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Report to the Ranking Member, Subcommittee on Highways and Transit, Committee on Transportation and Infrastructure, House of Representatives

October 2011

DISADVANTAGED BUSINESS ENTERPRISE PROGRAM

Assessing Use of Proxy Data Would Enhance Ability to Know If States Are Meeting Their Goals

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GAO Accountability * Integrity * Reliability

Highlights

Highlights of GAO-12-78, a report to the Ranking Member, Subcommittee on Highways and Transit, Committee on Transportation and Infrastructure, House of Representatives

Why GAO Did This Study

The U.S. Department of Transportation's (DOT) Disadvantaged Business Enterprise (DBE) program aims to increase the participation of small businesses owned and controlled by socially and economically disadvantaged individuals—known as DBEs—in highway contracting. In 2009, U.S. DOT awarded, through state and local governments, about $4 billion to DBEs nationwide. State DOTs are required to establish DBE programs and implement them on federal-aid highway projects. This report responds to a congressional request to examine U.S. DOT's Federal Highway Administration's (FHWA) oversight of state DOT DBE programs. It examines how FHWA (1) oversees state DOTs to ensure they implement their DBE programs according to applicable regulations, (2) assesses whether state DOTs have met their DBE goals, and (3) oversees organizations that certify businesses as DBEs. GAO analyzed FHWA data; reviewed relevant laws and regulations; and interviewed FHWA, and state DOT officials from five states, selected to obtain variation in, among other things, the methods state DOTs use to meet DBE goals.

What GAO Recommends

GAO recommends that FHWA (1) evaluate its committed spending data to determine if it is a reasonable proxy and (2) include statements in information provided to decision makers about potential data limitations. U.S. DOT provided comments on the draft recommendations; GAO clarified the recommendations based on U.S. DOT's comments. U.S. DOT agreed to consider the recommendations.

View GAO-12-78 or key components.
For more information, contact Lorelei St.James at (202) 512-2834 or stjamesl@gao.gov.

What GAO Found

FHWA uses a risk-based approach, which includes conducting risk assessments and day-to-day monitoring, to oversee DBE programs that state DOTs implement. In response to FHWA's designation of the DBE program as an agencywide high-risk area from 2007 through 2010 and other reasons, FHWA recently increased its oversight of state DOT DBE programs. For example, in 2010, FHWA hired a full-time DBE Program Manager and required FHWA division offices in each state to explain to FHWA headquarters how they oversee their state DOTs' DBE programs. While these steps could help FHWA ensure state DOT compliance with regulations, it is too early to assess their effectiveness.

Although FHWA has increased its oversight, FHWA faces two fundamental problems with the DBE data it collects from state DOTs to assess whether state DOTs have met their DBE goals. First, the data that FHWA collects from state DOTs on actual spending on DBEs can cover multiple fiscal years and cannot be meaningfully compared to state DOTs' DBE goals, which reflect the percent of federal-aid highway funds state DOTs will expect to spend on DBEs for one fiscal year. Thus, FHWA may not be able to effectively track whether state DOTs have met their goals as required by federal internal control standards. Second, data on committed spending on DBEs—the proxy measure that FHWA uses instead to measure whether goals were met—shows that about half of the state DOTs met their DBE goals each fiscal year from fiscal years 2006 through 2010; however, FHWA has not conducted a nationwide analysis comparing committed to actual spending to know whether committed spending reflects actual spending for DBEs in all state DOTs. Thus, FHWA does not know whether its data on committed spending can be relied on to evaluate a state DOT's progress in meeting DBE goals. Ensuring that committed spending data are a reasonable proxy is important because state DOTs and FHWA make program decisions based on this information. U.S. DOT's working group that considers various improvements to the administration of the DBE program could provide FHWA with an opportunity to identify options it can use to evaluate its proxy data. Also, while FHWA uses committed spending data to facilitate timely reporting of whether state DOTs have met their goals, FHWA's reporting of data on committed spending to describe progress towards DBE goals does not include statements about potential limitations of the data—namely that the data on committed spending on DBEs might not reflect actual spending.

FHWA oversees the certification activities of state DOTs, which certify that DBEs primarily working on federal-aid highway projects meet federal eligibility requirements. Other U.S. DOT administrations—the Federal Aviation Administration and the Federal Transit Administration—oversee other certifying organizations, such as local airport authorities and state transit agencies, that certify DBEs for work primarily in those areas; such DBEs might also have the skills required (e.g., paving) to work on highway projects. FHWA divisions use their discretion to determine how much and how often to oversee state DOT DBE certification activities.

