

**AUDIT  
REPORT**

**SMALL DISADVANTAGED  
BUSINESS PROGRAM AT THE  
CHICAGO OPERATIONS OFFICE**

**JANUARY 1999**

**DISTRIBUTION OF THIS DOCUMENT IS UNLIMITED**

**MASTER**

## DISCLAIMER

This report was prepared as an account of work sponsored by an agency of the United States Government. Neither the United States Government nor any agency thereof, nor any of their employees, makes any warranty, express or implied, or assumes any legal liability or responsibility for the accuracy, completeness, or usefulness of any information, apparatus, product, or process disclosed, or represents that its use would not infringe privately owned rights. Reference herein to any specific commercial product, process, or service by trade name, trademark, manufacturer, or otherwise does not necessarily constitute or imply its endorsement, recommendation, or favoring by the United States Government or any agency thereof. The views and opinions of authors expressed herein do not necessarily state or reflect those of the United States Government or any agency thereof.

## **DISCLAIMER**

**Portions of this document may be illegible in electronic image products. Images are produced from the best available original document.**



## DEPARTMENT OF ENERGY

Washington, DC 20585

January 25, 1999

### MEMORANDUM FOR THE ACTING MANAGER, CHICAGO OPERATIONS OFFICE

FROM: Terry L. Brendlinger, Manager  
Eastern Regional Audit Office  
Office of Inspector General

A handwritten signature in cursive script, reading "Terry L. Brendlinger", is written over the typed name and title.

SUBJECT: INFORMATION: Audit Report on "Small Disadvantaged Business Program at the Chicago Operations Office"

### BACKGROUND

The Small Business Act (Act) requires that small business concerns owned and controlled by socially or economically disadvantaged individuals have the maximum practicable opportunity to participate in contracts awarded by any Federal agency. Section 8(a) of the Act establishes a program that authorizes the Small Business Administration (SBA) to enter into contracts with other agencies and award subcontracts for performing those contracts to firms enrolled in the 8(a) Program directly to the agencies. Contracts are to be awarded competitively if the anticipated award price of the contract will exceed \$3 million and at least two responsible 8(a) firms could submit offers.

The objective of the audit was to determine whether the Chicago Operations Office (Chicago) was providing the maximum practicable opportunity for small disadvantaged businesses to participate in contract awards.

### RESULTS OF AUDIT

Chicago did not provide the maximum practicable opportunity for small disadvantaged businesses to participate in contract awards. Chicago had 12 contracts with small disadvantaged businesses in June 1998, nine of which were awarded non-competitively. Full and open competition among eligible small disadvantaged firms is essential if one of the most important goals of the program, to achieve the "maximum practicable opportunity," is to be satisfied. Consistent with this goal, the Department's objective should be to cast a "wide net" to ensure that eligible firms are: (i) aware of Departmental procurement opportunities for small disadvantaged firms and (ii) given an opportunity, in a competitive environment, to fully participate in such procurement activities. The approach taken at Chicago, as disclosed by this audit, in essence, discouraged maximum opportunity.

We also found that changes to the terms and conditions of two of the procurements suggest that adjustments were made to reduce the total anticipated costs to a level below the competitive threshold, allowing the contracts to be awarded without competition. This condition existed because Chicago did not require acquisition personnel to comply with all requirements of the Act.

As a result, the goal of the 8(a) program was not fully achieved at Chicago. Further, because of the lack of competition, the Department may have paid more than necessary for services provided by some 8(a) firms. We recommended that the Chicago Acquisition and Assistance Group establish a

policy to (1) require acquisition personnel to comply with the "maximum practicable opportunity" requirements of the Act; (2) prohibit acquisition personnel from modifying the terms or conditions of 8(a) procurements to reduce cost estimates and avoid the requirement to seek competitive bids; and (3) require acquisition personnel to seek competitive bids instead of awarding follow-on contracts to incumbent contractors on a sole-source basis.

#### MANAGEMENT REACTION

Management did not concur with the finding or recommendations, stating that the two examples in the report show Chicago did an outstanding job in negotiating fair and reasonable prices.

Management stated that Chicago used the cost proposals as the basis for negotiating prices that were in the Government's best interest rather than reducing estimates below the threshold for competition.

