office personnel were generally aware that monitoring guidelines and procedures were weak, but they generally had not tried to correct them. One regional director said that efforts were being made to increase monitoring efficiency; another said that the necessity to spend a lot of time on contract administration severely curtails the resources that can be devoted to contractor monitoring. In some cases, officials estimated that 50 percent of the project officer's time is taken up with contract monitoring because it has high priority. One result is that regional offices relied on internal audits to assure that contractors were performing effectively and conforming with contract provisions.

RELIANCE ON INTERNAL AUDIT

The Commerce Department's Office of Audits is required to audit, or allow independent public accountants to audit, OMBE contracts and grants at least once annually (interim audit) and upon contract completion or termination (final audit). Auditors are to examine contractor compliance with contract provisions and effectiveness in meeting OMBE program objectives (program results audit). The program results work is to include a determination of (1) the reliability of contractor-reported data and (2) the quality of assistance provided. The required interim or final audits had been done at all 17 contractors visited.

The Office of Audits' program results work was limited to analyzing contractor performance against goals in the time-phase plan. One Office regional director said that reviews of the time-phase plan were based on the premise that contractors performing at a high level of activity and meeting time-phase goals were conforming with OMBE's expectations. The director also stated that conclusions on program results are subjective because OMBE has not clearly defined program objectives. The director said objective reviews would be made once OMBE clarifies its criteria.

REPORTED ACCOMPLISHMENTS CAN BE MISLEADING

OMBE gathers, analyzes, and publishes a substantial amount of information on the progress of the national minority enterprise system. This includes activities of the coordinating committees, ^{1/} State and local government, private industry, and OMBE's own management-assistance program. OMBE publishes this data in various mediums, including reports, newsletters, and congressional testimony.

In reporting accomplishments for its management-assistance program, OMBE typically concentrates on activity levels, showing the total clients assisted and number and amount of loans and contracts obtained. (See app. III.) OMBE's reports do not show whether the management-assistance program is effective. OMBE reports the number of businesses started but does not show how many expanded or failed.

^{1/}These committees serve as a primary mechanism OMBE uses to implement its coordinating responsibility. They are known as the Inter-Agency Committee (made up of top officials in Washington, D.C.) and the Minority Business Opportunity Committee (made up of officials outside of Washington, D.C.).

OMBE reported that 24,683 clients had been assisted in fiscal year 1974 and 33,137 in fiscal year 1975. These statistics can be misleading because high activity levels and growth in activity levels can create an illusion of success. They also do not distinguish between clients not in business and those in business; our sample showed that 169 clients were not in business when they approached OMBE. Also, OMBE's statistics do not show that some clients were not given assistance--of the 344 clients in our sample, 127 clients (37 percent) were not given management assistance.

OMBE's statistics should distinguish between clients not in business and in business and should clearly state that only partial program results data is available.

Probably OMBE's most direct accomplishment in the management-assistance program relates to contractors themselves. A congressional investigative report evaluating OMBE (dated March 1975) reported that most OMBE contractors were formed in response to the OMBE program. OMBE has stated that only a limited number of qualified contractors existed before OMBE began its funding program, but that there is a growing number of firms that can provide effective service. This would be an accomplishment if these contractors became management-consultant firms. However, most of these firms receive all their income from OMBE, and they would likely go out of business almost immediately if OMBE stopped funding them.

CONCLUSIONS

OMBE judges its contractors' progress by comparing their activity levels with preestablished goals. A more proper criterion would be their success or lack of success in meeting OMBE's program objectives. OMBE should state, as policy, that such criteria will receive primary consideration and activity levels will play a secondary role.

OMBE's monitoring and evaluation systems do not now generate the information necessary to make such an analysis. The system must be revised so that an analysis can be made of each contractor's (1) effectiveness in meeting client objectives (to start or expand businesses) and (2) efficiency in providing clients a comprehensive assistance program.

Because OMBE has not been adequately monitoring contractors, project officers should be relieved of their heavy contract-administration duties so that more resources

will be available to monitor and evaluate. Less reliance should be placed on internal audit reports.

OMBE's information is valuable and allows administrators and legislators to gage the resources being put into the minority-business development. However, without program results data these officials cannot weed out weak and non-productive programs. OMBE should qualify published accomplishments by stating that program results data is generally not available so that observers are kept from drawing unduly optimistic conclusions from the fact that activity levels are growing.

