

**PARTICIPATION IN THE 8(A)
PROGRAM BY FIRMS OWNED BY
ALASKA NATIVE CORPORATIONS**

*Report Number: 9-15
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**Prepared by the
Office of Inspector General
U. S. Small Business Administration**

This September 9, 2009 revised version of the Report is the same as the one publicly released on July 10, 2009 except that we have corrected contract information on page 10 and in Appendix II.



U.S. Small Business Administration
Office Inspector General

Memorandum

To: Joseph G. Jordan
Associate Administrator, Government Contracting
and Business Development

Date: July 10, 2009

Jess. B. Knox
Associate Administrator, Office of Field Operations

From: Debra S. Ritt
Assistant Inspector General for Auditing

Subject: Participation in the 8(a) Program by Firms Owned by
Alaska Native Corporations, Report No. 9-15

This is the second report resulting from our audit of Alaska Native Corporation (ANC)-owned participants (ANC participants) in the 8(a) program. Our audit objectives were to: (1) identify 8(a) contracting trends relative to ANC-owned firms; (2) determine whether 8(a) contracting advantages have improved economic opportunities for Alaska Natives; and (3) assess SBA's ability to effectively monitor ANC compliance with program rules.

To identify 8(a) contracting trends, we reviewed Federal 8(a) obligations¹ made to ANC participants for fiscal years (FY) 2007 and 2008 that were reported in the Federal Procurement Data System (FPDS). At the time of the audit, all Federal procuring agencies had not yet certified to the accuracy of the FY 2008 data. We compared the FY 2007 and FY 2008 obligations to those reported for FY 2004 by the Government Accountability Office (GAO).² We also reviewed contract obligations to ANC participants reported by SBA in its *Fiscal Year 2007 Report to the U.S. Congress on Minority Small Business and Capital Ownership Development* to identify the firms receiving the majority of obligations. This was the latest available report and contained information only for active participants.

¹ The term "obligation" refers to the annual expenditure for a particular contract, and not the total award amount.

² GAO-06-399, *Increased Use of Alaska Native Corporations' Special 8(a) Provisions Calls for Tailored Oversight*, April 2006.

Because SBA does not track the volume of sole-source awards, we identified sole-source awards for 11 companies that collectively comprised 50 percent of the total Federal 8(a) obligations that went to ANC-owned firms participating in the program in FY 2007. We identified these awards by analyzing information in FPDS and SBA 8(a) files.

We interviewed officials from the parent companies of these 11 ANC participants to determine how 8(a) revenues were benefitting Alaska Natives and the extent to which the parent companies were involved in managing the ANC firms and overseeing compliance with 8(a) program rules. We also reviewed profit and dividend information in the Alaska Native Claims Settlement Act (ANCSA) Regional Association's *Alaska Native Corporations 2006 Economic Data Report* and the *Alaska Economic Performance Report* for 2007—the two latest reports—that were issued by the Governor of Alaska.

To determine the extent of oversight provided to ANC firms in the 8(a) program, we reviewed SBA policies and regulations governing the 8(a) program and interviewed officials in SBA's Alaska District Office, Office of Government Contracting and Business Development, and Office of Business Development. We also followed up on prior Office of Inspector General (OIG) and GAO audit recommendations related to improvements needed in SBA's oversight of ANC participants. Detailed information concerning our audit scope and methodology can be found in Appendix I. We performed our audit between July 2008 and May 2009 in accordance with *Government Auditing Standards* prescribed by the Comptroller General of the United States.

BACKGROUND

The Small Business Act (the Act) gives SBA authority to oversee and administer the 8(a) program, which was created to help small-disadvantaged businesses compete in the marketplace and to assist them in gaining access to Federal and private procurement markets. To be admitted to the program, a company must meet the eligibility criteria set out in 13 CFR Part 124, including (1) the size criteria to be a small business established in SBA regulations, and (2) the requirement that majority owners be economically and socially disadvantaged individuals.

Participants in the 8(a) program receive special consideration for Federal contracts. For example, the Small Business Act sets a goal for Federal agencies to award 5 percent of all contracting dollars to small-disadvantaged businesses, of which 8(a) firms are a subset. To meet this goal, procuring agencies can award contracts to 8(a) firms competitively or on a sole-source basis up to \$5.5 million for contracts involving manufacturing and up to \$3.5 million for other contracts.

With SBA approval, program participants may also enter into joint venture arrangements with one or more small business concerns for the purpose of performing 8(a) contracts or with large businesses under SBA-approved mentor/protégé agreements. In either case, under SBA regulations, the 8(a) participant must be designated as the managing partner and receive at least 51 percent of the net profits of the venture.

Since 1986, Congress has authorized ANC-owned businesses to participate in the 8(a) program. ANCs were created by ANCSA as the mechanism for distributing land and monetary benefits to Alaska Natives. With ANCSA's passage, Alaska Natives relinquished their land claims for the return promise of the establishment of ANCs, which are state-chartered for-profit corporations, with the ability and resources to advance the real economic and social needs of Alaska Natives. Under ANCSA, an ANC is considered to be owned and controlled by Alaska Natives and to be a minority and economically disadvantaged business enterprise as long as the stock that is held by Natives and their descendants represents a majority of both the total equity of the corporation and the total voting power of the corporation for electing directors. If similar standards are met, subsidiary corporations, joint ventures and partnerships of ANCs are also considered to be native-owned, minority, and economically disadvantaged businesses. Contract awards to these entities may be credited towards Federal goals for small and small-disadvantaged business procurement.

By statute and/or SBA regulation, ANC participants enjoy special procurement advantages beyond those afforded to most other 8(a) businesses.³ These advantages include exemptions from:

- Limits on the number of firms that ANCs can own as long as each business is in a different primary industry.
- The \$5.5 million and \$3.5 million competitive thresholds on the value of individual sole-source contracts an 8(a) firm can receive, which allows ANC participants to receive sole-source awards of any value.
- The cap on sole-source awards for each 8(a) contractor that has received a combined total of Federal 8(a) competitive and sole-source contracts in excess of \$100 million.⁴

³ Most of these advantages are also available to Indian tribes and Native Hawaiian Organizations.

⁴ 13 CFR 124.519.

- The requirement that 8(a) firms be managed by socially and economically disadvantaged owners.⁵

Although the ANCSA assigned responsibility for general oversight of ANCs to the Secretary of the Interior, under the Small Business Act⁶ SBA has oversight responsibility for contracts awarded through the 8(a) program, including those awarded to ANC-owned firms. SBA's Office of Business Development generally oversees the 8(a) program, and SBA's Alaska District Office has primary responsibility for overseeing the ANC-owned businesses that participate in the 8(a) program. As of April 2009, there were 203 ANC participants in the 8(a) program.

In April 2006, GAO issued a report on SBA's oversight of ANC 8(a) participants.⁷ GAO reported that SBA had not tailored its policies and oversight practices to account for ANCs' unique status and growth in the program, even though Agency officials recognized that ANCs typically enter into more complex business relationships than other 8(a) participants. The primary areas where SBA's oversight was cited as falling short involved its monitoring of: (1) secondary lines of business for multiple 8(a) participants owned by a single ANC; (2) changes in ownership of ANC participants and the holding companies that manage them; (3) whether ANC-owned firms have a substantial unfair competitive advantage within an industry; and (4) partnerships between ANC participants and large firms to ensure that they are functioning as intended.

In August 2008, we reported that non-native managers of two 8(a) ANC-owned firms had secured millions of dollars of 8(a) revenue for companies they owned through unapproved management agreements. We also reported that SBA's Alaska District Office did not perform adequate reviews of ANC participants' financial statements and lacked sufficient staff to handle the volume of contract actions and annual reviews for the current number of ANC participants.

RESULTS IN BRIEF

Based on data reported in FPDS, Federal 8(a) obligations to current and former ANC participants have grown by 1,386 percent since FY 2000, and have more than tripled in recent years, from \$1.1 billion in FY 2004 to \$3.9 billion in FY 2008. In FY 2008, obligations to ANC participants represented 26 percent of total 8(a) dollars—an increase from about 13 percent in FY 2004—although ANC

⁵ ANC-owned firms do not have to prove that they are "economically disadvantaged" because ANCSA conveys this status on them. Note: The information was obtained from 13 CFR 124.109 (2), 2008 Edition

⁶ 15 U.S.C. 637(a).

⁷ GAO-06-399, *Increased Use of Alaska Native Corporations' Special 8(a) Provisions Calls for Tailored Oversight*, April 2006.

participants constituted just 2 percent of companies in the 8(a) program and program graduates completing previously awarded 8(a) contracts. Approximately 84 percent of the \$3.9 billion in FY 2008 obligations went to current ANC participants, and 16 percent went to ANC firms that had graduated from the program.

Although the percentage of 8(a) obligations made to ANC firms has increased, the majority of those obligations went to just a few ANC participants, primarily through sole source awards. For example, 50 percent of Federal 8(a) obligations made to current ANC participants in FY 2007 went to just 11 (or 6 percent) of the ANC firms reported by SBA to Congress that year. Further, the ability of ANC firms to obtain unlimited sole-source awards, which is arguably one of the most powerful contracting advantages that ANC firms enjoy, has contributed to the increase in such awards to ANC participants. The top 11 firms received 82 percent of their 8(a) obligations non-competitively.