# **SMALL DISADVANTAGED BUSINESS PROGRAM AT THE CHICAGO OPERATIONS OFFICE**

---

## **TABLE OF CONTENTS**

### **Overview**

|                                   |   |
|-----------------------------------|---|
| Introduction and Objective .....  | 1 |
| Conclusions and Observations..... | 1 |

### **Maximum Practicable Competition**

|                                    |   |
|------------------------------------|---|
| Details of Finding .....           | 3 |
| Recommendations and Comments ..... | 6 |

### **Appendix**

|                             |   |
|-----------------------------|---|
| Scope and Methodology ..... | 7 |
|-----------------------------|---|

## Overview

---

### INTRODUCTION AND OBJECTIVE

The Act requires that small business concerns owned and controlled by socially or economically disadvantaged individuals have the maximum practicable opportunity to participate in contracts awarded by any Federal agency. Congressional policy implementing the Act requires that Federal agencies ensure a competitive economic climate that reduces the concentration of economic resources and expands competition.

Section 8(a) of the Act establishes a program that authorizes the SBA to enter into contracts with other agencies and award subcontracts for performing those contracts to firms eligible for program participation. The SBA has delegated the authority to contract with firms enrolled in the 8(a) Program directly to the agencies. Contracts are to be awarded competitively if the anticipated award price of the contract will exceed \$3 million and at least two responsible 8(a) firms could submit offers.

The Office of Inspector General performed audits of the Small Disadvantaged Business Program at five management and operating contractors in FY 1994.<sup>1</sup> The audits disclosed that none of the contractors fully met the intent of the Act and implementing regulations. The contractors awarded some subcontracts to firms of questionable program eligibility. Also, two of the contractors concentrated awards among a limited number of small disadvantaged businesses, and used procurement practices that precluded opportunities for many small disadvantaged businesses to participate.

The objective of this audit was to determine whether Chicago was providing the maximum practicable opportunity for small disadvantaged businesses to participate in contract awards.

### CONCLUSIONS AND OBSERVATIONS

Chicago did not provide the maximum practicable opportunity for small disadvantaged businesses to participate in contract awards. Chicago had twelve 8(a) contracts with small disadvantaged businesses in June 1998, and only 3 were awarded on a competitive basis. Also, changes to the terms and conditions of two of the procurements suggest that adjustments were made to reduce the total anticipated costs to a level

---

<sup>1</sup> *Audit of Administration of the Department of Energy's Small Disadvantaged Business Program* (Report DOE/IG-0364, December 1994)

---

below the competitive threshold, allowing the contracts to be awarded without competition. This condition existed because Chicago did not require acquisition personnel to comply with all requirements of the Act. As a result, the goal of the 8(a) Program was not fully achieved at Chicago, and the Department may have paid more than necessary for services provided by some 8(a) firms.

The audit identified an issue that management should consider when preparing its yearend assurance memorandum on internal controls.

*Office of Inspector General*  
Office of Inspector General



## Maximum Practicable Competition

### **Three of Twelve Contracts Were Awarded on a Competitive Basis**

As of June 1998, Chicago had 12 open contracts with small disadvantaged businesses enrolled in the 8(a) program with total estimated costs of \$41.2 million. Only 3 of the contracts, valued at \$23.0 million, were awarded on a competitive basis. The other 9 contracts were awarded as sole-source procurements with estimated costs below the \$3 million threshold requiring competition.

Chicago awarded one-third of its 8(a) contracts at amounts minimally below the threshold requiring competition (between \$2,900,000 and \$2,999,999). Further, Chicago had a higher percentage of 8(a) contracts minimally below the competitive threshold than any other operations office or Headquarters procurement activity. Overall, less than 6 percent of the Department's 8(a) contracts awarded by Headquarters and the other 7 operations offices were valued between \$2,900,000 and \$2,999,999. A summary of the procurement organizations and their percentages of 8(a) contracts minimally below the competitive threshold follows.

| <b>Procurement Activity</b> | <b>Total 8(a) Contracts</b> | <b>Total Between \$2,900,000 &amp; \$2,999,999</b> | <b>Percent in Range</b> |
|-----------------------------|-----------------------------|----------------------------------------------------|-------------------------|
| <b>Headquarters</b>         | 89                          | 5                                                  | 5.6                     |
| <b>Albuquerque</b>          | 23                          | 2                                                  | 8.7                     |
| <b>Oak Ridge</b>            | 18                          | 2                                                  | 11.1                    |
| <b>Idaho</b>                | 17                          | 0                                                  | 0.0                     |
| <b>Chicago</b>              | 12                          | 4                                                  | 33.3                    |
| <b>Nevada</b>               | 7                           | 1                                                  | 14.3                    |
| <b>Oakland</b>              | 6                           | 0                                                  | 0.0                     |
| <b>Richland</b>             | 5                           | 0                                                  | 0.0                     |
| <b>Savannah River</b>       | 4                           | 0                                                  | 0.0                     |

Chicago's percentage was more than twice that of any other procurement office, and more than five times the average for the other offices.