RECOMMENDATIONS

We recommend that the Secretary of Commerce require the Director of OMBE to:

- Provide that primary emphasis in the monitoring and evaluation systems is placed on determining whether contractors are meeting program objectives and secondary emphasis placed on the contractors' activity levels. Emphasis should also be placed on determining whether contractors are providing clients a comprehensive assistance program.
- Instruct regional offices to fully implement monitoring and evaluation regulations by (1) fully reviewing contractors' narrative reports, (2) making regular contractor site visits, and (3) regularly contacting clients. Regional offices should be discouraged from relying on internal audits as a substitution for monitoring.
- Study the possibility of freeing regional program officers from their heavy contract-administration workload.

OMBE concurred with our recommendations.

CHAPTER 5

SCOPE OF REVIEW

Our review was aimed at assessing how well OMBE had met its responsibilities for (1) helping clients start, maintain, or expand their business and (2) providing clients a comprehensive assistance program. We conducted our review at OMBE and SBA headquarters in Washington, D.C.; at OMBE regional offices in New York City, Washington, D.C., and San Francisco; and at an OMBE field office in Los Angeles. These cities had significant activity levels. We included (1) only contractors within the city limits of New York, Washington, and Los Angeles and (2) all contractors in an eight-county San Francisco metropolitan area.

OMBE funded 70 contractors at these locations. We excluded 17 from consideration because they were national or statewide in scope and had activities outside this report's selected geographical areas. Excluded were:

- Seven minority business and trade associations.
- Five national business-development organizations.
- Three private-resource programs.
- One construction-contractor assistance center.
- One contractor funded at the State level.

This process left us with a universe of 53 contractors; we then selected 27 contractors to be visited. This number was determined by the following constraints:

- To maintain the same proportion of each contractor type in the sample as was found in the universe of 53 contractors.
- To visit one of each contractor type in at least two geographic locations.
- It was impossible to visit all 53 contractors because of limited time and resources.

Twenty-five of the 27 contractors were selected randomly; 2 had to be included automatically to meet the above constraints because they were the only ones of their type left in the selected locations after the random selections were made.

However, after the 27 contractors were visited, 10 had to be dropped from our review because:

- Four were national or international in scope. Three private-resource programs and one experimental and developmental project had activities beyond the geographical scope of this review.
- Three had no clients. Two experimental and demonstration projects and one construction contractor center had no clients either because they were too new or because their operation did not involve providing client assistance.
- Two had very few clients. A minority-business and trade association had only 6 clients, and a contract-support service had only 10 clients. These contractors did not appear fully operational.
- One was educational and provided classroom training and, as a result, did not appear comparable to other contractors.

By excluding these 10 contractors, the number of contractors reviewed was reduced to 17. Each contractor was then visited to determine the number of clients each had, in accordance with OMBE's definition of client. Each contractor was asked to identify the number of clients it had as of December 31, 1974; this information was supplemented in some cases by reviewing contractor records. The 17 contractors had 4,996 clients; 376 of these were randomly selected for review in detail. The following table shows these sample contractors and clients arrayed first by type of contractor and then by location.

Sample Contractors and Clients

<u>Contractors</u>	<u>Number of contractors</u>	<u>Number of clients in universe</u>	<u>Number of clients in sample</u>
By type:			
Local business develop- ment associations	11	3,896	300
Construction contrac- tor assistance centers	2	245	18
Business resource centers	2	446	31
Minority business and trade associations	1	194	14
Contract support services	<u>1</u>	<u>215</u>	<u>13</u>
Total	<u>17</u>	<u>4,996</u>	<u>376</u>
By geographic area:			
Los Angeles	5	1,837	141
New York City	4	1,389	105
San Francisco	5	1,148	80
Washington, D.C.	<u>3</u>	<u>622</u>	<u>50</u>
Total	<u>17</u>	<u>4,996</u>	<u>376</u>

We reviewed contractor records and interviewed contractor officials to determine what assistance had been provided to the sample clients. Where possible, clients were interviewed in person or by telephone to determine their status and obtain their views about the program. We reviewed SBA records to determine what financial and management assistance was provided to the sample clients.

We interviewed OMBE officials and reviewed written policies, procedures, and reports in the three OMBE regions visited and the headquarters office.



UNITED STATES DEPARTMENT OF COMMERCE
The Assistant Secretary for Administration
Washington, D.C. 20230

JUN 29 1977

JUN 27 1977

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

Dear Mr. Eschwege:

This is in reply to your letter of May 2, 1977,
requesting comments on the draft report entitled
"The Office of Minority Business Enterprise Could
Do More To Start and Maintain Minority Business."

We have reviewed the enclosed comments of the
Director-designate, Office of Minority Business
Enterprise and believe they are responsive to
the matters discussed in the report.

Sincerely,

Elsa A. Porter
Assistant Secretary
for Administration

Enclosure



UNITED STATES DEPARTMENT OF COMMERCE
Office of Minority Business Enterprise
 Washington, D.C. 20230

June 10, 1977

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 request of May 2, 1977 for comments on the draft report to the Congress entitled "The Office of Minority Business Enterprise Could Do More to Start and Maintain Minority Businesses."

