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**ALASKA NATIVE
CORPORATIONS**

**Increased Use of Special
8(a) Provisions Calls for
Tailored Oversight**

Statement of Katherine V. Schinasi, Managing Director
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Highlights of [GAO-07-1251T](#), a testimony before the Committee on Natural Resources, House of Representatives

Why GAO Did This Study

Alaska Native corporations (ANC) were created to settle land claims with Alaska Natives and foster economic development. In 1986, legislation passed that allowed ANCs to participate in the Small Business Administration's (SBA) 8(a) program. Since then, Congress has extended special procurement advantages to 8(a) ANC firms, such as the ability to receive sole-source contracts for any dollar amount and to own multiple subsidiaries in the 8(a) program. We were asked to testify on an earlier report where we identified (1) trends in the government's 8(a) contracting with ANC firms, (2) the reasons agencies have awarded 8(a) sole-source contracts to ANC firms and the facts and circumstances behind some of these contracts, and (3) how ANCs are using the 8(a) program. GAO also evaluated SBA's oversight of 8(a) ANC firms.

GAO made recommendations aimed at improving SBA's oversight of 8(a) ANC contracting activity and ensuring that procuring agencies properly oversee 8(a) contracts they award to ANC firms. SBA has either taken action or plans to take action on the recommendations. The procuring agencies generally agreed with our recommendation to them.

We believe implementation of our recommendations will provide better oversight of 8(a) ANC contracting activity and provide decision makers with information to know whether the program is operating as intended.

www.gao.gov/cgi-bin/getrpt?GAO-07-1251T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Katherine Schinasi at (202) 512-4841 or schinasi@gao.gov.

ALASKA NATIVE CORPORATIONS Increased Use of Special 8(a) Provisions Calls for Tailored Oversight

What GAO Found

While representing a small amount of total federal procurement spending, obligations for 8(a) contracts to ANC firms increased from \$265 million in fiscal year 2000 to \$1.1 billion in 2004. Over the 5-year period, agencies obligated \$4.6 billion to ANC firms, of which \$2.9 billion, or 63 percent, went through the 8(a) program. During this period, six federal agencies—the departments of Defense, Energy, the Interior, State, and Transportation and the National Aeronautics and Space Administration—accounted for over 85 percent of 8(a) contracting activity. Obligations for 8(a) sole source contracts by these agencies to ANC firms increased from about \$180 million in fiscal year 2000 to about \$876 million in fiscal year 2004.

ANCs use the 8(a) program as one of many tools to generate revenue with the goal of providing benefits to their shareholders. Some ANCs are heavily reliant on the 8(a) program for revenues, while others approach the program as one of many revenue-generating opportunities. GAO found that some ANCs have increasingly made use of the congressionally authorized advantages afforded to them. One of the key practices is the creation of multiple 8(a) subsidiaries, sometimes in highly diversified lines of business. From fiscal year 1988 to 2005, ANC 8(a) subsidiaries increased from one subsidiary owned by one ANC to 154 subsidiaries owned by 49 ANCs.

In general, acquisition officials at the agencies reviewed told GAO that the option of using ANC firms under the 8(a) program allows them to quickly, easily, and legally award contracts for any value. They also noted that these contracts help them meet small business goals. In reviewing selected large sole-source 8(a) contracts awarded to ANC firms, GAO found that contracting officials had not always complied with certain requirements, such as notifying SBA of contract modifications and monitoring the percentage of work that is subcontracted.

SBA, which is primarily responsible for implementing the 8(a) program, had not tailored its policies and practices to account for ANCs' unique status and growth in the 8(a) program, even though SBA officials recognized that ANCs enter into more complex business relationships than other 8(a) participants. Areas where SBA's oversight fell short included determining whether more than one subsidiary of the same ANC was generating a majority of its revenue in the same primary industry, consistently determining whether awards to 8(a) ANC firms had resulted in other small businesses losing contract opportunities, and ensuring that the partnerships between 8(a) ANC firms and large firms were functioning in the way they were intended.

Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss our April 2006 report on Alaska Native Corporation (ANC) 8(a) firms.¹ In December 1971, Congress enacted the Alaska Native Claims Settlement Act to resolve long-standing aboriginal land claims and to foster economic development for Alaska Natives. This legislation created ANCs, which would become the vehicle for distributing land and monetary benefits to Alaska Natives in lieu of a reservation system. As of December 2005, there were 13 regional ANCs and 182 village, urban, and group corporations.

In 1986, legislation was enacted that allowed ANC-owned firms to participate in the Small Business Administration's (SBA) 8(a) program—one of the federal government's primary means for developing small businesses owned by socially and economically disadvantaged individuals. Since then, Congress has extended special procurement advantages to ANC firms. For example, ANC firms are permitted to receive noncompetitive contracts for any amount, whereas other 8(a) companies are subject to competitive thresholds of \$5 million for manufacturing contracts or \$3 million for all other contracts. ANCs can also own multiple subsidiaries participating in the 8(a) program,² unlike other 8(a) firms that may own only one in a lifetime and no more than 20 percent of another 8(a) firm.

Our 2006 report on 8(a) ANC contracting identified (1) trends in contracting with ANC firms, (2) the reasons agencies have awarded 8(a) sole-source contracts to ANC firms and the facts and circumstances behind some of these contracts, and (3) how ANCs are using the 8(a) program. We also evaluated SBA's oversight of 8(a) ANC firms. We made a number of recommendations to SBA and also recommended that the agencies in our review work with SBA to develop training for their contracting personnel.

Today I will discuss the highlights of our report and provide an update on actions SBA and the other agencies have taken to address our recommendations.

¹GAO, *Contract Management: Increased Use of Alaska Native Corporations' Special 8(a) Provisions Calls for Tailored Oversight*, GAO-06-399, (Washington, D.C.: Apr. 27, 2006).

²Each 8(a) ANC firm must be in a different primary industry.

To address the objectives of our 2006 report, we obtained data on federal 8(a) contracting with ANCs. It is important to note that there is no readily available central source of information on ANC 8(a) contracting activity. We obtained each ANC firm's Data Universal Numbering System (DUNS) number and used this information to obtain data from the Federal Procurement Data System (FPDS) and agencies. To assess the reliability of the procurement data, we (1) compared FPDS and agency data to verify its accuracy, (2) reviewed related documentation, including contract files, and (3) worked closely with agency officials to identify and resolve any data problems. When we found discrepancies, we brought them to the agency's attention and worked with them to correct the discrepancies before conducting our analyses. We also analyzed 16 large, sole-source 8(a) contracts awarded to ANC firms from the departments of Defense, Energy, the Interior, State, Transportation, and Homeland Security and the National Aeronautics and Space Administration (NASA). We selected the contracts based on high ultimate award values and high dollar obligations that represented a variety of contractors and services. We traveled to Alaska and met with executives of 13 regional ANCs and 17 village or urban corporations. The report on which this testimony is based was prepared in accordance with generally accepted government auditing standards.

Our work did not include within its scope an objective or analyses that either support or challenge special ANC advantages within the 8(a) program. The program has been established in law and any changes are up to the Congress.