Contents

Abbreviations

DBE	Disadvantaged Business Enterprise
DOT	Department of Transportation
FAA	Federal Aviation Administration
FHWA	Federal Highway Administration
FTA	Federal Transit Administration
GPRAMA	GPRA Modernization Act of 2010
NRT	National Review Team
Recovery Act	American Recovery and Reinvestment Act of 2009
SAFETEA-LU	Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users
STAA	Surface Transportation Assistance Act of 1982

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Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

October 13, 2011

The Honorable Peter A. DeFazio
Ranking Member
Subcommittee on Highways and Transit
Committee on Transportation and Infrastructure
House of Representatives

Dear Mr. DeFazio:

The U.S. Department of Transportation's (DOT) Disadvantaged Business Enterprise (DBE) program aims to increase the participation of small businesses owned and controlled by socially and economically disadvantaged individuals—known as DBEs—on certain contracts for which U.S. DOT provides financial assistance. According to U.S. DOT's regulations on the program, the DBE program also aims to, among other things, create a level playing field for DBEs so that they can compete fairly on these contracts. In 2009, U.S. DOT—through its Federal Highway Administration (FHWA), Federal Aviation Administration (FAA), and Federal Transit Administration (FTA)—awarded about $4 billion (or about 9.4 percent of U.S. DOT's total assisted contracting[1]) to DBEs nationwide. While recipients, such as state DOTs, of certain types of U.S. DOT funds[2] are responsible for implementing the DBE program, federal oversight of these recipients is critical for ensuring that the objectives of the program are achieved, federal funds are spent appropriately, and the program benefits qualified businesses. Furthermore, transparency in how federal dollars are spent in the DBE program is critical for ensuring

[1]U.S. DOT-assisted contract means any contract between a recipient (such as a state DOT) and a contractor (at any tier, e.g., prime- or sub-contractor) funded in whole or in part with U.S. DOT financial assistance, including letters of credit or loan guarantees, except a contract solely for the purchase of land. 49 C.F.R. § 26.5.

[2]For example, recipients of any of the following types of highway funds are required to implement a DBE program: federal-aid highway funds authorized for surface transportation, with certain exceptions, and intermodal transportation under the Intermodal Surface Transportation Efficiency Act of 1991, and federal-aid highway funds authorized for highways and transportation research under the Transportation Equity Act for the 21st Century. Pub. L. No. 102-240, 105 Stat. 1914; Pub. L. No. 105-178, 112 Stat. 107. *See* 49 C.F.R. § 26.3.

accountability in the program and ensuring the effective and efficient performance and management of the program.

FHWA, FAA, and FTA—which are operating administrations within U.S. DOT—are responsible for overseeing recipients' implementation of the DBE program. Specifically, FHWA is responsible for overseeing how state DOTs implement the DBE program on federal-aid highway projects[3] and whether state DOTs comply with the requirements set forth in statute and U.S. DOT's regulations.[4] A number of offices within FHWA are involved in helping oversee the DBE program. For example, at the national level, FHWA's Office of Civil Rights monitors nationwide progress in meeting DBE goals. FHWA's division offices—located in each state, the District of Columbia, and Puerto Rico—oversee state DOTs' day-to-day implementation of the DBE program. Given FHWA's role in overseeing the state DOTs' implementation of the DBE program, this report examines how FHWA

1. oversees state DOTs to ensure that they are implementing their DBE programs in accordance with applicable regulations,

2. assesses whether state DOTs are meeting their DBE goals, and

3. oversees organizations that certify DBEs that work on federal-aid highway projects.

To address our three objectives, we reviewed relevant laws and regulations pertaining to the DBE program. We also reviewed documentation and interviewed officials from U.S. DOT's and FHWA's Offices of Civil Rights, as well as officials and representatives from five

[3]Federal-aid highway funds are authorized by Congress to assist the states in providing for construction, reconstruction, and improvement of highways and bridges on eligible federal-aid highway routes and for other special purpose programs and projects.