Although we disagree with one of the key statements in the report, and take issue with a few findings, we believe that the report is essentially accurate in its statement of facts, well-balanced to its analysis of the situation, and -- with the exceptions noted below -- realistic in its recommendations. Overall, the tenor and specifics of the report are consistent with the recently completed evaluations of various aspects of the OMBE program we have commissioned. Together, the GAO reports and these evaluations will be of significant help to us in our efforts to improve the management of the OMBE program.

There are, however, several points which would materially clarify or otherwise strengthen the report. These are listed below, referenced by page number for your convenient reference.

One of the key statements (page 44) is that OMBE should use profits, rather than gross receipts, as its key measure of client progress. The basic reason advanced in the report (page 44) is that "the use of gross receipts data to analyze a client's progress can be misleading and can disguise serious problems."

We agree that a gross receipts measure, by itself, can be misleading in certain cases, and that it would be preferable to use net income (profit). However, the practical difficulties of relying on such a measure appear to be insuperable. These problems include:

(1) The virtual impossibility of obtaining reliable profit data from clients on a regular and on-going basis.

-- It is possible, through external sources (e.g., our contract with Dun and Bradstreet) to cross-check the sales volumes

(gross receipts) of our clients. It is not possible to obtain such a check of profit data; at least it is not possible within the resources available to OMBE. In theory, we could pay for an independent certified audit of the books of each client firm, and this would give us valid profit information. In theory too, we could access the IRS tapes and ascertain what each client firm has reported to Internal Revenue. However, the former course of action would be prohibitively expensive, and would represent a logistics nightmare. The latter course, no matter how carefully safeguarded, would be a gross breach of confidentiality. (In addition, IRS tapes run up to two years behind the fact; the data we receive would be for historical, not management, purposes.)

-- Doubtless, most clients would furnish us profit data if we required it. The reliability of this data, however, would be open to serious question. We note that SBA, which has a direct fiduciary relationship with its clients and could therefore be expected to obtain financial data quite readily, has had great difficulty in securing it. The Administrator of SBA recently testified that this was one of SBA's major problems.

(2) No other agency of government which provides technical assistance to businesses requires this regular submission of profit data. If OMBE were to do so, we would be imposing a clear double standard on minority entrepreneurs.

(3) Both the Congress and the Administration are committed to reducing the paperwork/reporting burden levied on small businesses by the Government. It would be difficult for us to justify, in such an environment, a requirement for regular reporting to us of profit data -- particularly when we can now obtain, without effort by the businesses concerned, their gross receipts figures.

(4) Senate Report No. 93-1168 of the Select Committee on Small Business states (page 19) that "A composite figure of net income is not as good a measure of outputs for classification within an industry division as is business receipts." It states further (page 24) that: "Business receipts income is a more reliable classifier of the size and the contribution (to the economy) of an individual business enterprise than net income. This assumption seems to hold whether comparisons are made on a year-to-year basis or on relative standings within its industry divisions at a given point in time."

-- Beginning in 1975, OMBE began to track the growth of minority firms by industry classification, in terms of both minority firms by themselves and vis-a-vis all U.S. industry (less public corporations). This has become an increasingly important measure, and reinforces our decision to adopt gross receipts rather than net income as our primary yardstick.

Findings

Page 15, paragraph 3. "OMBE has not established criteria which tell contractors when clients should have business plans prepared." The implication is that OMBE should establish hard criteria for the initiation of client business plans. We agree that this should be done for each serious client. It follows, however, that the development of such a plan would result in a greater number of continuing clients. Each contractor would, in a short time, reach a limit in its ability to accept new clients. GAO makes an excellent point that continued assistance must take place if OMBE services are to have a meaningful impact. There must be, however, a clear understanding by the Congress and within the Executive of the constraints placed on the eventual availability of OMBE services to new entrants. To put it simply: within existing and anticipated resources, we cannot have it both ways. OMBE can provide longer-range continuing assistance, or it can increase the number of its clients. We have chosen the first course. Thus, OMBE's FY 1978 Budget Request, submitted to the Congress in January, 1977, calls for a sharp reduction in the number of minority firms to receive OMBE assistance in FY 1978.

[See GAO note 1, p. 47]

[See GAO note 1, p. 47]

Pages 47-49. Comments on the Abt program evaluation. We emphatically do not agree with the three findings in this section.

(a) With regard to the high non-response rate, we fail to see why this resulted in a "substantial upward bias." Businesspeople, successful or unsuccessful, do not like to be bothered with questionnaires and interviews which detract from their working day. This has no direct correlation to bias in the sample.