Even if these ANC contracts had been awarded competitively, rather than on a sole-source basis, it is questionable whether other 8(a) firms could have successfully competed for them as the top 11 ANC participants had access to the resources of their large parent companies, which gave them a competitive advantage over other 8(a) firms. For example, the ANC-owned firms had access to capital, lines of credit, bonding capability, and administrative resources, as well as the management expertise of their parent companies. This may explain why 63 percent of the ANC participants received obligations in FY 2007, while only 44 percent of the non-ANC firms received obligations that year.

As reported by GAO and others, Federal agencies favor sole-sourcing awards to ANC participants because it is a quick, easy, and legal method of meeting their small business goals. However, such awards may not result in the best value for the government and have been discouraged by a recent presidential memorandum unless their use can be fully justified and safeguards put in place to protect taxpayers.

While the playing field is not level for all 8(a) participants, the program has helped ANCs fulfill a mission that is broader than the bottom line of the corporations—namely, to help Alaska Natives achieve economic self-sufficiency. Unlike other 8(a) businesses, whose profits generally go to one or two disadvantaged individuals, the profits from ANCs are shared by hundreds, and sometimes even thousands of tribal members or Native shareholders. A large number of ANC parent companies told us they derive most of their revenue from the 8(a) program, and that profits from those revenues have helped to pay shareholder dividends and fund cultural programs, employment assistance, jobs, scholarships, internships, subsistence activities and numerous other services to the communities where their

shareholders live and work. However, because such benefits are distributed from total ANC profits, which include non-8(a) revenue, they cannot be linked, dollar for dollar, to 8(a) revenue.

The growth in 8(a) obligations to ANC firms and the complexities inherent in their business relationships have challenged SBA's ability to provide effective oversight. For example, the number of ANC subsidiaries in the 8(a) program has grown from 1 subsidiary owned by a single ANC in 1988 to 203 subsidiaries owned by 58 ANCs in 2009. This has made it difficult for SBA to determine whether more than one subsidiary of the same ANC is generating a majority of its revenue in the same primary industry, and to monitor ownership changes to ensure that Alaska Natives maintain their majority ownership in the participant firms. Further, the growth in obligations has made it difficult to monitor ANC partnerships, such as joint ventures, to ensure that the partnerships are functioning as intended. SBA also does not have a management information system that collects all of the information needed to adequately manage ANC participant activity.

Prior GAO and OIG reports have assessed SBA's oversight of ANC participants, and recommended that the Agency revise its policies and procedures to tailor its oversight to account for ANCs' unique status in the program and devote adequate resources to monitor ANC participant activity. However, in the 3 years since GAO issued its report, SBA has implemented only 2 of the 10 recommendations in the report. Also, while the Agency has taken steps to address staffing shortages in the Alaska District Office that were identified by the OIG's previous report, current staffing levels remain insufficient to handle the growth and complexities in ANC participant activity.

While continued contracting assistance may be needed to fulfill the economic goals of ANCSA, increases in 8(a) awards to ANC firms may have resulted in diminished opportunities for other 8(a) participants. For this reason, Congress may want to consider whether ANC-owned firms should continue to be exempt from competitive threshold limits on sole-source awards and whether such awards should be capped. Congress may also want to consider: legislatively clarifying that SBA must determine whether ANC-owned firms have a substantial unfair competitive advantage before exempting them from the size affiliation rules; requiring that ANC 8(a) firms report to SBA on how 8(a) revenues are benefiting Alaska Natives; and revising Federal agencies' small-disadvantaged business procurements goals.

Further, SBA should conduct a program review to evaluate the extent to which the growth in ANC 8(a) participation has or will adversely impact other 8(a) firms and the overall effectiveness of the 8(a) program, and whether firms owned by ANCs

and Indian tribes should continue to be exempt from the cap on total sole-source awards. SBA should also centrally track 8(a) awards to joint ventures involving ANC participants and awards that are sole sourced to ANC-owned firms. Finally, the Agency should: expedite completion of a management information system to increase its capability to oversee ANC participant activity; finalize policies and procedures needed to implement GAO's recommendations; and fully staff the Alaska District Office, as recommended by the OIG.

On July 2, 2009, the Associate Administrator for Government Contracting and Business Development and the Associate Administrator for Field Operations provided written comments, expressing concern with several aspects of the draft report. The Agency's comments generally did not state either agreement or disagreement with the audit findings and recommendations, except that management reported it had implemented five of GAO's recommendations, in contrast to the two we reported. Management also did not identify actions it would take to respond to the audit recommendations in the report. Consequently, we considered management's comments to be non-responsive and have requested that management identify what, if any, steps it will take to implement our audit recommendations. If management is not responsive to our request or does not plan to take action, we plan to pursue implementation of the recommendations through the audit resolution process. Our assessment of management's comments is provided on page 22 of this report.

RESULTS

8(a) Obligations to ANC Participants Have Significantly Increased Since 2000, with a Significant Percentage of the Obligations Being Sole Sourced to a Small Percentage of Firms

Since 2000, Federal obligations to ANC participants have significantly increased, both in value and as a percentage of total obligations to 8(a) firms. These obligations have grown by 1,386 percent since FY 2000, and have more than tripled in recent years, from \$1.1 billion in FY 2004 to \$3.9 billion in FY 2008. In FY 2008, obligations to ANC participants represented 26 percent of total 8(a) dollars—an increase from about 13 percent in FY 2004—even though ANC firms comprised just 2 percent of companies currently in the 8(a) program and program graduates completing previously awarded 8(a) contracts. Of the \$3.9 billion, 84 percent went to current ANC participants, and 16 percent went to ANC firms that had graduated from the program. These trends show that ANC participants are receiving a disproportionate share of Federal obligations to 8(a) firms.

Further, in FY 2007, a significant percentage of 8(a) obligations to ANC participants went to a small percentage of firms through sole-source contracts.

ANC-owned firms are exempt from the cap on sole-source awards that is triggered when total competitive and sole-source 8(a) awards exceed \$100 million, and some of them would not have qualified for these awards without the exemption. While these contracts provided an expedient way for Federal procuring agencies to achieve their small business contracting goals, such awards may not have resulted in the best value for the government.

A Small Percentage of Firms Received the Majority of Federal 8(a) Obligations to ANC Participants in FY 2007

According to SBA's *FY 2007 Report to the U.S. Congress on Minority Small Business and Capital Ownership Development*, approximately 50 percent of Federal 8(a) obligations made to ANC participants in the program that year went to 11 (or 6 percent) of the ANC firms in the program. For example, in FY 2007, \$1 billion of the \$2.2 billion obligated to current ANC participants went to 11 of the 193 ANC firms in the program that year. The top 4 firms, which received collectively about \$600 million, accounted for less than 4 percent of the 109,210 Alaska native shareholders represented by all of the ANC participant firms.

As shown in Table 1 below, one firm accounted for nearly 20 percent of the total Federal 8(a) obligations made to active ANC firms in FY 2007. This firm had 750 shareholders, or less than 1 percent of the total population of ANC shareholders.

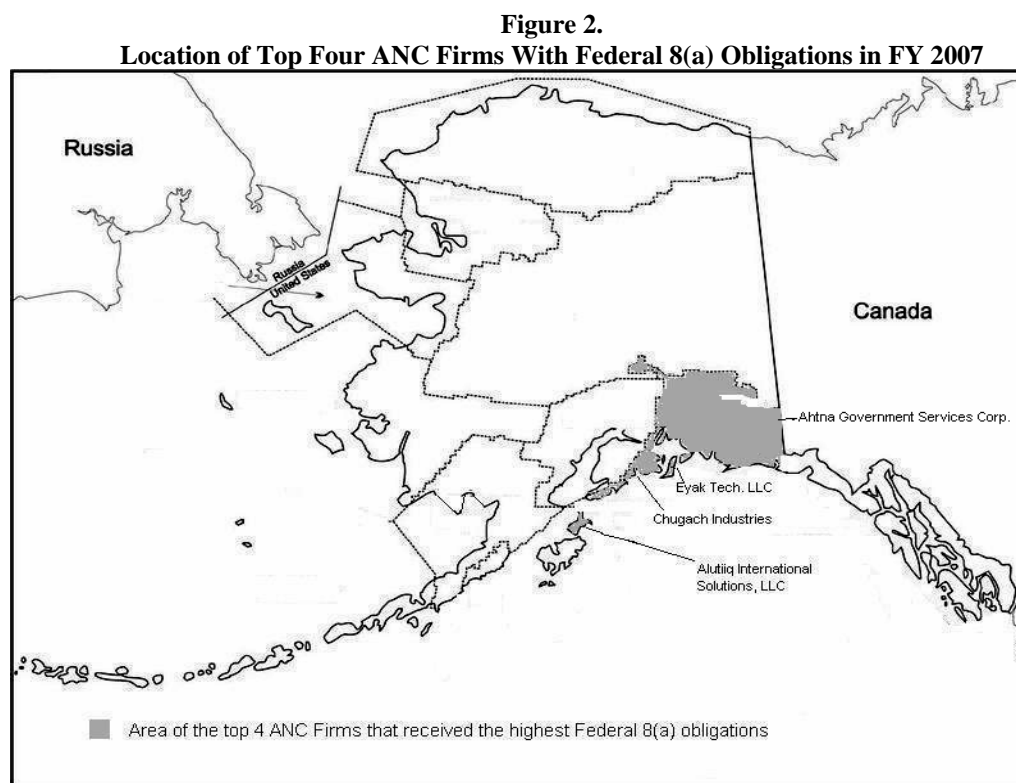
Table 1.
Top 11 ANC Participants with Federal 8(a) Obligations in FY 2007