[4]23 U.S.C. § 101 note, 49 C.F.R. part 26. FAA and FTA are responsible for overseeing DBE programs implemented by recipients of federal-aid airport and transit funds, respectively. This report focuses on FHWA's oversight of DBE programs implemented by recipients of federal highway funds, which are primarily state DOTs. For this report, we use the term "state DOTs" to refer to state DOTs in all 50 states, the District of Columbia, and Puerto Rico. According to FHWA officials, each state should only have one DBE program—the state DOT's DBE program—for highway funds. State DOTs may pass federal highway funds to subrecipients (i.e., local jurisdictions).

states: Florida, Minnesota, Missouri, Washington, and Wisconsin.[5] We judgmentally selected the five states to obtain variation in, among other areas, the extent to which state DOTs met their DBE goals, the number of certifying organizations in the state, and geographic location. Specifically, in each of the states, we reviewed documentation and interviewed officials from FHWA divisions and state DOTs about FHWA's oversight of state DOTs' DBE activities. In each state, we also reviewed documentation and interviewed officials from organizations that certify DBEs that work on federally funded highway projects—such as state DOTs and local transit agencies—and judgmentally selected these organizations based on, among other things, their geographic location and whether they certified DBEs that work on highway projects. We compared FHWA's oversight of state DOTs' DBE activities to GAO reports on oversight and accountability, including GAO guidance on internal controls.[6] Additionally, to address the three objectives, we reviewed the findings of the National Review Team (NRT) that FHWA established to oversee DBE program implementation on American Recovery and Reinvestment Act of 2009 (Recovery Act)[7] projects.[8] Separately, to examine how FHWA assesses whether state DOTs are meeting their DBE goals, we analyzed FHWA's national data on state DOTs' committed and actual spending and how FHWA determined whether state DOTs achieved their DBE goals for fiscal years 2006 through 2010.[9] We conducted selected quality checks of the data, compared FHWA's national data to the data in the *Uniform Report of DBE Awards or Commitments and Payments* (commonly referred to as the Uniform Report) for the five state DOTs that we contacted, and resolved inconsistencies with the appropriate agency officials. Given our review of the data provided to us by FHWA, we identified problems with the data

[5]Since these states were selected as a nonprobability sample, the information we gathered from officials in these states cannot be generalized to all states. The examples we use throughout this report are included for illustrative purposes.

[6]GAO, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

[7]Pub. L. No. 111-5, 123 Stat. 115 (2009).

[8]Although the NRT's review focused on Recovery Act projects, the data and analyses gathered by the team were useful for our review because DBE requirements are the same for Recovery and non-Recovery Act projects.

[9]We did not evaluate the appropriateness of the state DOT DBE goals.

FHWA uses to assess whether state DOTs achieved their DBE goals, which we discuss in this report.

We conducted this performance audit from September 2010 to October 2011 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. See appendix I for more information about our scope and methodology.

Background

U.S. DOT established a minority and women's business enterprise program for its highway, airport, and transit programs by regulation in 1980.[10] The Surface Transportation Assistance Act of 1982 (STAA) contained the first statutory DBE provision authorizing a U.S. DOT DBE program. As amended, the provision requires that not less than 10 percent of the amounts made available by the act be expended through small businesses owned and controlled by socially and economically disadvantaged individuals—known as disadvantaged business enterprises or DBEs—unless the Secretary of Transportation determines otherwise.[11] Following STAA, the DBE program continued to be reauthorized, and was last reauthorized in the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU).[12]

[10]The program was first established under the authority of Title VI of the Civil Rights Act of 1964 and other nondiscrimination statutes that apply to U.S. DOT financial assistance programs.

[11]Pub. L. No. 97-424, § 105(f), 96 Stat. 2097, 2100 (1983), as amended at 23 U.S.C. § 101 note. U.S. DOT's regulations on the DBE program state that the statutory 10 percent goal is an aspirational goal, meaning that state DOTs and other recipients of certain federal transportation funds are not authorized or required to set overall or contract goals at the 10 percent level, or any other particular level, or to take any special administrative steps if their goals are above or below 10 percent. According to the regulations, the 10 percent goal is merely a means for U.S. DOT to evaluate the overall performance of the DBE program nationwide. 49 C.F.R. § 26.41.

[12]Pub. L. No. 109-59, § 1101(b), 119 Stat. 1144, 1156 (2005), as amended at 23 U.S.C. § 101 note.