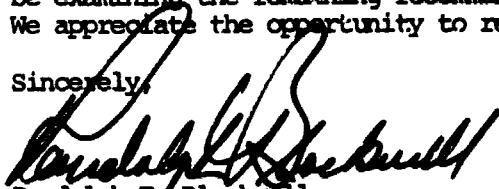
(b) With regard to the omission of costs in computing the benefit cost ratio, we agree with Abt that the costs in question did not relate directly to the BDO or CCAC programs, and therefore it would have been irrelevant to include them in the computation. The report asks, for example, why Program Research and Development costs were excluded but Public and Congressional Affairs included. The answer is simple: The latter office is frequently involved with our local contractors in such areas as advising on promotion, advertising and replies to Congressional inquiries. Our R&D operation, however, then and now, has no such contact.

(c) With regard to the general adequacy of Abt's benefit/cost calculations, we believe that the study did, in fact, account for all significant and relevant costs, and that the benefits are fully supportable in the documentation appended to the report. The GAO findings do not present data to the contrary. We therefore remain convinced that the Abt Report did provide an accurate picture of program impact.

[See GAO note 1, p. 47]

As I stated at the beginning of this letter, we found the report to be helpful in the management of the OMBE program. Plans are already underway to improve the programs consistent with a number of recommendations. We anticipate that in the near future we will be examining the remaining recommendations for future implementation. We appreciate the opportunity to review and comment on this report.

Sincerely,



Randolph T. Blackwell
Director-designate

- GAO note 1: Deleted comments refer to material contained in the draft that has been revised or has not been included in the final report.

- GAO note 2: Page references in this letter may not correspond to pages in the final report.

ABT ASSOCIATES INC.
 55 WHEELER STREET CAMBRIDGE, MASSACHUSETTS 02138
 TELEPHONE AREA 617-492-7100

May 17, 1977

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

MAY 19 1977

Dear Mr. Eschwege:

We are responding to your letter of May 4 requesting comments on GAO's observations and conclusions regarding Abt Associates' evaluation of LBDOS and CCACs. We will comment in turn on: the three identified evaluation "weaknesses"; GAO's major conclusions; and the general thrust of GAO's analysis.

Nonresponse and Replacements

GAO concludes that a high nonresponse rate coupled with random replacement resulted in a "substantial upward bias" in minority business operating characteristics reported in Volume II, Chapter 4. This conclusion is apparently based on the feeling that, because Abt Associates did not sample nonrespondents, the sample reporting is "overloaded...with successful operating businesses owned by persons who are probably satisfied with the program." In our view, neither this observation nor GAO's conclusion are valid. GAO's conclusion is justified only if a case can be made for consistent differences in operating characteristics between a majority of nonrespondents and sampled firms. Using nonrespondent data from Volume III, Appendix B, we find that only 6.6% (41 firms) of the sample of 623 are replacements with operating characteristics that may differ from the firms they replaced. We firmly believe that this degree of nonresponse bias warrants the "modest upward bias" conclusion in Volume III, Appendix B, rather than GAO's opinion that this bias is "substantial."

The analysis of nonrespondent data leading to our conclusion is as follows:

- 35 percent of nonrespondents could not be contacted, either because business owners did not return repeated phone calls or because the businesses had no phone, and owners could never be located at their places of business. In our view, inability to contact resulted from either owner disinterest in the research project or lack of local interviewer incentive to continue to track down owners after a reasonable effort had been made. In neither of these situations can inability to contact be consistently associated with any particular set of operating (balance sheet or income statement) characteristics.

Mr. Henry Eschwege

May 17, 1977

- 32.1 percent of nonrespondents refused to respond to detailed questions once they were contacted and the study was explained to them. Three-quarters of these nonrespondents simply would not spend the considerable time required or would not provide operating data they considered confidential. Fifteen percent of these nonrespondents (3.7 percent of all nonrespondents) would not cooperate because they were dissatisfied with assistance they had received. (No specific reasons for refusal can be attributed to the remainder of these nonrespondents.) Again, noncooperation due to unwillingness to spend time or reveal confidential data cannot be logically linked to particular attributes of business performance; that is, it is probably equally likely that owners of either healthy or weak firms would have attitudes that lead to refusal to respond.
- 13.2 percent of nonrespondent businesses were not operating (due to seasonal or sporadic existence), and 3.7 percent had failed. Exclusion of currently inoperative businesses probably excludes smaller, marginal, seasonal construction and retail/service firms from the reporting sample. No data are available to indicate how failed nonrespondents might differ from the reporting sample; however, it is likely that these failed firms suffered from a combination of inadequate capitalization, burdensome debts, inefficient operations, low profit margins, and declining revenues. Any or all of these attributes could set these firms apart from operating, nonfailing firms.
- 5.8 percent of nonrespondents were start-ups that had existed for less than six months. These start-ups were never meant to be included in the study sample (see Volume II, Chapter 1, Page 21). (We found that, in general, many firms are not even generating revenues six months from incorporation (or registration for proprietorships). Hence, we excluded these firms from the data base so that operating characteristics would not be biased. Benefit-cost ratio calculations for "start-ups" thus are based on firms that are at least six months old.) Hence, the 5.8 percent of nonrespondents categorized as "start-ups" are firms that should have been excluded but were simply not caught in the first screen of the universe.
- Exclusion of the 4.9 percent of nonrespondents that had never existed has no effect on the validity of reported data, given the random replacement of these firms in the data base.