ANC Participant	8(a) Obligations	Number of Shareholders
Alutiiq International Solutions, LLC	\$206,534,000	750
Eyak Technology, LLC	\$159,419,000	409
Ahtna Government Services Corp.	\$118,628,000	1,200
Chugach Industries, Inc.	\$115,290,000	1,621 ^a
APM, LLC	\$80,013,000	310
Chenega Federal Systems, LLC	\$79,075,000	170
SNC Telecommunications, LLC	\$69,880,000	2,783
ASRC Management Services, Inc.	\$65,795,000	9,000
Tyonek Manufacturing, LLC	\$62,419,000	600
TKC Integration Services, LLC	\$56,849,000	12,000
Bristol Design Build Services, LLC	\$53,885,000	8,000
	\$1,067,787,000	36,843

^a To avoid double counting, we reduced the 2,200 shareholders of Chugach by the 409 individuals who are shareholders of both Eyak and Chugach and the 170 individuals who are shareholders of both Chenega and Chugach.

Source: SBA's *Fiscal Year 2007 Report to the U.S. Congress on Minority Small Business and Capital Ownership Development* and data provided by ANC parent companies.

As shown in Figure 2 below, shareholders of the top four firms were primarily located in the southeastern territories of Alaska.



Source: Generated by the SBA OIG based on data obtained from the ANCs and Alaska Department of Commerce.

A Large Percentage of 8(a) Funds Obligated to ANC Participants Were Sole Sourced

In April 2006, GAO reported that over the 5-year period, from FY 2000 to FY 2004, 77 percent of 6 agencies' obligations to ANCs were sole-sourced. Our audit determined that since FY 2004, sole-source contracts have continued to be a major contracting mechanism for Federal obligations to ANC participants. Although SBA does not compile statistics on sole-source awards, our analysis of the top 11 firms that received almost 50 percent of the 8(a) obligations in FY 2007 showed that 82 percent of their 8(a) obligations, totaling \$847.9 million, were sole-sourced.

As noted in GAO's 2006 report, agencies have turned to ANC-owned 8(a) firms as a quick, easy, and legal method of awarding contracts for any value, which helped them meet their small business contracting goals. Agencies that GAO reviewed reported that they sole-sourced awards to ANCs because they:

- Did not have the staff to administer contracts with full and open competition;

- Had to meet time-sensitive or urgent requirements that were over the competitive limits for other 8(a) firms; or
- Could take credit in more than one small business category in achieving their small business goals.

In February 2008, a report by the Department of Interior OIG reaffirmed that use of sole-source awards to ANC participants was the preferred method for obtaining small-disadvantaged business contracting goals at Interior, which was one of the agencies reviewed by GAO.⁸ The report identified a culture at Interior that valued expediency fueled by a preference for sole-source contracts in meeting its small business contracting goals.

Further, unlike other 8(a) firms, ANC participants and Indian tribes are exempt from the cap on 8(a) sole-source awards that is triggered when total 8(a) awards reach a certain level. This cap, which is set forth in 13 CFR 124.519, precludes 8(a) firms from receiving sole-source awards once they have received any combination of competitive and sole source 8(a) contracts totaling \$100 million.⁹ However, when establishing the cap, SBA exempted firms owned by ANCs and Indian tribes from the \$100 million cap. Consequently, ANC participants are not restricted in the total amount of 8(a) sole source awards they can receive relative to the total value of 8(a) contracts they are awarded. For example, 4 of the 11 ANC participants we reviewed received contracts valued in excess of \$100 million over just the 2-year period, FY 2007 to FY 2008. One ANC participant alone received approximately \$531 million in contracts, of which \$426 million was sole sourced. The regulatory exemption from the cap on sole-source awards allowed this ANC-owned firm to receive all but one of these awards non-competitively. A summary of contract awards made to the 11 ANC participants during FYs 2007 and 2008 is provided in Appendix II.

SBA issued the limits on sole-source awards in response to concerns that a small number of participating firms were receiving a disproportionate percentage of 8(a) contracts. In announcing the rule in a Federal Register notice, the Agency stated

⁸ Report No. W-EV-MOA-0001-2007, *Sole Source Contracting: Culture of Expediency Curtails Competition in Department of the Interior Contracting*, February 2008.

⁹ There are two caps on sole source awards. First, 48 CFR 19.805-1 caps individual sole-source 8(a) awards to \$3.5 million for service contracts and \$5.5 million for manufacturing contracts, unless the award has been accepted by SBA as a sole-source procurement on behalf of a tribally-owned or ANC-owned concern. Second, 13 CFR 124.519 caps sole-source awards to all participants that are not owned by an ANC or Indian tribe once total 8(a) awards (including both sole-source and competitive awards) have reached a certain level. An 8(a) firm with a revenue-based size standard cannot receive additional 8(a) sole-source awards once it has obtained 8(a) awards of either 5 times the amount of its size standard or \$100 million, whichever is less; firms with employee-based size standards are subject to a \$100 million cap.

“the change was designed to promote the equitable distribution of 8(a) contracts to an increased number of 8(a) participants and to foster business development on a wider scale,” but did not explain its reasons for exempting firms owned by ANCs and Indian tribes. As demonstrated by recent contracting trends, the exemption extended to ANC-owned firms has had a paradoxical effect on the distribution of 8(a) awards, as ANC-owned firms are receiving a disproportionate share of 8(a) contract awards.

Further, while sole-sourcing contracts to ANC firms may provide an expedient means of meeting small business goals, due to the lack of competitive bidding, such awards often do not result in the best value for the government. Rather, competition is generally viewed as better protecting taxpayers by driving prices down and quality up. Reports by OIGs and GAO have shown that noncompetitive contracts have been misused, resulting in wasted taxpayer resources, poor contractor performance, and inadequate accountability for results. This was exemplified by a 2007 Department of Homeland Security OIG report, which found that a \$475 million sole-source border security contract to Chenega Technology Services, an affiliate of Chenega Corporation, likely did not provide the government the best value. The contract was awarded under the wrong NAICS code, and 67 percent of the labor cost under the contract was subcontracted out by Chenega, in violation of 8(a) rules.

ANC Participants Who Received the Majority of 8(a) ANC Obligations Had Substantial Advantages over Other 8(a) Firms

The 8(a) program was originally intended to help small-disadvantaged businesses compete in the economy by providing them with business development assistance and Federal contracting preferences. Extending those same preferences to ANC-owned firms, while exempting them from certain 8(a) eligibility and contracting requirements, has provided ANC participants with substantial advantages over other 8(a) firms. Essentially it has created a loophole through which corporate entities that would not otherwise qualify for small business assistance can, without competition, access contracts of unlimited value that have been set aside for small businesses.

Generally, businesses must be small and owned and controlled by one or more socially and economically disadvantaged individuals to be admitted to the 8(a) program. To be considered economically disadvantaged, the owner’s ability to compete in the free enterprise system must be impaired due to diminished capital and credit opportunities when compared with others in the same or similar lines of business that are not socially disadvantaged. However, ANC-owned firms do not have to prove that they are “economically disadvantaged” because ANCSA conveys this status on them.

SBA's size eligibility rules also provide ANC participants with a significant advantage over other 8(a) firms. When determining whether a company is "small," under SBA's size standards, the Agency typically considers the combined number of employees or revenues of the business concern and any other affiliated firms. However, the Small Business Act and SBA regulations contain an exemption for ANC participants, providing that a firm will not be considered to be affiliated with its parent ANC, or other business concerns owned by the ANC, unless the Administrator determines that the business concern has obtained, or is likely to obtain, a substantial unfair competitive advantage in an industry.¹⁰ Therefore, because the revenue and employees of the parent and affiliate companies are not included in the ANC participant's size determination, ANC-owned firms that are large through affiliation are allowed to compete for 8(a) contracts against smaller firms.

Visits to the parent companies of the 11 ANC participants who received the most 8(a) obligations in FY 2007 disclosed that they were predominantly large businesses with significant resources at their disposal. For example, between 2007 and 2009, all 11 ANCs had reached annual revenues of over \$32.5 million, and 7 of the 11 had workforces of over 1,500, which would generally qualify them as large under SBA's size standards. In fact, 6 of the 7 ANCs had revenues in excess of \$500 million. Interviews with the parent corporations confirmed that the ANC participants also had access to the resources of their parents. For example, several of the parent companies told us that they had provided their 8(a) firms with:

- Financial assistance, such as access to capital, lines of credit, and bonding capability;
- Administrative and financial reporting services, which were provided either directly by the parent company or through holding companies that had been established to oversee the ANC participants; and
- Management expertise.