As a condition of receiving certain federal transportation funds from U.S. DOT, recipients of these funds, such as state DOTs, are required to implement a DBE program in accordance with U.S. DOT's DBE regulations.[13] The regulations require that each state DOT set an annual goal for DBE participation in federal-aid highway projects, expressed as the percent of federal-aid highway funds it will expect to spend on DBEs for contracts that are awarded or committed in a fiscal year.[14] According to U.S. DOT, these goals are based on each state DOT's particular circumstances and represent the level of DBE participation that the state DOT would expect absent the effects of discrimination in a relevant market area.[15] For fiscal year 2010, state DOTs' DBE goals ranged from 4 percent to about 24 percent of each state DOTs' federal-aid highway funds. For example, in fiscal year 2010, one state DOT's goal was to spend 12.6 percent of its federal-aid highway funds on DBEs. In establishing their DBE goals, state DOTs must provide for public participation, which includes, for example, consulting with contractor groups and accepting comments on the proposed goal.[16] Once established, the methodology and process that state DOTs use to develop the goals are subject to FHWA approval, according to FHWA.[17] To help meet their DBE goals, state DOTs can take various actions, including setting DBE goals on individual U.S. DOT-assisted contracts. DBE goals on these U.S. DOT-assisted contracts are called contract

[13]49 C.F.R. §§ 26.3, 26.101. U.S. DOT's DBE regulations are contained at 49 C.F.R. part 26.

[14]Unlike prime contracts that are awarded, subcontracts can either be awarded or committed. In general, state DOTs award contracts to prime contractors, which may be DBEs, and prime contractors award subcontracts to DBE subcontractors, or commit to provide funds to DBE subcontractors. *See* 49 C.F.R. part 26, appendix B.

[15]49 C.F.R. § 26.45(b).

[16]49 C.F.R. § 26.45(g).

[17]In addition, according to U.S. DOT officials, as part of its internal review process, FHWA also conducts legal sufficiency reviews of the decisions it makes regarding the methodologies and processes state DOTs use to establish their goals.

goals.[18, 19] Each contract goal on an individual U.S. DOT-assisted contract is expressed as the percentage of federal-aid highway funds the state DOT will expend on DBEs on the individual contract.

When a state DOT sets DBE contract goals on individual U.S. DOT-assisted contracts, bidders on those contracts must make good faith efforts to meet those goals.[20] The bidder can meet this requirement in one of two ways: (1) meet the goal on the individual U.S. DOT-assisted contract, or (2) document that it made adequate good faith efforts—meaning that the bidder took the necessary and reasonable steps to achieve the goal even though it did not succeed in obtaining enough DBE participation to do so.[21] State DOTs are responsible for evaluating whether bidders made good faith efforts to meet their goals, and according to U.S. DOT officials, this evaluation is subject to FHWA review as appropriate.

FHWA collects data from state DOTs on their DBE programs. Specifically, U.S. DOT's DBE regulations require that all state DOTs report to FHWA their federal spending on DBEs using a form called the *Uniform Report of DBE Awards or Commitments and Payments* (commonly referred to as the Uniform Report).[22] These reports are due June 1 and December 1 each fiscal year, covering two reporting periods—the first and second half of the fiscal year, respectively. In the Uniform Reports, state DOTs report

[18]49 C.F.R. § 26.51(d). State DOTs must meet as much of their DBE participation goal as possible using race-neutral methods—actions that assist all small businesses without consideration of DBE status. When a state cannot achieve its goal using race-neutral methods, it must use race-conscious methods—actions used to assist only DBEs—to meet the remaining portion of the goal. The primary race-conscious method is setting contract goals on individual U.S. DOT-assisted contracts. 49 C.F.R. § 26.51. *See also* 49 C.F.R. § 26.5. According to FHWA officials, most states use a combination of race-neutral and race-conscious methods to meet their state goals.

[19]FHWA approval of each contract goal is not necessarily required; however, FHWA may review and approve or disapprove any contract goal established. 49 C.F.R. § 26.51(e)(3).

[20]49 C.F.R. § 26.53. *See* 49 C.F.R. part 26, appendix A, I.

[21]49 C.F.R. § 26.53(a). *See also* 49 C.F.R. part 26, appendix A. In addition, according to U.S. DOT, bidders who meet only a portion of the contract goal must document good faith efforts for the portion of the goal not met.