Mr. Henry Eschwege

May 17, 1977

- Finally, 5.3 percent of nonrespondent businesses had changed ownership subsequent to LBDO/CCAC assistance and prior to the Abt evaluation. (New owners would not respond to inquiries, data on the firm prior to transfer of ownership were not available, or the previous owner could not be located.) Do these transfers mainly include rapidly growing and successful firms, were they headed for trouble before a new owner was found to turn these businesses around, or were they more or less average firms in terms of their recent operating history? We frankly do not know. However, there is no clear justification for assuming that these firms were anything but average. (Indeed, the fact that a buyer was found suggests that it is more likely that these transfers outperformed rather than underperformed the reporting businesses.)

Exclusion of Certain Administrative Costs from Regional Cost Allocation

There is a simple and logical explanation for the exclusion of \$1,871,820 in National Programs, Advisory Council, and Program Research and Development headquarters costs from the regional and LBDO/CCAC overhead allocation, which negates GAO's conclusion that "significant amounts of costs" were excluded in computing the benefit-cost ratio. Specifically, our review of program documentation and extensive discussion with OMB headquarters personnel indicated that none of the activities with these three program areas provided policy or administrative support services directly to LBDO and CCAC technical-assistance contractors (see Volume III, Appendix E, Page 4). In contrast, portions of the Office of the Director, Public and Congressional Affairs, and the General Counsel's Office were found to support LBDO/CCAC activities through the headquarters Field Operations Division and Regional Offices. The three excluded divisions support LBDO/CCAC activities only in the most general sense that each portion of the OMB effort must perform well for the entire effort to be judged a success; however, the criterion that a staff function be directed toward LBDO/CCAC contractor support in a clearly identified way logically eliminates these divisions from the cost-allocation calculations.

Benefit/Cost Calculations

GAO's third conclusion that benefit/cost calculations are biased is based on three observations: (1) "costs are included only for those firms that were successfully assisted"; (2) costs associated with unsuccessful firms excluded from the universe are excluded; and (3) National Programs, Advisory Council, and Program Research and Development costs were excluded.

The first and second observations are technically correct. However, they are misleading in the context of how benefit/cost results are formulated and presented in Volume II, Chapter 6. Furthermore, they do not support GAO's conclusion. Table 1 on the following page summarizes benefit/cost calculations

TABLE 1

Benefit/Cost Results: Formulation (a)

$$\left(\frac{\alpha[(B_1 - B_0) - (C_1 - C_0)]}{c^1} \right)$$

Bank Administrative Costs Included

	Discounted Benefit/Cost Ratio	Attribution Factor (α) Values						Break-even α Value
		1.0	.75	.5	.25	.1	.05	
Business Starts	8.9α							
Business Saves	19.8α	19.8	14.7	9.8	4.9	2.0	1.0	.05
Operational Business	43.5α			21.8	10.9	4.4	2.2	.02

Benefit/Cost Results: Formulation (b)

$$\left\{ \frac{(B_1 - B_0)}{(C_1 - C_0) + c^1} \right\}$$

	Discounted Benefit/Cost Ratio
Business Starts	.43
Business Saves	1.15
Operational Firms	5.25

Bank Administrative Costs Included

Mr. Henry Eschwege

May 17, 1977

from Tables 6.13 and 6.14 of the final report. Ratios are calculated separately for each of three types of assisted firms ("starts," "saves," and other "operational"). These ratios are calculated from data characterizing sample businesses. Using weighting procedures described in Chapter 1 (Volume II) and a computerized algorithm, these ratios provide unbiased estimates of program benefits and costs for three classes of LBDO/CCAC-assisted businesses. For each of these classes of businesses, administrative and resource opportunity costs are matched with corresponding value-added benefits.