The access that certain ANC participants have to their parent corporations' resources places other 8(a) firms at a disadvantage for awards because they must essentially compete against the resources of the large parent corporations. Consequently, non-ANC 8(a) firms may be losing 8(a) contract opportunities to large ANC companies. This appears to be inconsistent with the original intent of the 8(a) program, which is to benefit small businesses. These disadvantages, along with the growing number of awards to ANC-owned firms, which count

¹⁰ 15 U.S.C. 636(j)(10)(J)(ii)(II); 13 CFR 124.109(c)(2)(iii).

towards procuring agencies' small business contracting goals, raise questions about the extent to which the program is achieving its intended purpose of helping small, disadvantaged businesses.

SBA Has Not Evaluated How ANC Contracting Trends Have Impacted Other 8(a) Participants

Small businesses have complained to SBA and to Congress that contracting advantages for ANC participants have curtailed their ability to compete for Federal contracts. Despite these complaints, SBA has not evaluated how ANC contracting trends have impacted other 8(a) firms, the overall effectiveness of the program, or the achievement of agency small-disadvantaged business procurement goals.

For example, annually, SBA negotiates with Federal agencies concerning their prime contracting goals for small and disadvantaged businesses to ensure that small businesses have the maximum practicable opportunity for Federal contracts. In reporting goal achievement, however, awards made to 8(a) firms owned by ANCs are counted, although these firms are technically large through affiliation with their parent companies. Given the growth in ANC 8(a) activity, procuring agencies may be achieving their small-disadvantaged business goals largely through sole-source awards to ANC firms. However, SBA has not assessed the manner in which the goals are being met to ensure that other 8(a) companies are provided maximum opportunity to obtain 8(a) contracts.

Additionally, the growing share of 8(a) obligations going to ANC participants, particularly in certain industry categories raises questions about how such growth has impacted other participants and the overall effectiveness of the 8(a) program. For example, in FY 2008, ANC participants received 66 percent of 8(a) obligations made under the "facilities support services" NAICS code,¹¹ which was the second largest industry code for 8(a) purchasing in 2008. Despite these trends and other concerns, SBA has not conducted a study to determine whether the increase in ANC contracting activity has harmed other 8(a) firms and overall program performance.

Based on a 2005 Program Assessment Rating Tool (PART) evaluation of the 8(a) program by the Office of Management and Budget (OMB), which was updated in 2008, the effectiveness of the 8(a) program was rated as adequate. An adequate rating indicates that the program is performing, but needs to set more ambitious goals, achieve better results, or strengthen its management practices. For example, only 8 percent of the over 9,500 small businesses participating in the program at

¹¹ NAICS 561210.

the end of FY 2007 were expected to get contracts. Moreover, the PART evaluation found that SBA had not undertaken independent evaluations of the program to measure its effectiveness and had not regularly collected timely and credible performance information needed for such evaluations. Given the growth in sole source awards to ANC participants, evaluations of whether such growth has impacted other participants, as well as the overall effectiveness of the 8(a) program, would provide SBA with critical information to help it administer the program.

ANCs Are Heavily Reliant on the 8(a) Program to Provide Economic Assistance to Alaska Natives

According to the Association of ANCSA Regional Corporation Presidents, ANCs were established to build economic self-sufficiency, while addressing the social and cultural needs of Alaska Natives. Federal contracts awarded through the 8(a) program are one of a number of sources of revenue for ANC participants. Unlike other 8(a) businesses, whose profits generally go to one or two individuals, the profits from ANCs are shared by hundreds, and sometimes thousands, of tribal members or Native shareholders.

ANCs use their profits to fulfill a mission that is broader than the bottom line of the corporations. For example, in addition to paying dividends to shareholders, ANC profits fund cultural programs, employment assistance, jobs, scholarships, internships, subsistence activities, and numerous other services to the communities where shareholders live and work. ANCs must also fulfill ANCSA obligations that saddle them with expenses of land selection, land management, maintenance of shareholder records, and annual audits.

While not all ANCs have generated profits in the past, in recent years the overall financial performance of ANCs has significantly improved. According to the *ANCSA Regional Association's 2006 Report*, in 2006 total revenues for 13 regional ANCs grew 22 percent, from \$4.4 billion in 2005 to \$5.4 billion in 2006, and profits increased by 75.6 percent, from \$282.4 million in 2005 to \$495.9 million in 2006. Approximately \$1.8 billion of the revenues earned in 2006 came from Federal 8(a) contracting preferences, which represented a 32-percent growth in 8(a) revenue as compared to 2005. The regional corporations paid out \$104.6 million in dividends to their shareholders—a 36.8 percent increase from the previous year. The ANCSA Regional Association's report shows that some of the other profits were invested in scholarships and other assistance for Alaska Natives.

While the ANCSA Regional Association did not issue a similar report for 2007 or 2008, the Alaska Governor issued the *Alaska Economic Performance Report for*

2007, which showed that revenues for 12 of the 13 regional corporations totaled \$5.77 billion, with profits of \$483.7 million. ANC shareholders were paid dividends from those profits ranging from \$1.00 per share to \$58.55 per share.

The majority of the parent corporations of the 11 ANC participants receiving most of the 8(a) obligations in 2007 advised us that they continue to rely heavily on the 8(a) program to fund shareholder benefits. Eight of the ANCs told us they derived at least 50 percent or more of their revenues from the 8(a) program, with two relying on the program for 90 percent or more of their revenues. These firms advised that they paid out the majority of their profits in dividends to shareholders. For example, in 2007, Bristol Bay paid \$5.9 million in dividends to its 8,000 shareholders, \$235,000 for social and educational programs, and \$2.7 million in shareholder wages. Another large ANC, the Northwest Alaska Native Association (NANA), paid \$35 million in dividends to its 12,000 shareholders, \$33 million to its elders' trust fund, \$8 million for social and educational programs, \$1 million in shareholder development, and \$41 million in wages to shareholders who worked for the ANC. Other ANCs, however, paid little or no dividends. While these numbers show that ANC participation in the 8(a) program has benefited certain Alaska Natives, dollar for dollar, it is difficult to link these benefits to revenues earned from the 8(a) program, as they are financed from profits that have been generated by different revenue sources.

Growth in ANC Participation Has Created Oversight Challenges for SBA

The growth in 8(a) awards to ANC firms and the complexities inherent in their business relationships have presented challenges for SBA in overseeing the activities of the ANC participants in the program. As highlighted in recent GAO and OIG reports, the practice of ANCs creating multiple subsidiaries has increased the volume of affiliate businesses that the Agency must monitor. Additionally, partnerships between ANCs and other individuals, as well as frequent changes in ownership, have challenged the Agency's ability to ensure that benefits flow to the intended participants. Although SBA officials recognize that ANCs enter into more complex business relationships than other 8(a) participants, it has not tailored its oversight to account for the unique status enjoyed by ANC-owned firms and their growth in the program, or the role that ANC parent corporations play in ensuring compliance with 8(a) program rules.

Some of the areas where GAO and/or the OIG have found SBA's oversight to have fallen short include:

- Determining whether more than one subsidiary of the same ANC is operating in the same primary industry category;

- Identifying and approving changes in ownership of ANC participants and the holding companies that manage them;
- Determining whether ANC firms, when entering the program or at the time of each contract award, have or are likely to have a substantial unfair competitive advantage within an industry;
- Ensuring that partnerships between ANC participants and large firms are functioning as intended; and
- Reviewing participant financial statements to determine whether they have entered into unapproved management agreements involving their 8(a) contracts.

Although SBA agreed to address most of these shortcomings in its responses to previous GAO and OIG reports, it has made few adjustments to its oversight activities to recognize that ANCs require special attention or that parent companies play a significant role in managing the participant firms. For example, in the 3 years since GAO issued its report, the Agency has implemented only 2 of the 10 recommendations made by GAO. Further, it has not fully addressed staffing shortages in its Alaska District Office, which is the office that has primary responsibility for overseeing ANC participants. SBA's responses to the recommendations made by GAO and the OIG are discussed below.

SBA is Not Tracking Secondary Lines of Business for Multiple 8(a) Participants Owned by a Single ANC

SBA regulations limit the number of ANC participants owned by the same parent company that are allowed to operate in the same primary NAICS codes, representing the same line of business. However, as reported by GAO in 2006, one of the key practices of ANCs is the creation of multiple 8(a) subsidiaries. For example, GAO reported that from FY 1988 to 2005, ANC 8(a) subsidiaries increased from 1 subsidiary owned by a single ANC to 154 owned by 49 ANCs. Today, there are 203 subsidiaries owned by 58 ANCs. In addition, we found that many of the parent companies of the 11 ANC participants we reviewed routinely established new 8(a) firms when existing ANC firms graduated, as shown in Table 2 below.

Table 2.
Number of Graduated and Current ANC Participants in the 8(a) Program
Since 2000 for the 11 ANCs Reviewed

ANC Name	As of	2000 - 2005		2006 - 2008		As of
	12/31/99	Entered	Exited	Entered	Exited	12/31/08
	Active					Active
Afognak Native Corp.	0	6	2	3	1	6
Ahtna, Inc.	4	2	2	3	2	5
Arctic Slope Native Corp	5	5	2	3	4	7
Bristol Bay Native Corp.	2	5	1	10	1	15
Cape Fox Corporation	0	4	0	3	1	6
Chenega Corp.	3	4	2	2	1	6
Chugach Alaska Corp.	3	3	4	2	2	2
Eyak Corporation	0	3	0	0	0	3
NANA Regional Corp.	2	13	1	7	3	18
Sitnasauk Native Corp.	2	1	2	1	0	2
Tyonek Native Corp.	3	5	1	2	4	5
TOTAL	24	51	17	36	19	75

Source: Generated by the OIG based on data provided by SBA's Alaska District Office.