ANC Trends in and Use of 8(a) Contracting

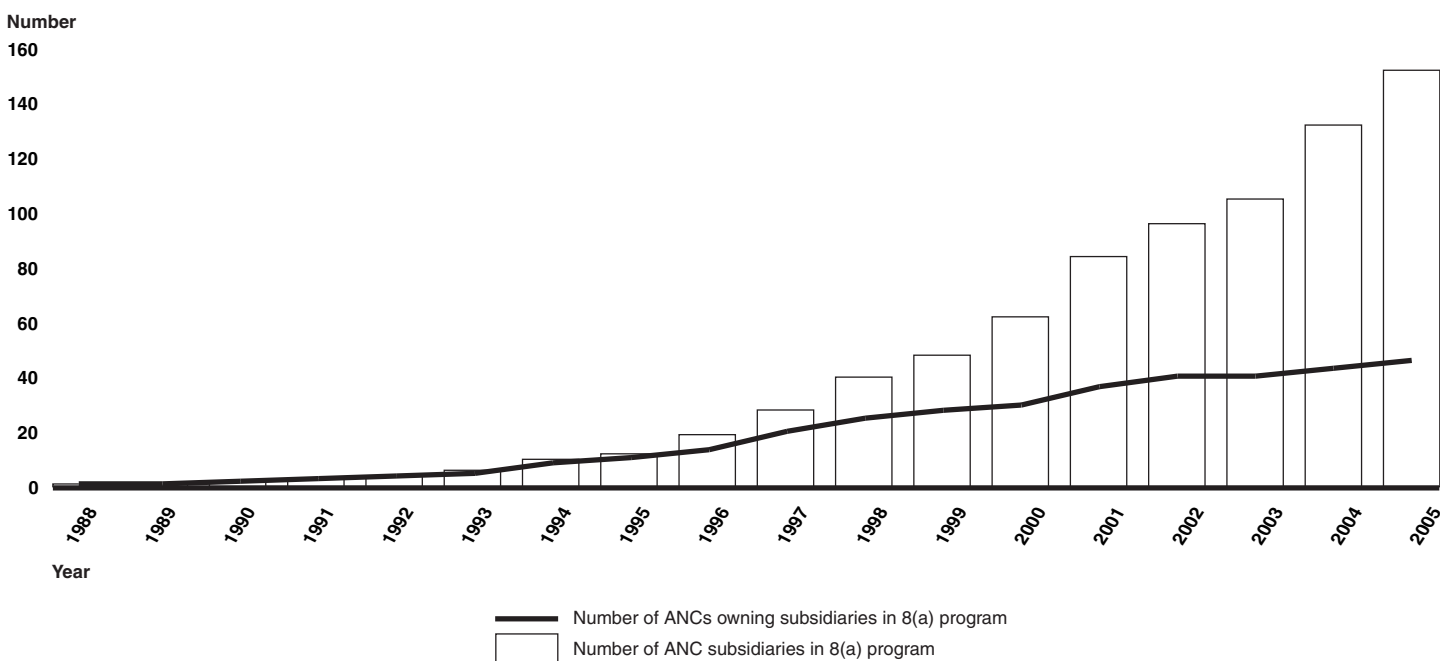
8(a) ANC contracting represents a small amount of total federal procurement spending. However, dollars obligated to ANC firms through the 8(a) program grew from \$265 million in fiscal year 2000 to \$1.1 billion in 2004. Overall, during the 5-year period, the government obligated \$4.6 billion to ANC firms, of which \$2.9 billion, or 63 percent, went through the 8(a) program.

During this period, six federal agencies—the departments of Defense, Energy, the Interior, State, and Transportation and NASA—accounted for almost 85 percent of total 8(a) ANC obligations. Obligations for 8(a) sole-source contracts by these agencies to ANC firms increased from about \$180 million in fiscal year 2000 to about \$876 million in fiscal year 2004.

ANCs use the 8(a) program as one of many tools to generate revenue with the goal of benefiting their shareholders. Some ANCs are heavily reliant on the 8(a) program for revenues, while others approach the program as one

of many revenue-generating opportunities, such as investments in stocks or real estate. ANCs are using the congressionally authorized advantages afforded to them, such as ownership of multiple 8(a) subsidiaries,³ sometimes in diversified lines of business. From fiscal year 1988 to 2005, numbers increased from one 8(a) subsidiary owned by one ANC to 154 subsidiaries owned by 49 ANCs. Figure 1 shows the recent growth in ANCs' 8(a) subsidiaries.