We do not present an overall benefit/cost ratio for OMBE technical assistance in Chapter 6, Volume II. Nor do we present separate benefit/cost ratios for firms that failed despite LBDO/CCAC assistance or that were purposefully excluded from the universe (e.g., firms that had received fewer than five recorded inputs of management and technical-assistance services). The last paragraph of Page 6-43 (Volume II) shows that Abt Associates' concluding observation on program benefits is carefully worded to make it clear that benefit/cost results are different among classes of firms.

The more general conclusion on Page 8-2 (Volume II) that "costs borne by society to support minority-owned firms are exceeded by their benefits to society" is, admittedly, not clearly supported by the analyses in Chapter 6. However, some additional calculations suggest that, even with costs associated with unsuccessful firms included in benefit/cost ratios, this conclusion is justified. Attachment 1 describes the conservative assumptions and calculations that produce unbiased program benefit/cost ratios of 2.07 and 1.24, using the two benefit/cost formulations described in Volume II, Chapter 5, of the final report.

GAO's third observation, although correct, does not support GAO's conclusion, given the rationale for excluding certain administrative costs outlined in the previous section of this response.

GAO's Major Conclusions

GAO concludes that the evaluation "contains weaknesses which...affect the validity of Abt's conclusions" and that "the study did not provide OMBE with accurate information about program results." Based upon our analysis of GAO's comments and reexamination of the final report (Volumes II and III), we cannot concur with GAO's extreme, generalized, and overstated conclusions.

What GAO's Analysis Does Not Say

Abt Associates took a conservative approach in all of its analyses. Limitations of data and analysis techniques are explicitly recognized; key conclusions do not stretch the limits of available information and analysis. The results are, we believe, both valid and reasonably accurate. Conclusions are generally favorable but point to numerous opportunities for program improvement; recommendations presented in Chapter 8 of Volume II and in the cover letter accompanying the final report (Attachment 2) provide additional

Mr. Henry Eschwege

May 17, 1977

specific and constructive guidance for changes and improvements in program policy, strategy, and administration.

We are frankly disappointed that GAO analysts did not examine the Abt study with the same thoroughness with which Abt evaluated the LBDO and CCAC programs. Further, we believe that GAO could have more constructively spent time highlighting key Abt conclusions and recommendations that have a bearing on the future direction, effectiveness, and efficiency of OMBE programs. Using the information in Volume II, Chapter 8, and Attachment 2 to this letter, GAO could have strengthened its analysis considerably by incorporating many of the interesting and useful results of Abt Associates' work.

I trust that the foregoing discussion adequately responds to your request for comments. If you have any further questions, please feel free to call me.

Sincerely,



Dean R. Ericson
Deputy Area Manager
Economic and Environmental Analysis

/cac

Attachments (2) [See GAO note]

cc: Alan Stephenson
Sherman Funk

GAO note: The attachments to this letter have been deleted since they have no effect on our position in this report.

PLANNED VERSUS ACTUAL ACCOMPLISHMENTS FOROMBE'S MANAGEMENT-ASSISTANCE PROGRAM--FISCAL YEARS 1974 AND 1975 (note a)

	<u>1975</u>		<u>1974</u>	
	<u>Planned</u>	<u>Actual</u>	<u>Planned</u>	<u>Actual</u>
Total potential or established businesses	21,575	33,137	24,700	24,683
Potential or established businesses receiving management and technical assistance	18,500	30,746	20,300	14,010
Business packaging assistance:				
Number of loans approved	4,175	5,008	5,100	4,597
Value of loans (dollars in million)	\$203.1	\$244.8	\$225.0	\$200.8
Contract procurement assistance:				
Number of contracts approved	4,150	5,708	1,650	3,824
Value of contracts (dollars in millions)	\$231.0	\$433.6	\$215.0	\$252.6

a/See discussion on reported accomplishments beginning on page 36.

CONTRACTOR TYPES FUNDED BY OMBE

OMBE funds different organization types to provide business assistance. These organizations and OMBE's description of their functions are listed below.

- Local business-development organizations are the primary contact point for minority entrepreneurs needing assistance. These contractor services include providing management and technical assistance; preparing financial packages (such as loan packages), feasibility studies, and profit and loss statements; and assisting in obtaining procurement contracts.
- National business-development organizations are local business-development organizations affiliated with a national office that provides centralized administrative services and a national scope of activities.
- Construction-contractor assistance centers provide local business-development organization-type services to minority contractors needing general business services peculiar to construction contracting.
- Minority business and trade associations are national and local minority peer-group associations comprised of representatives from either diverse business backgrounds or a single trade. The management-assistance functions are largely determined by their membership, but activities usually include exchanging information and techniques on projects such as joint purchasing, sales promotion, and sponsoring special projects for members.
- Business resource centers provide management assistance to clients that other organizations do not normally provide. These contractors are also supposed to identify and mobilize private resources to help minority entrepreneurs.
- Private resource programs stimulate business opportunities and provide management assistance through national professional and trade organizations which in turn are to involve their members at the local level.