As shown in Figure 3 below, one of the 11 ANCs had as many as 18 subsidiaries in the 8(a) program.

Figure 3. Corporate Structure of NANA Regional Corporation as of 12/31/08

NANA REGIONAL CORPORATION (NRC)																																													
NANA Development Corp. (NDC) (Holding Company)	Subsidiaries of NANA Development Corp.																																												
	<table border="1"> <tr> <td>1. KI Prof. Services Group, LLC</td> <td>Subsidiaries of KI Professional Services</td> </tr> <tr> <td>2. ASCG Incorporated</td> <td>1. Five Rivers Services, LLC (8a)</td> </tr> <tr> <td>3. DOWL, LLC</td> <td>2. KI, LLC (8a)</td> </tr> <tr> <td>4. NANA/Colt Engineering, LLC</td> <td>3. Wolverine Services, LLC (8a)</td> </tr> <tr> <td>5. NANA Management Services, LLC</td> <td></td> </tr> <tr> <td>6. Qivliq, LLC (90% NDC) **</td> <td>Subsidiaries of Qivliq, LLC</td> </tr> <tr> <td>7. Courtyard by Marriott</td> <td>1. TKC Communications, LLC ***</td> </tr> <tr> <td>8. Residence Inn by Marriott</td> <td>2. Truestone, LLC (8a)</td> </tr> <tr> <td>9. Springhill Suites by Marriott</td> <td>3. TKC Integration Services, LLC</td> </tr> <tr> <td>10. Nullagvik, LLC</td> <td>4. Nakuuruq Solutions, LLC (8a) **</td> </tr> <tr> <td>11. NANA Dynatec Mining, LLC</td> <td>5. SAVA Workforce Solutions, LLC (8a) **</td> </tr> <tr> <td>12. NANA/Lynden Logistics, LLC</td> <td>6. Synteras, (8a)</td> </tr> <tr> <td>13. NANA Major Drilling, LLC</td> <td>7. Cazador Apparel, LLC (8a)</td> </tr> <tr> <td>14. NANA Oilfield Services, Inc.</td> <td>8. TKC Global Solutions, LLC (8a)</td> </tr> <tr> <td>15. WorkSafe, Inc</td> <td>9. Portico Realty Services, LLC (8a)</td> </tr> <tr> <td>16. Akima Management Services, Inc. (80% NDC)**</td> <td>Subsidiaries of Akima Management Services, Inc.</td> </tr> <tr> <td>17. Red Dog Mine</td> <td>1. Akima Corporation</td> </tr> <tr> <td>18. Professional Services Group, LLC</td> <td>2. Akima Intra-Data, LLC (8a)</td> </tr> <tr> <td></td> <td>3. Akima Construction Services, LLC (8a)</td> </tr> <tr> <td></td> <td>4. Akima Infrastructure Services, LLC (8a)</td> </tr> <tr> <td></td> <td>5. Akima Facilities Management, LLC (8a)</td> </tr> <tr> <td></td> <td>6. Akima Logistics Services, LLC (8a)</td> </tr> </table>	1. KI Prof. Services Group, LLC	Subsidiaries of KI Professional Services	2. ASCG Incorporated	1. Five Rivers Services, LLC (8a)	3. DOWL, LLC	2. KI, LLC (8a)	4. NANA/Colt Engineering, LLC	3. Wolverine Services, LLC (8a)	5. NANA Management Services, LLC		6. Qivliq, LLC (90% NDC) **	Subsidiaries of Qivliq, LLC	7. Courtyard by Marriott	1. TKC Communications, LLC ***	8. Residence Inn by Marriott	2. Truestone, LLC (8a)	9. Springhill Suites by Marriott	3. TKC Integration Services, LLC	10. Nullagvik, LLC	4. Nakuuruq Solutions, LLC (8a) **	11. NANA Dynatec Mining, LLC	5. SAVA Workforce Solutions, LLC (8a) **	12. NANA/Lynden Logistics, LLC	6. Synteras, (8a)	13. NANA Major Drilling, LLC	7. Cazador Apparel, LLC (8a)	14. NANA Oilfield Services, Inc.	8. TKC Global Solutions, LLC (8a)	15. WorkSafe, Inc	9. Portico Realty Services, LLC (8a)	16. Akima Management Services, Inc. (80% NDC)**	Subsidiaries of Akima Management Services, Inc.	17. Red Dog Mine	1. Akima Corporation	18. Professional Services Group, LLC	2. Akima Intra-Data, LLC (8a)		3. Akima Construction Services, LLC (8a)		4. Akima Infrastructure Services, LLC (8a)		5. Akima Facilities Management, LLC (8a)		6. Akima Logistics Services, LLC (8a)
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3. Kisaq, LLC (8a)																																													
4. ASTS, Inc.																																													

** Ownership shared with another ANC
 *** Majority owner of a joint venture firm

Source: Generated by SBA OIG using data obtained from SBA's Alaska District Office and Audited Financial Statements of NANA Regional Corporation.

The growth in subsidiaries has made it difficult for SBA to monitor compliance with the regulatory restriction on the number of ANC subsidiaries that are certified in the 8(a) program under the same primary NAICS codes. GAO has reported that SBA's oversight has fallen short in that it does not track the business industries in which ANC subsidiaries have 8(a) contracts. Thus, GAO reported that SBA is not ensuring that a firm's secondary NAICS codes do not, in effect, become the primary business line by generating the majority of revenue. This situation could allow an ANC to have more than one 8(a) subsidiary perform most of its work under the same primary NAICS code, which SBA regulations limit.

GAO recommended that SBA collect information on ANC participants as part of required overall 8(a) monitoring, to include tracking the primary sources of revenue for ANC participants to ensure that multiple subsidiaries under one ANC are not generating most of their revenue in the same primary industry. In responding to GAO, SBA indicated that it was developing a Business Development Management Information System (BDMIS) to electronically manage all aspects of the 8(a) program, which would have such tracking capability. This project was launched on July 28, 2008, but is not yet completed. Consequently, SBA still does not have an automated means of track primary revenue generators for ANC participants. SBA's Director of Business Development also told us that the Agency identifies ANC participant revenue sources during the annual review process, but does not link those revenues back to industry codes to establish whether an ANC's subsidiary firms are generating most of their revenue in the same primary industry.

SBA Is Not Always Identifying Changes in Ownership of ANC Participants and Holding Companies

SBA regulations require that ANC participants be majority-owned by an ANC or a wholly-owned entity of an ANC, such as a holding company.¹² ANCs must seek approval from SBA before changing ownership of the 8(a) participant. Ownership of the ANC subsidiaries and holding companies require constant monitoring by SBA to ensure that Alaska Natives continue to own the required share of these companies. However, the growth in ANC subsidiaries and creation of holding companies has strained SBA's ability to adequately monitor ownership changes. According to the Director of SBA's Alaska District Office, ownership changes occur so frequently that her staff has had difficulty keeping up with the volume of changes it must approve. She also told us that this activity consumes the majority of her staff's time, precluding them from monitoring other aspects of ANC compliance with 8(a) rules.

The large volume of ownership change requests requiring review and approval has also left little time for staff to monitor the ownership structure of ANC-owned firms to identify ownership changes that have not been reported to SBA, as required. For example, our last audit report identified an instance that had not been reported to SBA where an owner of a former 8(a) company had purchased a 45-percent ownership interest in an ANC participant. This level of ownership was in violation of SBA's regulation, which restricts former 8(a) participants from having more than a 20-percent equity ownership in a current 8(a) participant.¹³ While this change of ownership was disclosed in notes to the participant's

¹² 13 CFR 124 105(i).

¹³ 13 CFR 124 105(h)(2).

financial statements, it went undetected because the district office did not thoroughly review this financial information as part of its annual review of the participant firm.

The Agency Is Not Determining Whether ANC Firms Have or Are Likely to Have a Substantial Unfair Competitive Advantage within an Industry

GAO reported that the Agency was not complying with statutory and regulatory requirements when evaluating the size of ANC-owned firms¹⁴ for entrance into the 8(a) program and acceptance of 8(a) contracts. The Small Business Act states that “in determining the size of a small business concern owned by a socially and economically disadvantaged Indian tribe (or wholly owned business entity of each tribe) each firm’s size shall be independently determined without regard to its affiliation with the tribe, any entity of the tribal government, or any other business enterprise owned by the tribe, *unless* the Administrator determines that one or more such tribally owned business concerns have obtained, or are likely to obtain, a substantial unfair competitive advantage within an industry category.” GAO found that, while SBA had incorporated this language into its 8(a) regulations, it was not making determinations as to whether these business concerns had obtained, or were likely to obtain, a substantial unfair competitive advantage. In fact, GAO found that the Agency had no policy or procedures in place to make these determinations.