[22]According to FHWA, subrecipients of federal highway funds, such as local jurisdictions, should report the total amount of federal funds they commit to and actually spend on DBEs to the state DOT for inclusion in the state DOT's Uniform Report.

to FHWA two types of data on spending on DBEs: committed spending on DBEs and actual spending on DBEs. Committed spending on DBEs is the total amount of federal funds that state DOTs award or commit to DBEs in the fiscal year.[23, 24] Committed spending data on contracts awarded in the fiscal year include data on contracts that will be completed in the fiscal year as well as ongoing contracts.[25] These data include completed and ongoing contracts because some highway contracts can be relatively short and can be awarded and completed within the same fiscal year, whereas other highway contracts can cover multiple years between award and completion.[26] Actual spending on DBEs is the total amount of actual payments that state DOTs make to DBEs using federal funds on contracts that are *completed* in the fiscal year.[27] Actual spending includes spending on contracts completed in the fiscal year and can include contracts that were awarded in previous years.

[23]State DOTs award contracts to prime contractors, which may be DBEs, and prime contractors award subcontracts to DBE subcontractors, or commit to provide funds to DBE subcontractors. For each reporting period, the DBE regulations require state DOTs to provide data on the total amount of federal funds that are awarded to DBEs on U.S. DOT-assisted prime contracts, and the total amount of federal funds that are awarded or committed to DBEs on U.S. DOT-assisted subcontracts. 49 C.F.R. part 26, appendix B. Although applicable regulations refer to this as "Awards/Commitments," for purposes of this report, we refer to this as "committed spending" or "committed spending on DBEs."

[24]To determine committed spending on DBEs for the entire fiscal year, FHWA combines the committed spending data from both reporting periods, or some state DOTs provide FHWA committed spending data for the entire fiscal year in the report they submit on December 1.

[25]Ongoing contracts means contracts that were awarded in the fiscal year but will not be completed in the fiscal year.

[26]We have previously reported that according to FHWA, the construction of major projects takes 2 to 6 years to complete once a contract is awarded. GAO, *Federal-Aid Highways: Federal Requirements for Highways May Influence Funding Decisions and Create Challenges, but Benefits and Costs Are Not Tracked*, GAO-09-36 (Washington, D.C.: Dec. 12, 2008).

[27]For each reporting period, the DBE regulations require state DOTs to provide data on the total actual payments that they made to DBEs using federal funds on prime contracts that are completed in the reporting period. 49 C.F.R. part 26, appendix B. Although applicable regulations refer to this as "Actual Payments," for purposes of this report, we refer to this as "actual spending" or "actual spending on DBEs". To determine actual spending on DBEs for the entire fiscal year, FHWA would combine the actual spending data from both reporting periods, or some state DOTs provide FHWA actual spending data for the entire fiscal year in the report they submit on December 1.

For certification of DBEs, U.S. DOT requires DBEs to be certified in each state where they want to bid on or participate in U.S. DOT-assisted contracts. DBEs are certified according to U.S. DOT's regulatory eligibility requirements and certification procedures.[28] Specifically, DBEs must be small businesses that are at least 51 percent owned by one or more individuals who are socially and economically disadvantaged, and that are managed, operated, and controlled by these owners.[29] (See app. II for more details on the eligibility requirements.) Organizations that certify DBEs must take many steps to ensure that a DBE firm meets certification requirements—this includes, among other things, reviewing firms' applications for certification; conducting on-site visits and interviews; and reviewing licenses, stock ownership, equipment, work completed, resumes of principal owners, and the bonding and financial capacity of the firm. Furthermore, DBEs are certified only in the type or types of work, such as paving, that they can perform. According to U.S. DOT, in 2009, about 27,000 DBEs were certified under its program.[30]

Generally, organizations within each state that receive DOT funds decide which organizations within the state can certify DBEs. While some states have multiple organizations certifying DBEs, others have one certifying organization. For example, in the five states we focused on as part of this review, four states (Florida, Minnesota, Missouri, and Wisconsin) have multiple organizations within the state that certify DBEs, and the remaining state (Washington) has one organization that certifies DBEs for the entire state. Each state is required by DBE regulations to have a unified approach to certification so that the certification decisions of one organization are honored by all the organizations receiving U.S. DOT