- Contract support services provide management assistance to qualified minority businesses whose needs cannot be served by other organizations.
- Business management development organizations conduct management development programs and provide education.
- State OMBE organizations are to duplicate OMBE's efforts but at the State level. They are also to establish State minority procurement set-aside programs and provide management assistance to areas not serviced by OMBE's other contractors.
- Experiment and demonstration projects examine the feasibility of new program approaches or methods for developing minority businesses.

These various contractor types make up OMBE's delivery system. Some types are to serve as initial point of contact and service clients' overall general needs. Other types are to provide specialized services to meet a client's particular problems or needs.

By design, this system makes available to each contractor whatever resources are needed to meet a client's needs. It requires that contractors support each other by accepting and referring clients.

Three contractor types are to generally assist minorities to start, maintain, and expand successful businesses by providing general assistance. Business development organizations extend into the community to provide general business information, loan packaging and procurement assistance, and management and technical assistance. Construction-contractors assistance centers provide contractors with planning, bidding, estimating, legal, and subcontracting assistance. Minority business and trade associations exchange information, share business experiences, develop trade credit, and sponsor trade fairs.

Three other contractor types are to work primarily to develop the private sector for minority entrepreneurs and to provide specialized management and technical assistance where business needs cannot be met by other contractors. Business resource centers develop investment capital, management and technical resources, and specialized assistance capabilities. Private resource programs are to support trade associations individually to best utilize resources

to help minority business. Contracted support services contractors are to meet the needs of large businesses with complex problems that cannot be met by other OMBE contractors.

Two more contractor types further supplement OMBE's activity. State OMBEs are to develop special procurement and training programs while experiment and demonstration contractors conduct pilot projects for delivering services and develop innovative programs for developing business skills.

FUNDING BY CONTRACTOR TYPE

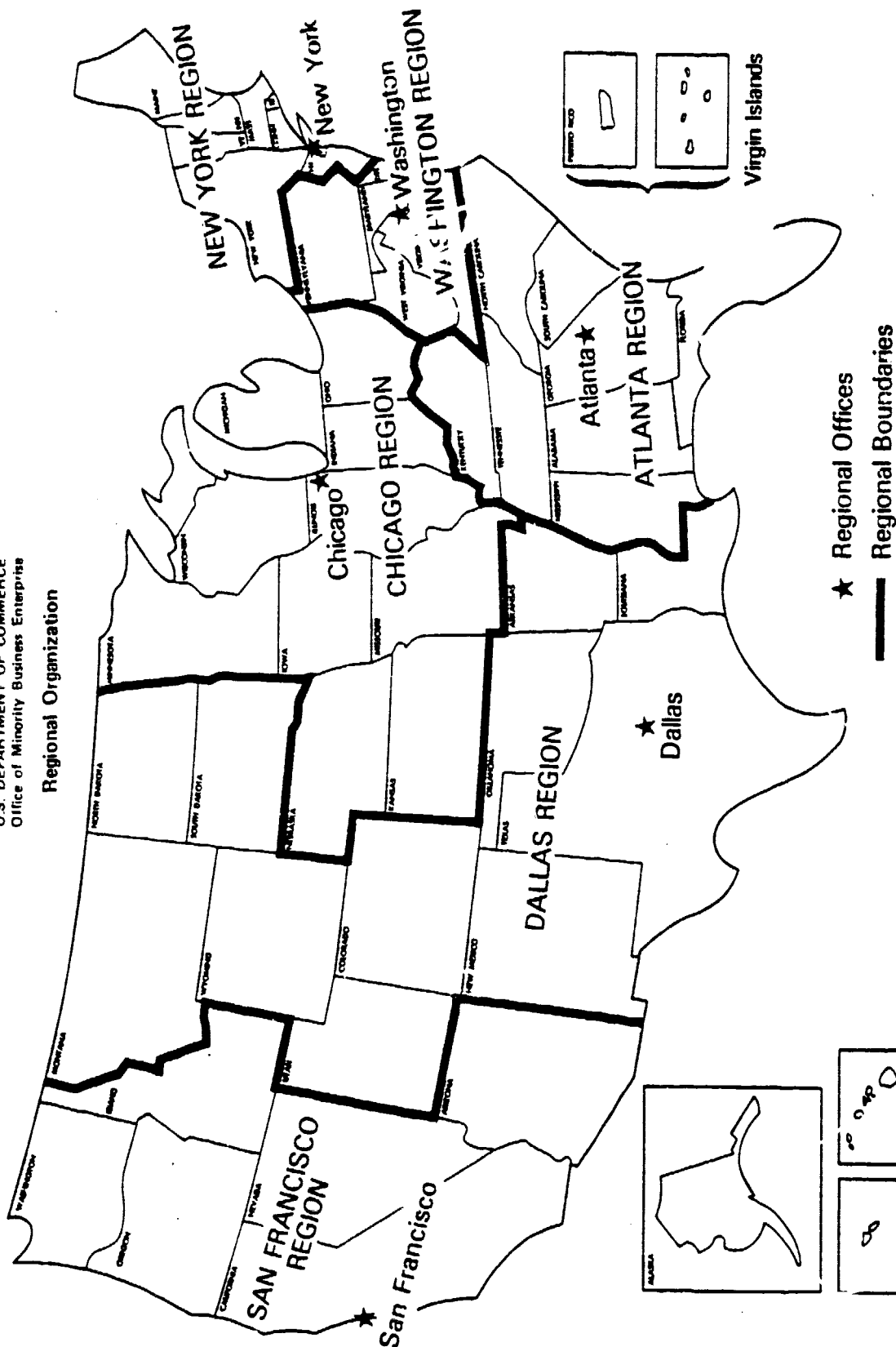
Organization type	Obligated funds between FY 1972 and FY 1975		Obligated funds in FY 1975	
	<u>Number of organizations</u>	<u>Total funds</u>	<u>Number of organizatons</u>	<u>Total funds</u>
		(millions)		(millions)
Local business- development organization	183	\$79.4	126	\$24.9
National business development organization	10	6.4	0	0
Construction- contractors assistance center	35	12.7	30	6.3
Minority business and trade association	24	8.4	16	2.9
Business resource center	29	8.8	21	3.7
Contracted support service	53	12.3	14	2.8
Private resource program	34	8.7	15	2.8
Experiment and demonstration	66	7.5	50	4.3
Business management development (note a)	35	5.5	17	2.1
Government investment	<u>20</u>	<u>6.1</u>	<u>18</u>	<u>2.4</u>
Total	<u>489</u>	<u>\$155.8</u>	<u>307</u>	<u>\$52.2</u>