SBA officials told GAO that the statute was confusing and that they were not sure how to implement it. Further, they did not expect that an ANC would have a substantial unfair competitive advantage in one industry because the amount of ANC participation in Federal contracting was so minimal. GAO reported that it did not understand how SBA could ignore the fact that Congress had directed it to make such determinations specifically for ANC firms. GAO also recommended that SBA ascertain and clearly articulate in regulation how it would comply with existing law to determine whether and when one or more ANC firms were obtaining, or were likely to obtain, a substantial unfair competitive advantage in an industry. In initially responding to the recommendation, SBA wrote in June 2007 that it was 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 limitations to joint ventures between tribally and ANC-owned 8(a) firms and other business concerns.

While SBA’s response would have closed a loophole that allows ANC participants to joint venture with large businesses on sole-source contracts of unlimited value, which potentially has given them a substantial unfair competitive advantage, it

¹⁴ These requirements also apply to all Indian tribes.

was never implemented. Since that time, SBA has adopted a different approach, which involves training its Business Development Specialist (BDS) staff and Federal agencies to ensure that a previous procurement history is provided in offer letters to facilitate such determinations. However, this approach does not appear to address GAO's recommendation that SBA should issue a regulation stating how it will determine substantial unfair competitive advantage.

SBA Is Not Monitoring Partnerships between ANC Participants and Large Firms to Ensure that They Are Functioning as Intended

As discussed previously, ANC 8(a) firms may create partnerships, such as joint ventures and mentor-protégé arrangements, with individuals or other businesses by entering into business agreements, which can complicate the oversight process. SBA is required to approve partnerships between the 8(a) and other firms to ensure the agreements will be of substantial benefit to the 8(a) concern. Under the 8(a) program, the ANC participant must manage the joint venture and receive at least 51 percent of venture profits. SBA requires joint ventures to submit quarterly financial statements and a final report at the end of the venture's term so that it can determine whether the required share of venture profits went to the ANC participant.

GAO reported that it found indications that oversight of these partnerships may not be adequate, particularly in the context of ANCs' unique provisions and large businesses wanting to take advantage of those provisions. GAO reported instances where mentors abandoned the ANC participant when a contract was not won or where the ANC participant believed the mentor firm exploited it for its 8(a) status. It also reported instances where SBA did not inquire as to whether partnerships were working as intended. SBA acknowledged that joint ventures between mentors and their protégés may be inappropriate for 8(a) sole source contracts above competitive thresholds set for other 8(a) firms. This acknowledgement was based on complaints that non-8(a) firms have received substantial benefits through the performance of large sole-source 8(a) contracts as joint venture partners with 8(a) ANC participants. Further, where the joint venture involves a large business mentor, SBA recognized a perception that large businesses may be unduly benefitting from the 8(a) program.

Despite these concerns, our audit revealed that neither SBA headquarters nor any of its other district offices were adequately monitoring the performance of joint venture contracts involving ANC participants and large businesses to ensure that they were functioning as intended. In addition, SBA headquarters was unable to identify the number of joint ventures that existed, including those involving ANC participants. Similarly, SBA headquarters did not have a central tracking system to identify which 8(a) sole source contracts involved joint venture partners. SBA

believes that BDMIS, once fully implemented, will provide the capability needed to oversee ANC program participation.

SBA Did Not Identify Management Agreements Involving ANC Participant 8(a) Contract Revenues

Our August 2008 report on the oversight of two ANC participants highlighted weaknesses in SBA's review of financial information reported annually by program participants. For example, because SBA was not carefully reviewing participant financial statements, it did not discover that non-native managers of two ANC firms received over \$23 million out of \$109 million in 8(a) revenues through business agreements that were not disclosed or approved by SBA. The financial statements that had been submitted to the Agency disclosed that firms had management agreements with their non-native managers. SBA should have detected and requested copies of these agreements to determine how they impacted the participants' continued eligibility in the 8(a) program and eligibility for contract awards.

Our report questioned whether the staffing of the Alaska District Office, which has oversight responsibility for the majority of ANC participants, was sufficient to handle the volume of contract actions and complexity of annual reviews for the current level of ANC participants. At the time of the audit, the office was staffed with only two full-time and one part-time BDS to oversee over 200 8(a) participants, of which 166 were ANC-owned firms.

In responding to our report, SBA agreed to re-evaluate staffing needs for the Alaska District Office. Using a recent workforce analysis, SBA determined that each BDS in the Alaska District Office should manage a workload of no more than 40 participants. According to the Director of Business Development, two new BDS positions have been approved for the Alaska District Office which, if implemented, should provide for more effective reviews.

CONCLUSIONS

Long-term 8(a) contracting trends show a continued and significant increase in obligations to ANC-owned participants, many of which were made through sole-source contracts. This growth suggests that the special advantages afforded ANC participants may be limiting the number of non-ANC disadvantaged firms that secure 8(a) contracts. In addition, while the 8(a) program is undeniably benefiting Alaska Natives, our audit showed that a few ANC participants received a disproportionate share of the 8(a) obligations. Further, because studies have shown that sole-source contracts do not always provide the Government with the

best value, it is questionable whether ANC contracting advantages under the 8(a) program are the most cost-effective way of assisting Alaska Natives.

Although designated by statute as disadvantaged, many ANC firms have clear advantages over other 8(a) program participants when competing for contracts due to their association with their large parent corporations and affiliates, which often provide them access to capital and credit as well as management expertise. Requiring non-ANC small businesses to compete against these ANC participants appears to be inconsistent with the primary purpose of the 8(a) program of helping small-disadvantaged firms develop the skills needed to compete in the American economy. However, SBA has not undertaken a program review to determine whether ANC participation is adversely impacting other 8(a) participants. Further, the Agency has been slow to expand and fully staff its oversight capabilities to address the complex nature of ANC business relationships and ANC growth in the program.

MATTERS FOR CONGRESSIONAL CONSIDERATION

Congress may wish to consider whether:

1. ANC-owned firms should continue to be exempt from the competitive threshold limits on the amount of individual sole-source awards, or whether there should be a statutory cap on the total amount of sole-source awards they may receive.
2. The Small Business Act should be clarified to require SBA to determine that ANC-owned firms do not have a substantial unfair competitive advantage within an industry category before exempting ANC participants from size affiliation rules, or whether other limits should be placed on the affiliation rules applicable to ANC participants.
3. ANCs should be required to submit regular reports to SBA identifying the percentage of its profits that are derived from 8(a) contracts, describing how the 8(a) share of its profits are being distributed in dividends or other support for Alaska Natives, and explaining how the distributed benefits assisted the Natives.
4. The Small Business Act should be amended to either establish larger small-disadvantaged business contracting goals for procuring agencies that account for the growth in ANC 8(a) awards and; or establish a separate goal for awards to tribally-owned companies to ensure that other 8(a) companies are provided maximum opportunity to obtain 8(a) contracts.

RECOMMENDATIONS

We recommend that the Associate Administrator for Government Contracting and Business Development take the appropriate steps to:

1. Conduct a program review to evaluate whether the growth in ANC 8(a) obligations has adversely impacted, or will adversely impact, other 8(a) firms and the overall effectiveness of the 8(a) program and, if so, make programmatic revisions to minimize the adverse impact.
2. As part of this program review, determine whether 8(a) firms owned by ANCs and tribes should continue to be exempt from the cap on total sole source awards in CFR 124.519 and, if not, remove the exemption from this regulation.
3. Centrally track the award of 8(a) contracts to joint ventures involving ANC participants and the award of sole-source contracts to ANC participants.
4. Expedite the implementation of BDMIS to ensure that the Agency has timely and credible performance information needed to oversee ANC participant activity.
5. Finalize regulations and actions needed to fully implement GAO's recommendations.

We recommend that the Associate Administrator for Field Operations take the appropriate steps to:

6. Fully staff the Alaska District Office to ensure that adequate oversight of ANC participants is provided.

AGENCY COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE

On June 8, 2009, we provided a draft of the report to SBA's Office of Government Contracting and Business Development and Office of Field Operations for comment. On July 2, 2009, the Associate Administrator for Government Contracting and Business Development and the Associate Administrator for Field Operations provided written comments, which are contained in their entirety in Appendix III.

The Agency neither expressed agreement or disagreement with the audit findings and recommendations, with one exception (see comment 8 below). Further,

management did not indicate whether or not it plans to implement the six audit recommendations from this report. Therefore, we do not consider management's comments to be responsive to the recommendations, and have requested that the Agency identify the actions it plans to take on each audit recommendation. If the Agency is not responsive to our request or does not agree to take action, we plan to seek a decision on the recommendations through the audit resolution process.

Finally, in its written comments, SBA took issue with several aspects of the report. SBA's comments and our evaluation of them are summarized below.

Management Comments

Comment 1 – OIG Report Repeats Findings from GAO Report

Management stated that the report is primarily repeating the GAO report from 2006, the exception being a review of contracting activities of a small sample of 11 ANCs.

OIG Response

Our audit was conducted in accordance with *Government Auditing Standards*, which provide that auditors should determine whether other auditors have completed work related to the objectives of the current audit.¹⁵ It also provides that prior audits conducted by others may be used to support findings or conclusions for the current audit. Consequently, we determined that GAO's 2006 report on *Increased Use of Alaska Native Corporations' Special 8(a) Provisions Calls for Tailored Oversight*, which provided information on SBA's oversight of ANC 8(a) activity, was relevant to our audit objectives. As a result, our audit appropriately followed-up on actions taken by SBA on GAO's recommendations.