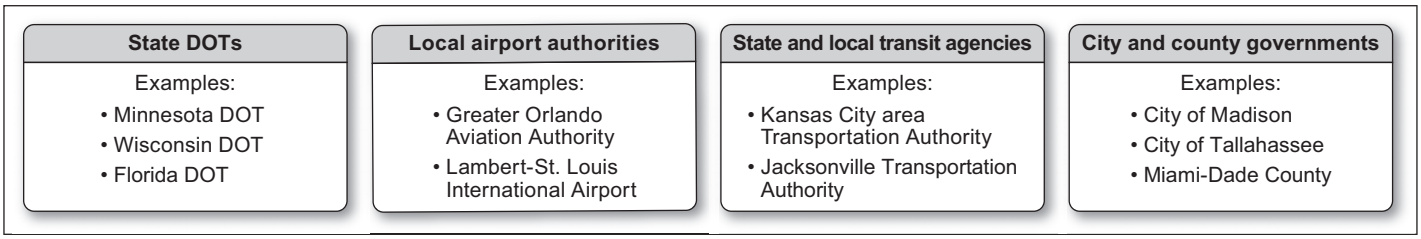
[28] *See* 49 C.F.R. part 26, subparts D, E.

[29] 49 C.F.R. § 26.5.

[30] According to U.S. DOT officials, the number of certified DBEs could include duplicates—when a DBE firm is certified in more than one state or when a firm is certified to conduct both highway and airport work.

funds in the state.[31] This essentially allows for a "one-stop shop" for DBE firms seeking certification, meaning that a DBE only needs to apply for certification with one organization in the state, rather than apply for certification from all the organizations in the state with which the DBE wants to conduct work. The organizations that certify DBEs may include the state DOT, local airport authorities, state and local transit agencies, and city and county governments. For example, Florida has 13 organizations that certify DBEs—including Florida DOT, the Greater Orlando Aviation Authority, and Miami-Dade County. See figure 1 for examples of organizations that certify DBEs.

Figure 1: Examples of Organizations that Certify DBEs



Source: GAO analysis.

The type of work a DBE performs and the DBE's geographic location can play a role in some states in determining which organization in the state reviews a firm's application for certification and certifies the firm as a DBE. State DOTs primarily review applications and certify DBEs that work on highway projects, while local airport authorities and state and local transit agencies primarily review applications and certify DBEs that work on airport and transit projects, respectively. Nevertheless, the DBEs certified by organizations other than state DOTs (such as local airport authorities and state and local transit agencies) can also work on highway projects if the type of work they are certified to perform can be applied to

[31]Each state's unified approach to certification is described in an agreement between all the organizations that receive U.S. DOT funds in the state. This agreement establishes a state's Unified Certification Program (or UCP), commits the certifying organization(s) to follow DBE certification regulations, and describes the certification responsibilities of the organization(s) that certify DBEs in the state. For example in one state, each of the three certifying organizations are responsible for processing DBE certification applications, but the organizations collectively decide whether to certify a firm as a DBE. In another state, each of the certifying organizations process DBE certification applications but each independently decides whether to certify a firm as a DBE.

both airport or transit and highway projects. For example, if a DBE is certified to do paving, this DBE may be able to do paving work on both highway and airport projects. Geographic location may also play a role in determining which organization reviews a firm's application for certification and certifies DBEs. For example, a county government in Wisconsin certifies DBEs from six nearby counties in the state, regardless of whether the DBE is interested in working on federal highway, transit, or airport projects.

FHWA's Oversight of State DOT DBE Programs

FHWA Uses a Risk-Based Approach to Oversee State DOT DBE Programs and Has Identified the DBE Program as a Risk Area

Federal agencies should perform a number of oversight activities to safeguard against fraud and to ensure that federal programs meet their objectives and comply with federal regulations.[32] FHWA oversees the DBE program as part of its oversight of state DOTs' implementation of federal-aid highway programs. FHWA offices—including FHWA's Office of Civil Rights, a program office located in the agency's headquarters office, and FHWA's 52 division offices, which are located in each state, the District of Columbia, and Puerto Rico—oversee the DBE program. FHWA's Office of Civil Rights is responsible for a number of civil rights programs, including the DBE program, and the division offices perform primary oversight of state DOT activities. In general, these offices oversee the DBE program through risk assessments, day-to-day monitoring of state DOT activities, and program reviews.

Risk Assessments

FHWA's annual risk assessments identify and assess risks across all federal-aid highway programs, including the DBE program.[33] FHWA uses

[32]GAO/AIMD-00-21.3.1.

[33]In 2009, we concluded that FHWA had strengthened its oversight of its programs by improving its risk management approach. GAO, *Federal-Aid Highways: FHWA Has Improved Its Risk Management Approach, but Needs to Improve Its Oversight of Project Costs*, GAO-09-751 (Washington D.C.: July 24, 2009).

the results of these risk assessments to help it determine how to focus its oversight. Both FHWA's program offices and division offices conduct these assessments and use the results to take actions to address the risks they identify, which have recently included the DBE program.[34] In addition, FHWA uses the results of the program office and division office risk assessments to identify agencywide risk.