Figure 1: Number of ANC Parent Corporations and Subsidiaries Active in the 8(a) Program, 1988 to 2005



Source: GAO analysis of SBA data.

ANCs use their ability to own multiple businesses in the 8(a) program, as allowed by law, in different ways. For example, some ANCs

- create a second subsidiary in anticipation of winning follow-on work from one of their graduating subsidiaries;⁴

³In this testimony, “ANC” refers to the parent corporation. The term “ANC firm” denotes a business owned by an ANC. We use the term “ANC firm” and “subsidiary” interchangeably.

⁴There is a 9-year limit to participation in the 8(a) program; firms could graduate earlier if they outgrow their primary industry size standards.

-
- wholly own their 8(a) subsidiaries, while others invest in partially-owned subsidiaries; and
 - diversify their subsidiaries' capabilities to increase opportunities to win government contracts in various industries.

Contract Execution Shortfalls

Our review of 16 large sole-source contracts awarded by 7 agencies found that agency officials view contracting with 8(a) ANC firms as a quick, easy, and legal way to award contracts while at the same time helping their agencies meet small business goals.⁵

Memoranda of Understanding (partnership agreements) between SBA and agencies delegate the contract execution function to federal agencies, although SBA remains responsible for implementing the 8(a) program. We found that contracting officials had not always complied with requirements to notify SBA when modifying contracts, such as increasing the scope of work or the dollar value, and to monitor the percentage of the work performed by the 8(a) firms versus their subcontractors. For example:

- Federal regulation requires that when 8(a) firms subcontract under an 8(a) service contract, they incur at least 50 percent of the personnel costs with their own employees.⁶ The purpose of this provision, which limits the amount of work that can be performed by the subcontractor, is to ensure that small businesses do not pass along the benefits of their contracts to their subcontractors. For the 16 files we reviewed, we found almost no evidence that the agencies are effectively monitoring compliance with this requirement. In general, the contracting officers we spoke with were confused about whose responsibility it is.
- Agencies are also required to notify SBA of all 8(a) contract awards, modifications, and exercised options where the contract execution function has been delegated to the agencies in the partnership agreements. We found that not all contracting officers were doing so. In one case, the Department of Energy contracting officer had broadened the scope of a contract a year after award, adding 10 additional lines of business that almost tripled the value of the

⁵ANC firms in the 8(a) program are deemed by law as socially and economically disadvantaged. Awards to these firms are credited to agencies' small business goals.

⁶For general construction, the 8(a) firm is required to incur at least 15 percent of the personnel costs.

contract. These changes were not coordinated with SBA.

SBA Lacks Oversight of 8(a) ANC Activity

We reported in 2006 that SBA had not tailored its policies and practices to account for ANCs' unique status and growth in the 8(a) program, even though officials recognize that ANC firms enter into more complex business relationships than other 8(a) participants. SBA officials told us that they have faced a challenge in overseeing the activity of the 8(a) ANC firms because ANCs' charter under the Alaska Native Claims Settlement Act is not always consistent with the business development intent of the 8(a) program. The officials noted that the goal of ANCs—economic development for Alaska Natives from a community standpoint—can be in conflict with the primary purpose of the 8(a) program, which is business development for individual small, disadvantaged businesses.

SBA's oversight fell short in that it did not:

- track the primary business industries in which ANC subsidiaries had 8(a) contracts to ensure that more than one subsidiary of the same ANC was not generating the majority of its revenue under the same primary industry code;
- consistently determine whether other small businesses were losing contracting opportunities when large sole-source contracts were awarded to 8(a) ANC firms;
- adhere to a statutory and regulatory requirement to ascertain whether 8(a) ANC firms, when entering the 8(a) program or for each contract award, had, or were likely to obtain, a substantial unfair competitive advantage within an industry;⁷
- ensure that partnerships between 8(a) ANC firms and large firms were functioning in the way they were intended under the 8(a) program; and
- maintain information on ANC 8(a) activity.