In addition to the GAO information, the audit presents new information on recent obligations made to ANC 8(a) firms, the number of ANC 8(a) firms receiving the majority of obligations made to ANC participants, the percentage of obligations made to ANC participants through sole-source contracts, and the regulatory and statutory provisions that convey special contracting preferences on ANC participants. The report also provides new information on ANC participant reliance on the 8(a) program and how Alaska Natives have benefited from the special contracting advantages afforded ANC-owned firms under the 8(a) program.

Comments 2 and 3 – Report Does Not Discuss Contract Activity of other Program Participant Groups or Indicate that All Had Increased Contracting Activity

¹⁵ GAO-07-731G, *Government Auditing Standards*, Section 7.41 and 7.42, issued July 2007.

Management expressed concern that the report did not provide an analysis of contract activity of the other program participant groups within the 8(a) program or acknowledge that all groups had increased contract activity.

OIG Response

The scope of the audit was limited to ANC participants. While other participant groups may have had increased contract activity in terms of absolute dollars awarded, one of the key findings of this report was that the *percentage* of 8(a) contracts awarded to ANC-owned participants had gone up from 13 percent in 2004 to 26 percent in 2008, a significant increase. Much of the increase was due to the use of large, sole-source contracts to ANC-owned companies. As more of the percentage of the small-disadvantaged business goal is attributed to ANC-owned companies, there will be less contracting opportunities for other companies in the 8(a) program. Because of this, we have added as another matter for Congress to consider that it amend the small-disadvantaged business goal in the Small Business Act by either increasing the overall goal or establishing a separate goal for tribally-owned companies.

Comment 4 – Report Does Not Mention that Contracting Officers Must Certify that Awards Provide Best Value or Reasonable Price

Management stated that the report did not mention that contracting officers must certify that any award, including those made to ANCs, represent a fair and reasonable price and/or best value to the Federal government.

OIG Response

While we agree that contracting officers must make such a certification for each award, other OIGs and GAO have reported that noncompetitive contracts have been misused, resulting in wasted taxpayer resources, poor contractor performance, and inadequate accountability for results.

Comment 5 – Report Does Not Cite Any Contracts with ANC Firms that Did Not Meet the Government’s Expectations

Management stated that not one contract awarded to an ANC was cited in the report for not meeting the government expectation.

OIG Response

We disagree with management’s assertion. The report discusses an award made by the Department of Homeland Security to Chenega Technology Services, which likely did not provide the government with the best value. The contract was

awarded under the wrong NAICS code, and 67 percent of the labor cost under the contract was subcontracted out by Chenega, in violation of 8(a) program rules.

Comment 6 – Sole-Source Awards to ANC, Tribal and Native Hawaiian Organizations Helps Them to Compete Against Large Businesses

Management commented that the ability of ANC, Tribal and Native Hawaiian organizations to get unlimited sole-source awards helps them compete against large businesses.

OIG Response

We do not believe, as management suggests, that all sole-source awards to ANC participants would have gone to large businesses had ANCs not been exempted from the competitive thresholds on sole-source contracts, or that other 8(a) firms were not adversely impacted. The Agency's response is neither supported by analysis or discussion with procuring agencies.

We believe that if such awards had been competed, other 8(a) firms may have been able to compete for some of them (depending on the size of the award) or may have entered into joint venture arrangements to compete for the larger contracts. In evaluating management's response, we contacted managers in SBA's district offices, who interact with small businesses daily, to get their assessment of whether sole-source awards to ANC 8(a) firms were adversely impacting other small businesses in their areas. Twenty district offices that service ANC participants provided us examples where small businesses reported that they had missed out on contracts that were ultimately awarded to ANC firms. Of note is that several companies serviced by the Alabama, El Paso, Montana, North Carolina, North Dakota, Oregon, Santa Ana, South Carolina, and Syracuse district offices reported that ANC firms were getting sole-source contracts in their lines of business for which they could have competed.

A recent legal decision by GAO also provides further evidence that 8(a) firms are losing opportunities to ANC-owned firms.¹⁶ On May 4, 2009, GAO rendered a decision on a protest regarding a sole-source award made to an ANC firm. The award was being protested by Mission Critical Solutions, an 8(a) firm located in a historically underutilized business zone. On January 2008 the Army had awarded a 1-year contract to Mission Critical Solutions for \$3.45 million for IT support services. Near the conclusion of the contract period, the Army decided it would award a sole-source, follow-on contract to include a base and 2 option years. Because the anticipated contract value exceeded the \$3.5 million competitive

¹⁶ U.S. GAO B-401057, Mission Critical Solutions, May 4, 2009.

threshold, the incumbent firm could not be considered for award, which ultimately went to an ANC firm.

Comment 7 – Tone of Report, like the Previous GAO Report, is Unsettling

Management commented that the tone of the report was unsettling because ANCs are utilizing the statute to bring resources back to improve their Native Alaskan communities. Current law gives Federal contracting offices the ability to use all aspects of the 8(a) Business Development Program.

OIG Response

The report does not take issue with how ANC firms are using the profits realized from 8(a) awards. We acknowledge that 8(a) revenue earned by ANC-owned firms are used to improve Native Alaskan communities and that ANC profits are distributed to hundreds, and sometimes even thousands of tribal members or Native shareholders. We also believe that it is reasonable to suggest that if the growth in ANC participant activity is adversely impacting other firms in the program, Congress may want to consider whether adjustments are needed either in procurement goals or sole-source award exemptions so that the two can co-exist in the program and both benefit.

We believe that SBA, the Federal advocate for small businesses, should be concerned that 8(a) firms may be adversely impacted by the growth in ANC activity, and that it should comply with statutory requirements to evaluate whether ANC-owned firms have a substantial unfair competitive advantage within an industry before exempting ANC participants from size affiliation rules.

Comment 8 – The report incorrectly states that SBA has implemented only 2 of the 10 GAO recommendations

Management stated that it has taken the necessary corrective actions to implement 5 of the 10 GAO recommendations.

OIG Response

After receiving management's comments, on July 6, 2009, we contacted GAO to determine whether SBA had implemented additional recommendations beyond those that we had listed in our draft report. GAO officials confirmed that only two of their recommendations had been implemented, and that the remaining eight recommendations were still open. GAO officials also told us that SBA had not contacted them to close any additional recommendations.

The three additional recommendations, which we reported as open, but SBA says it has implemented, include:

- “In regulation, specifically address SBA’s role in monitoring ownership of ANC holding companies that manage 8(a) operations to ensure that any changes in ownership are reported to SBA.”
 - *Management claims it addressed this issue by issuing a Procedural Notice and a letter to all 8(a) participants; however neither document specifically addresses SBA’s role in monitoring ownership of ANC holding companies, and the Agency has not issued regulations that address this issue.*
- “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.”
 - *Management stated it launched a Business Development Information System which will have the capability to electronically manage all aspects of the 8(a) program. As noted in the report, the system does not yet have the capability to track primary revenue generators for 8(a) firms, which is planned for a later phase of the project.*
- “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.”
 - *Management believes that the current regulations along with recently revised Partnership Agreements between SBA and the 39 Federal agencies provide clear guidance. Also language requiring that agencies provide copies of contracts and modifications at the time of award has been placed in the revised Partnership Agreements. However, management has not reissued its regulations or established thresholds for when SBA is to be notified.*

ACTIONS REQUIRED

We request that you submit written comments identifying (1) actions proposed or taken in response to each of the six recommendations, and (2) target completion dates for each action. We would appreciate receiving your additional comments within 15 days of the final report date.

We appreciate the courtesies and cooperation of the Associate Administrator, Government Contracting and Business Development, Director of Business Development and the Associate Administrator for Field Operations. If you have any questions concerning this report, please call me at (202) 205-7203 or Riccardo Buglisi, Director, Government Contracting and Business Development at (202) 205-7489.

cc: Joseph Loddo
Director, Business Development

APPENDIX I. SCOPE AND METHODOLOGY

The audit objectives were to: (1) identify 8(a) contracting trends relative to ANC-owned firms; (2) determine whether 8(a) contracting advantages have improved economic opportunities for Alaska Natives; and (3) assess SBA's ability to effectively monitor ANC compliance with program rules.

To identify 8(a) contracting trends relative to ANC participants, we reviewed Federal 8(a) obligations made to ANC participants for fiscal years (FY) 2007 and 2008 that were reported in the Federal Procurement Data System (FPDS). Although prior studies have determined FPDS data to be inaccurate and incomplete, we relied on the information as it was the official and only source for data on Federal obligations to 8(a) firms. As a result, the obligations reported as being made to ANC participants may be over- or understated. At the time of the audit, all Federal procuring agencies had not yet certified to the accuracy of the FY 2008 data. We compared the 2007 and 2008 obligations to that reported for 2004 by the Government Accountability Office (GAO).¹⁷ We also reviewed contract obligations to active ANC participants reported by SBA in its *Fiscal Year 2007 Report to the U.S. Congress on Minority Small Business and Capital Ownership Development* to identify the firms getting the majority of obligations. This was the latest available report and contained information on only active participants.