Additionally, 3 of the 4 contracts valued between \$2,900,000 and \$2,999,999 were awarded as follow-on contracts to firms that had

performed similar work for slightly more or less than \$3 million in the previous contracts. The contract files did not document any effort to obtain competition for the award of the current contracts, even though 2 of the 3 previous contracts exceeded \$3 million. The following schedule shows the estimated contract values for the current and previous contracts and the current estimates to complete or open obligations for the previous contracts:

| Contract Number | <u>Current Contract</u> | <u>Previous Contract</u> |               |
|-----------------|-------------------------|--------------------------|---------------|
|                 | Estimated Amount        | Estimated Amount         | Current Value |
| 1               | \$2,994,815             | \$2,989,108              | \$3,134,107   |
| 2               | \$2,904,508             | \$2,957,789              | \$2,466,768   |
| 3               | \$2,956,380             | \$2,988,466              | \$3,513,023   |

The previous contracts for Numbers 1 and 2 were awarded by the Headquarters procurement organization. The Headquarters program offices requested that Chicago award the follow-on contracts to the incumbent firms. However, limiting the award of 8(a) contracts to incumbent firms provides no opportunity for other 8(a) firms to compete for the contracts.

#### **Contract Values Were Reduced to Avoid Competition**

Changes to the terms and conditions of two of Chicago's procurements suggest that adjustments were made to reduce the total anticipated costs to a level below the competitive threshold, allowing the contracts to be awarded without competition. One contract was awarded to an incumbent contractor after three Government cost estimates were prepared and submitted by a Headquarters program office. The first estimate was for a 3-year term at a cost of \$2.7 million. The program office decided that a 4-year term would be more appropriate and increased the cost estimate to \$3.2 million. According to the program office's file, Chicago informed the program office that the second estimate was too high and needed to be reduced to an amount below \$3 million to allow the award of the contract, without competition, to the incumbent contractor. The cost estimate was subsequently reduced to \$2,904,508 by lowering the labor rates and using a lower escalation factor for annual increases. After the cost estimate was reduced below \$3 million, the award was made to the incumbent contractor without competition from other 8(a) firms.

---

Another contract was awarded in a similar fashion. The program office requested a cost proposal from the incumbent 8(a) contractor. The contractor estimated total costs at \$4.5 million. Rather than compete the procurement, Chicago reduced the term of the acquisition by 1 year and reduced the total cost estimate below \$3 million. Afterward, the award was made to the incumbent contractor for \$2,956,380 without competition.

**Small Business Act  
Requires Maximum  
Opportunity for Small  
Disadvantaged  
Businesses**

The Act requires that small business concerns owned and controlled by socially or economically disadvantaged individuals have the maximum practicable opportunity to participate in contracts awarded by Federal agencies, including the Department of Energy. The Congressional policy implementing the Act requires that Federal agencies ensure a competitive economic climate that reduces the concentration of economic resources and expands competition. Section 8(a) of the Act states that contracts are to be awarded competitively if at least two responsible 8(a) firms submit offers and the anticipated price of the contract is expected to exceed \$3 million.

**Chicago Did Not  
Enforce the  
Requirements of the  
Small Disadvantaged  
Business Act**

Chicago did not require its acquisition personnel to comply with the "maximum practicable opportunity" requirements of the Act. Chicago had an internal review process for Small Disadvantaged Business Program procurements. However, the review process did not identify any procurements where the terms and conditions were modified to reduce costs below the \$3 million threshold.

**The Program Goal Was  
Not Fully Achieved, and  
the Department May Have  
Paid More Than Necessary  
for Some 8(a) Contracts**

As a result of these conditions, Chicago did not fully achieve the goal of the Small Disadvantaged Business Program, and the Department may have paid more than necessary for the services provided by some 8(a) firms. Chicago exceeded its goal of awarding 15 percent of its contracts to small disadvantaged businesses. However, Chicago did not give small disadvantaged businesses the maximum practicable opportunity to participate in contract awards. Further, the Department may have paid more than necessary for the services provided by some 8(a) firms because the contracts were awarded without the benefit of competition. Had Chicago sought competitive bids instead of awarding contracts to incumbents or sole sources on the basis of a single bid, the competitive forces of the market place might have resulted in lower prices for the Department.