SBA officials from the Alaska district office had reported to headquarters that the makeup of their 8(a) portfolio was challenging and required more contracting knowledge and business savvy than usual because the majority of the firms they oversee are owned by ANCs and tribal entities. The officials commented that these firms tend to pursue complex business relationships and tend to be awarded large and often complex contracts. We found that the district office officials were having difficulty managing their large volume and the unique type of work in their 8(a) portfolio.

⁷ This requirement is set forth in the Small Business Act (15 U.S.C. § 636(j)(10)(J)(ii)(II)).

When we began our review, SBA headquarters officials responsible for overseeing the 8(a) program did not seem aware of the growth in the ANC 8(a) portfolio and had not taken steps to address the increased volume of work in their Alaska office.

Previous Conclusions, Recommendations, and Agency Responses

In 2006, we reported that ANCs were increasingly using the contracting advantages Congress has provided them. Our work showed that procuring agencies' contracting officers are in need of guidance on how to use these contracts while exercising diligence to ensure that taxpayer dollars are spent effectively. Equally important, we stated, significant improvements were needed in SBA's oversight of the program. Without stronger oversight, we noted the potential for abuse and unintended consequences.

In our April 2006 report, we made 10 recommendations to SBA on actions that can be taken to revise its regulations and policies and to improve practices pertaining to its oversight of ANC 8(a) procurements. Our recommendations and SBA's June 2007 response are as follows.

We recommended that the Administrator of SBA:

1. Ascertain and then clearly articulate in regulation how SBA will comply with existing law to determine whether and when one or more ANC firms are obtaining, or are likely to obtain, a substantial unfair competitive advantage in an industry.

SBA response: SBA is exploring possible regulatory changes that would address the issue of better controlling the award of sole-source 8(a) contracts over the competitive threshold dollar limitation to joint ventures between tribally and ANC-owned 8(a) firms and other business concerns.

2. In regulation, specifically address SBA's role in monitoring ownership of ANC holding companies that manage 8(a) operations to ensure that the companies are wholly owned by the ANC and that any changes in ownership are reported to SBA.

SBA response: SBA is building a Business Development Management Information System to electronically manage all aspects of the 8(a) program. According to SBA, this system, scheduled to be completed in fiscal year 2008, will monitor program participants' continuing eligibility in the 8(a) program and could include an ANC element in the electronic annual review that would monitor the ownership of ANC holding companies that

manage 8(a) operations and ensure that any changes in ownership are reported to SBA.

3. Collect information on ANC's 8(a) participation as part of required overall 8(a) monitoring, to include tracking the primary revenue generators for 8(a) ANC firms to ensure that multiple subsidiaries under one ANC are not generating their revenue in the same primary industry.

SBA response: The planned electronic annual review can collect information on ANC's multiple subsidiaries to ensure that they are not generating the majority of their revenues from the same primary industry. Further, to ensure that an ANC-owned firm does not enter the 8(a) program with the same North American Industry Classification System (NAICS) code⁸ as another current or former 8(a) firm owned by that ANC, the ANC-owned applicant must certify that it operates in a distinct primary industry and must demonstrate that fact through revenues generated. SBA notes that the planned annual electronic reviews can validate this information.

4. Revisit regulation that requires agencies to notify SBA of all contract modifications and consider establishing thresholds for notification, such as when new NAICS codes are added to the contract or there is a certain percentage increase in the dollar value of the contract. Once notification criteria are determined, provide guidance to the agencies on when to notify SBA of contract modifications and scope changes.