Because SBA does not track the volume of sole-source awards, we identified sole-source awards for 11 companies that collectively comprised 50 percent of the total Federal 8(a) obligations that went to ANC-owned firms participating in the program in FY 2007. We identified these awards by analyzing information in FPDS and SBA 8(a) files.

To determine whether 8(a) contracting advantages have improved economic opportunities for Alaska Native shareholders, we obtained and reviewed audited financial statements for the top 11 ANC participants receiving the majority of the 8(a) obligations in FY 2007. We also reviewed revenue, profit, and dividend information for the 12 regional ANCs contained in the *Alaska Economic Performance Report* for 2007, that was prepared by the Governor of Alaska and the ANCSA Regional Association's *Alaska Native Corporations 2006 Economic Data*. We interviewed SBA officials in Headquarters and the Alaska District Office as well as various ANC representatives and reviewed previous audit reports to identify the type of benefits that Alaska Native shareholders received from 8(a) contract revenues. Further, we interviewed the parent companies of the top 11

¹⁷ GAO-06-399, *Increased Use of Alaska Native Corporations' Special 8(a) Provisions Calls for Tailored Oversight*, April 2006.

ANC participants in FY 2007 to determine how the 8(a) revenues were benefiting the ANC community and the extent to which the parent companies were involved in managing the ANC firms and overseeing compliance with 8(a) program rules.

To determine the effectiveness of oversight on ANC firms' compliance with 8(a) program rules, we reviewed SBA policies and regulations governing the 8(a) program and interviewed officials in SBA's Alaska District Office, Office of Government Contracting, and Office of Business Development. We also reviewed Program Assessment Tool ratings of the 8(a) program that were prepared by the Office of Management and Budget and followed up on prior OIG and GAO audit recommendations related to improvements needed in SBA's oversight of ANC participants.

The audit was performed between July 2008 and May 2009, in accordance with the *Government Auditing Standards* prescribed by the Comptroller General of the United States.

APPENDIX II. 8(A) AWARDS TO ANC PARTICIPANTS THAT RECEIVED A SIGNIFICANT SHARE OF 8(A) OBLIGATIONS MADE TO ANC-OWNED FIRMS IN FYS 2007 AND 2008

Fiscal Year 2007 (Oct. 1, 2006 - Sept. 30, 2007)			
ANC-owned Firm:	Contract Award Number:	Estimated Contract Award Amount:	Type of Contract:
Alutiiq International Solutions	W911KB-07-C-0031	\$5,000,000.00	sole source
	N69450-07-C-3628	\$2,000,000.00	sole source
	W912DS-07-C-0031	\$10,000,000.00	sole source
	W911KB-07-C-0026	\$7,000,000.00	sole source
	SAQMMA07D0044	\$375,000,000.00	sole source
	SB134107CN0030	\$160,000.00	sole source
	HSCEOP-07-C-00018	\$8,600,000.00	sole source
	HSSCCG-07-D-00001	\$4,500,000.00	sole source
APM, LLC	FA4427-07-C-0108	\$4,780,000.00	sole source
	W912DR-07-C-0066	\$10,000,000.00	sole source
ASRC Management Services	DOC50PAPT0701001	\$120,000,000.00	competed
	DOLJ079E24786	\$3,000,000.00	sole source
	DJA07D000030	\$3,500,000.00	competed
	AG-3151-C-07-0004	\$6,511,400.00	sole source
Chenega Federal Services	W9132V-07-D-0001	\$29,500,000.00	sole source
	N62478-07-G-3026	\$3,000,000.00	competed
	W909MY-07-P-0003	\$75,000.00	sole source
	HSFEEM-07-D-0002	\$15,000,000.00	sole source
Chugach Industries	N00178-07-D-2001	\$12,300,000.00	sole source
	N65236-07-C-6286	\$133,566.00	sole source
	FA4800-07-P-0057	\$1,600,000.00	sole source
Eyak Technology	W91RUS-07-P-0433	\$448,303.00	sole source
SNC Telecommunication, LLC	SPM1C1-07-D-0041	\$46,846,000.00	sole source
	W911QY-07-C-0023	\$20,000,000.00	sole source
	W911QY-07-C-0028	\$22,000,000.00	sole source
Tyonek Manufacturing	W31P4Q-07-C-0189	\$223,000.00	sole source
Total:		\$711,177,269.00	

Fiscal Year 2008 (Oct. 1, 2007 - Sept. 30, 2008)			
ANC-owned Firm:	Contract Award Number:	Estimated Contract Award Amount:	Type of Contract :
Alutiiq International Solutions	N40080-08-C-3018	\$1,727,145.00	sole source
	NRC-10-08-380	\$421,648.00	sole source
	W911KB-08-D-0009	\$105,000,000.00	competed
	N69450-08-C-3585	\$825,000.00	sole source
	W912DS-08-C-0030	\$10,000,000.00	sole source
	N69450-08-C-3582	\$1,000,000.00	sole source
Bristol Design Build Services	W911KB-08-D-0008	\$105,000,000.00	competed
Chenega Federal Services	W909MY-08-C-0022	\$414,000.00	sole source
	HSFECP-08-P-0001	\$88,964.00	sole source
Eyak Technology	FA3010-08-C-0009	\$785,544.22	sole source
	08-PO-142-000152720	\$20,249.00	sole source
SNC Telecommunication, LLC	FA8902-08-C-1009	\$3,518,800.00	sole source
	W911QY-08-C-0040	\$7,800,000.00	sole source
	SPM1C1-08-D-1087	\$51,155,550.00	sole source
Total:		\$287,756,900.22	

Source: OIG Analysis of SBA's Alaska and Santa Ana District Office contract files.

APPENDIX III. MANAGEMENT COMMENTS



U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, DC 20416

July 2, 2009

Ms. Debra S. Ritt
Assistant Inspector General for Auditing
Office of Inspector General
U.S. Small Business Administration
Washington, DC 20416

Dear Ms. Ritt:

Thank you for the opportunity to comment on the draft report issued June 2, 2009, entitled, "Growth in 8(a) Awards to Alaska Native Corporation Firms Has Disadvantaged Other Program Participants and Challenged SBA's Oversight Capability" (Project No. 8005).

The draft report shows that the Alaska Native Corporations (ANCs) have successfully utilized the U.S. Small Business Administration's (SBA) 8(a) Business Development Program (8(a)) to improve local conditions and provide increased social services to Native Alaskans.

As noted in the draft report, Federal contract dollars obligated to firms owned by ANC's grew 831 percent since FY 2000 to \$3.9 billion in FY 2008. However, the report neglects to report that even after subtracting the ANC growth, the 8(a) BD Program showed a steady increase in contract awards.

This draft report restates much of what was previously outlined in the 2006 GAO report entitled "Contract management: Increased Use of Alaska Native Corporations' Special 8(a) Provisions Calls for Tailored Oversight" (GAO-06-399). The June 2, 2009 draft report appears to have reviewed a small sampling of only 11 ANCs from the Alaska District Office (out of the 170 ANCs that are located there).

SBA takes its role in continued oversight of Federal procurement programs very seriously. Since the issuance of the 2006 GAO report and well before a "Discussion Document" of the current draft report was provided to the program office, the Agency had already taken a number of steps to improve the oversight of the 8(a) program.

The SBA is concerned however with the Inspector General report's repeated reliance on the 2006 GAO report despite the fact that the Agency had questioned the subjective nature and conjecture of the concerns cited in that 2006 report.

The report is accurate in that "ANCs fulfill a mission that is broader than the bottom line of the corporations-namely, to help Alaska Natives achieve economic self-sufficiency. Unlike other 8(a) businesses whose profits generally go to one or two disadvantaged individuals, the profits from ANCs are shared by hundreds, and sometimes even thousands of tribal members or Native shareholders." We believe that this is exactly what Congress intended.

The Agency also has several specific concerns with the draft report as outlined below:

- The report is primarily repeating the GAO report from 2006. The exception being a review of contracting activities of a small sample of 11 ANCs.

- The report does not provide an analysis of contract activity of the other program participants groups within the 8(a) Business Development Program.
- The report does not indicate that all of the program participant groups within the 8(a) Business Development program have increased contracting activity
- The report failed to mention that contracting officer must certify that any award, including ANC's, represents a fair and reasonable price and/or best value to the federal government
- Not one contract awarded to a ANC has been cited in the report for not meeting the government expectation
- The sole award for ANC, Tribal, and Native Hawaiian Organizations gives a competitive advantage to these groups in competing with large businesses.
- Like the previous GAO report, the tone of this report is unsettling. The ANCs are utilizing the statute to bring resources back to improve their Native Alaskan communities. Current law gives Federal contracting officers the ability to use all aspects of the 8(a) Business Development program.
- The draft report inaccurately states that: "...in the 3 years since GAO issued its report, SBA has implemented only two of the ten recommendations in the report." **This is incorrect.** SBA has taken the necessary corrective actions and implemented five of the ten recommendations. The remaining five recommendations will be completed by the end of the fiscal year.

We look forward to working with the Office of Inspector General as we continue to provide the oversight of the 8(a) Business Development program. Since 2006, significant internal controls have been implemented as the program office continues to provide a program of continuous oversight and improvement.

Sincerely,

Joseph G. Jordan
Associate Administrator for
Government Contracting
and Business Development

Sincerely,

Jess B. Knox
Associate Administrator for
Field Operations