- *Program office risk assessments*. In 2010 FHWA's Office of Civil Rights identified the DBE program as a risk area because of the potential for, among other things, a significant increase in fraud and abuse, improper program implementation, and costly litigation. Furthermore, the office identified specific risk areas within the DBE program, including DBE goals and DBE certifications. Given the Office of Civil Rights' identification of the DBE program as a risk area, the office has taken actions, such as hiring a full-time DBE Program Manager, to help address the potential problems identified (e.g., fraud, improper program implementation, and other risks).

- *Division office risk assessments*. In 2010, 23 of 52 FHWA division offices identified the DBE program as a risk area. These divisions identified the DBE program as a risk area because of, among other things, challenges related to the stewardship and administration of state DOTs' DBE programs and to contractor compliance with DBE program requirements. For example, one division office identified the DBE program as a risk area because of concerns regarding the stewardship and oversight of a state DOT's DBE program that could lead to, among other things, confusion and lack of understanding about how to properly implement the DBE program requirements, increasing the opportunity for fraud and abuse. To address these risks, the division planned to provide training to state DOT officials on requirements specified in the DBE regulations and planned to conduct a program review of the state DOT's implementation of specific DBE regulations, such as those related to monitoring and achieving contract goals.

- *Agencywide risk identification*. Based on the results of program office and division office risk assessments, FHWA identifies risks that are

[34]When conducting these risk assessments, FHWA identifies risks by taking into consideration many different sources of information, including the results of audits, such as Inspector General audits, and trends or changes.

relevant for the entire agency. These risks become key drivers in developing FHWA's strategic implementation plan, which reflects the administration's priorities for the upcoming year. According to FHWA officials, FHWA first identified the DBE program as an agencywide high-risk area in 2007 because the DBE program accounted for 50 percent of the risks identified in the entire civil rights area. This designation as a high-risk area continued through 2010.[35] In response to the agencywide designation of the DBE program as a high-risk area, FHWA has recently increased its oversight of the DBE program.

Day-to-Day Monitoring

FHWA division officials we interviewed from all five of the states we focused on said that they monitor state DOT activities on an ongoing basis to help oversee all federal-aid highway programs implemented by state DOTs, including the DBE program, and to help identify areas that need increased oversight attention. For example, one division official we interviewed said that as a part of his day-to-day oversight, he reviews the state DOT's process for setting contract goals. In some instances, this division official said that he found that the state DOT had set all contract goals too low to meet the state DOT's DBE goal.[36] Furthermore, officials from all five of the division offices said that they participate in meetings with state DOTs and/or receive reports from state DOTs that help them identify areas where there may be problems and where they need to focus their attention. For example, one division office that we focused on as part of our review requires its state DOT to provide quarterly progress reports on DBE contract goals. The official we interviewed from this division office said that these reports help her identify issues, such as issues related to goals on individual U.S. DOT-assisted contracts, which she may not otherwise hear about from her daily interactions with the state DOT.

Program Reviews

In 2007 and 2008, FHWA conducted program reviews of all its federal-aid highway programs, including the DBE program. FHWA conducted these reviews to determine which federal highway programs required greater federal oversight and assistance. For the DBE program reviews, FHWA officials—including those from the divisions—reviewed each state DOT's implementation of the DBE regulations to determine if the state DOT

[35]At the time of this review, FHWA had not identified its agencywide risks for 2011.

[36]This division official said that when he noticed such problems, he worked with the state DOT to establish more realistic contract goals as needed.

needed more federal oversight and assistance in implementing the regulations.[37] Based on the results of the 2007 and 2008 reviews, FHWA's Office of Civil Rights decided to conduct the DBE program reviews again in 2010 and 2011.[38] Like the 2007 and 2008 reviews, the 2010 and 2011 reviews assessed how state DOTs implemented the DBE regulations. The 2010 and 2011 program reviews assessed, for example, whether a state DOT provided opportunities for public participation when establishing its DBE goal, as required by the DBE regulations. An official from FHWA's Office of Civil Rights said that based on the results of the recent program reviews, the office plans to compile all the concerns and problems identified in the reviews in a report for FHWA division and state DOT leadership, and also implement improvements in state DOTs' DBE programs. Officials from FHWA's Office of Civil Rights said that they are still collecting the results of the program reviews from FHWA divisions and state DOTs and, as a result, have not yet completed an initial report that compiles all the concerns or problems identified nor implemented any improvements in state DOT DBE programs.