SBA response: SBA stated that its revisions to its partnership agreements with federal agencies address this recommendation. However, we note that the revised agreement does not establish thresholds or include new criteria for when agencies should send SBA contract modifications or award documentation. The agreement states that agencies "shall provide a copy of any

⁸ SBA has designated a small business size standard for every NAICS code. 8(a) applicants must qualify as small under their primary NAICS code at the time of application and SBA's certification date. SBA regulation requires that at least 2 years lapse after an ANC firm exits the 8(a) program before another firm owned by the same parent ANC can enter the program with the prior firm's primary NAICS code. However, once accepted into the program, 8(a) firms may pursue contracts in any line of work, called secondary NAICS codes.

contract...including basic contracts, orders, modifications, and purchase orders” to SBA.

5. Consistently determine whether other small businesses are losing contracting opportunities when awarding contracts through the 8(a) program to ANC firms.

SBA response: SBA stated that it plans to require the contracting agencies to include impact statements in their contract offer letters to SBA.

6. Standardize approval letters for each 8(a) procurement to clearly assign accountability for monitoring of subcontracting and for notifying SBA of contract modifications.

SBA response: SBA agreed with the recommendation but did not indicate an action taken or planned.

7. Tailor wording in approval letters to explain the basis for adverse impact determinations.

SBA response: SBA agreed with the recommendation but did not indicate an action taken or planned.

8. Clarify memorandums of understanding (known as partnership agreements) with procuring agencies to state that it is the agency contracting officer’s responsibility to monitor compliance with the limitation on subcontracting clause.

SBA response: SBA has implemented this recommendation by revising the partnership agreements with the procuring agencies. It added several provisions that delineate the agencies’ responsibilities for oversight, monitoring, and compliance with procurement laws and regulations governing 8(a) contracts, including the limitation on subcontracting clause.

9. Evaluate staffing levels and training needed to effectively oversee ANC participation in the 8(a) program and take steps to allocate appropriate resources to the Alaska district office.

SBA response: SBA stated that the planned Business Development Management Information System should help the Alaska district office more effectively oversee ANC participation in the 8(a) program. It stated that it is providing training to the Alaska district

office. However, no plans were in place to evaluate staffing levels at the office.

10. Provide more training to agencies on the 8(a) program, specifically including a component on ANC 8(a) participation.

SBA response: SBA has provided training to agencies on the revised 8(a) partnership agreements; however, our review of the slides SBA used for the training found no reference to ANC 8(a) firms specifically. According to an SBA official, SBA will include a component on ANC 8(a) participants in future training sessions.

We also recommended that procuring agencies provide guidance to contracting officers to ensure proper oversight of ANC contracts. The procuring agencies generally agreed with the recommendation. Some agencies are waiting for SBA to implement our recommendations before they take their own actions, but others have taken steps to tighten their oversight of contracts with 8(a) ANC firms. The Department of Homeland Security, for example, recently issued an “acquisition alert” requiring that its heads of contracting activities provide guidance and training on the use of 8(a) firms owned by ANCs. The alert provides that use of the authority to award sole-source 8(a) contracts to ANCs must be judicious with appropriate safeguards to ensure that the cost/price is fair and reasonable, that the ANC has the technical ability to perform the work, that the ANC will be performing the required percentage of the work and that the award is in the best interests of the government. The Department of Energy revised its acquisition guidance regarding small business programs to remind contracting officers to use care in awarding and administering ANC contracts, to include notifying SBA of contract modifications and monitoring the limits on subcontracting. The Department also provided training on the 8(a) program, to include contracting with ANC firms. By providing contracting officers with appropriate training on these issues, the government is taking steps to ensure that the ANC firms are operating in the program as intended, thereby mitigating the risk of unintended consequences or abuse of some of the privileges provided to these firms.

This concludes my testimony. I would be happy to answer any questions you may have.

Contacts and Staff Acknowledgements

For further information regarding this testimony, please contact Katherine V. Schinasi at (202) 512-4841 or schinasik@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Key contributors were Michele Mackin, Sylvia Schatz, and Tatiana Winger.

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