a/This type of contractor was not funded by OMBE after fiscal year 1975.

A MAP OF OMBE REGIONS

U.S. DEPARTMENT OF COMMERCE
Office of Minority Business Enterprise

Regional Organization



★ Regional Offices
— Regional Boundaries

To San Francisco Region

FREQUENCY OF MANAGEMENT ASSISTANCE BY TYPE

<u>Type of assistance</u>	<u>Total clients receiving each type</u>	<u>Percent of clients receiving assistance</u>
Marketing	64	29
Management	61	28
Accounting	56	26
Finance	32	15
Legal	21	10
Loan packaging (note a)	21	10
Procurement	20	9
Site selection	13	6
Insurance	5	3
Income tax	2	0
Other (note b)	79	36

a/Contractors did not consistently charge this category when preparing loan packages. That is why this category does not agree with the total number of loan packages prepared (94) as discussed on page 22.

b/The largest category shown (other) seemed to be used as a catchall category by contractors.

PRINCIPAL DEPARTMENT OF COMMERCE OFFICIALS
RESPONSIBLE FOR ADMINISTERING ACTIVITIES
DISCUSSED IN THIS REPORT

	<u>Tenure of office</u>	
	<u>From</u>	<u>To</u>
SECRETARY OF COMMERCE:		
Juanita M. Kreps	Jan. 1977	Present
Elliot L. Richardson	Feb. 1976	Jan. 1977
Rogers C. B. Morton	May 1975	Feb. 1976
John K. Tabor (acting)	Mar. 1975	Apr. 1975
Frederick B. Dent	Feb. 1973	Mar. 1975
Peter G. Peterson	Feb. 1972	Jan. 1973
Maurice H. Stans	Jan. 1969	Feb. 1972
DIRECTOR, OFFICE OF MINORITY BUSINESS ENTERPRISE (note a):		
Randolph T. Blackwell	July 1977	Present
Allan A. Stephenson (acting)	Jan. 1977	July 1977
Alex M. Armendaris	Apr. 1973	Jan. 1977
Walter Sorg (acting)	Mar. 1973	Apr. 1973
John L. Jenkins	Aug. 1971	Mar. 1973
Vacant	May 1971	Aug. 1971
Abraham S. Venable	Apr. 1970	Apr. 1971
Abraham S. Venable (acting)	Jan. 1970	Apr. 1970
Thomas F. Roeser	Apr. 1969	Jan. 1970

a/The present position was established effective April 1970. Previously, minority activities were headed by an assistant to the Secretary.