---

## RECOMMENDATIONS

We recommend that the Acting Manager, Chicago Operations Office, direct the Acquisitions and Assistance Group to establish policy to:

1. Require acquisition personnel to comply with the "maximum practicable opportunity" requirements of the Act,
2. Prohibit acquisition personnel from modifying the terms or conditions of 8(a) procurements to reduce cost estimates and avoid the requirement to seek competitive bids, and
3. Require acquisition personnel to seek competitive bids instead of awarding follow-on contracts to incumbent contractors on a sole-source basis.

## MANAGEMENT REACTION

Management did not concur with the finding or recommendations, stating that the two examples in the report show Chicago did an outstanding job in negotiating fair and reasonable prices. Management stated that Chicago used cost proposals as the basis for negotiating prices that were in the Government's best interest rather than reducing estimates below the threshold for competition. Also, management stated that Chicago is frequently approached by various Headquarters program offices to handle their small, support-service type agreements, thereby contributing to a higher percentage of 8(a) contracts awarded at lower dollar levels.

## AUDITOR COMMENTS

We disagree with management's statement that the procurements in the examples were negotiated in the Government's best interest. A fundamental policy of Federal procurement is that competition is to be obtained whenever practicable. Further, it is the responsibility of the contracting officer to make every possible effort to obtain competition in negotiated contracts. Had Chicago accepted the terms and conditions of the procurements discussed in the report without regard to the \$3 million threshold, the procurements could have been competed and the Government's best interests would have been fully protected.

We recognize that Headquarters program offices frequently request that Chicago handle their small, support-service type agreements. This probably accounts for the frequency of contracts awarded for less than \$3 million at Chicago. However, it does not account for the high percentage of 8(a) contracts awarded at prices between \$2.9 million and \$3 million.

## Appendix 1

---

### SCOPE

The audit was performed at the Chicago Operations Office and Headquarters program offices located in Washington, D.C., and Germantown, Maryland, between June 30, 1998, and October 20, 1998. The audit covered small disadvantaged business contracts in effect as of June 15, 1998.

### METHODOLOGY

To accomplish the audit objective, we:

- Reviewed the requirements of the Small Business Act,
- Evaluated Federal and Departmental regulations concerning the award of contracts to small disadvantaged businesses,
- Reviewed procurement files maintained by Chicago's Acquisition and Assistance Group for contracts awarded to small disadvantaged businesses, and
- Interviewed Chicago procurement personnel and Headquarters program office personnel associated with 8(a) contracts at Chicago.

The audit was conducted in accordance with generally accepted Government auditing standards for performance audits, and included such tests of internal controls and compliance with laws and regulations to the extent necessary to satisfy the objective of the audit. Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. We placed minimal reliance on computer generated data, and validated such data when possible.

## CUSTOMER RESPONSE FORM

The Office of Inspector General has a continuing interest in improving the usefulness of its products. We wish to make our reports as responsive as possible to our customers' requirements, and, therefore, ask that you consider sharing your thoughts with us. On the back of this form, you may suggest improvements to enhance the effectiveness of future reports. Please include answers to the following questions if they are applicable to you:

1. What additional background information about the selection, scheduling, scope, or procedures of the audit would have been helpful to the reader in understanding this report?
2. What additional information related to findings and recommendations could have been included in this report to assist management in implementing corrective actions?
3. What format, stylistic, or organizational changes might have made this report's overall message more clear to the reader?
4. What additional actions could the Office of Inspector General have taken on the issues discussed in this report which would have been helpful?

Please include your name and telephone number so that we may contact you should we have any questions about your comments.

Name \_\_\_\_\_ Date \_\_\_\_\_

Telephone \_\_\_\_\_ Organization \_\_\_\_\_

When you have completed this form, you may telefax it to the Office of Inspector General at (202) 586-0948, or you may mail it to:

Office of Inspector General (IG-1)  
Department of Energy  
Washington, DC 20585

ATTN: Customer Relations

If you wish to discuss this report or your comments with a staff member of the Office of Inspector General, please contact Wilma Slaughter at (202) 586-1924.

The Office of Inspector General wants to make the distribution of its reports as customer friendly and cost effective as possible. Therefore, this report will be available electronically through the Internet at the following alternative address:

Department of Energy Human Resources and Administration Home Page  
<http://www.hr.doe.gov/ig>

Your comments would be appreciated and can be provided on the  
Customer Response Form attached to the report.

This report can be obtained from the  
U.S. Department of Energy  
Office of Scientific and Technical Information  
P.O. Box 62  
Oak Ridge, Tennessee 37831