FHWA Has Recently Increased Its Oversight to Help Ensure State DOTs' Compliance with DBE Regulations

In response to the current administration's focus on small business programs (such as the DBE program), U.S. DOT's interest in increasing accountability in DBE program implementation, and FHWA's continued designation of the DBE program as an agencywide high risk area, FHWA and U.S. DOT have taken a number of steps in the past 2 years to increase its oversight of state DOT DBE programs. Some of the more significant actions are as follows:

- *DBE Program Manager*. FHWA hired a full-time National DBE Program Manager in 2010 to help oversee state DOTs' implementation of the DBE program.
- *Action Plans*. Starting in 2010, FHWA's Office of Civil Rights required that all FHWA divisions develop and submit action plans that, in part, describe division office oversight activities, identify areas in state DOT DBE programs that need improvement, and identify actions the

[37]According to FHWA officials, the DBE program reviews are not compliance reviews, but rather an information-gathering exercise so that FHWA can determine how to focus its oversight and assistance efforts.

[38]In addition, FHWA's Office of Civil Rights decided to conduct the program reviews every 3 years going forward.

division offices will take to improve their and the states' leadership and management of the DBE program. The Office of Civil Rights also required that FHWA divisions submit quarterly reports that provide an update on what they are doing to implement the actions the divisions have identified to improve the leadership and management of the DBE program.

- *Regulations*. In January 2011, U.S. DOT updated its DBE regulations to, among other things, add a requirement for state DOTs to analyze in detail the reasons for any difference between their state DOT DBE goal and the amount of federal funds the state DOT committed to spend on DBEs for each fiscal year. State DOTs must then establish specific steps and milestones to correct the problems they identified in their analysis and to fully meet its DBE goal in the next fiscal year.[39] These requirements went into effect in February 2011.[40] According to U.S. DOT, the added requirement will help state DOTs understand, when applicable, why their DBE goals are not being met, and will increase state DOTs' accountability for meeting DBE goals. Based on FHWA's most recent data, 54 percent of state DOTs did not meet their DBE goals in fiscal year 2010 and would have been subject to this requirement in fiscal year 2010 if it had been in effect. See appendix III for further information on the number and percent of state DOTs meeting their DBE goals based on committed spending.

- *National Review Team (NRT)*. In response to FHWA's 2009 risk assessment, FHWA established the NRT to review six areas, including the DBE program, that posed a nationwide risk of misuse of Recovery Act funds.[41] FHWA used the results of the NRT review to identify areas for improved oversight and training. For example, the NRT identified concerns about the process that some state DOTs were using to evaluate whether prime contractors bidding on contracts

[39]49 C.F.R. § 26.47(c).

[40]In addition to these requirements, U.S. DOT incorporated additional requirements in its January 2011 update to the DBE regulations, some of which have implementation dates after February 2011.

[41]The other risk areas are preliminary plans, specifications, and estimates; contract administration; quality assurance of construction materials; local public agencies; and eligibility for payments.

made adequate good faith efforts to meet DBE contract goals.[42] Specifically, in one of these states, the NRT found that the state DOT awarded a majority of its contracts to prime contractors who did not meet the DBE contract goals, but provided documentation that they made good faith efforts to do so.[43] While DBE regulations allow state DOTs to award contracts based on bidders' good faith efforts and do not limit the number of contracts that can be awarded in this way, FHWA officials explained that awarding a high number of contracts on the basis of good faith efforts might be a reason state DOTs do not meet their state DBE goals. To address these concerns, the FHWA division in this state trained state DOT staff on this issue, tracked the number of contracts that the state DOT awarded based on good faith efforts on a monthly basis, and further reviewed the state DOT's process for evaluating prime contractor good faith efforts to ensure that the state DOT was complying with the DBE regulations.[44] Furthermore, on a nationwide level, FHWA's Office of Civil Rights increased its training to FHWA's division officials on this issue.

In addition to these steps, FHWA took a number of other actions. For example, it increased its training on the DBE program for FHWA division offices. FHWA also increased its focus on the DBE program during national seminars and conferences. Furthermore, FHWA included the DBE program, along with other civil rights areas, in its 2011 strategic implementation plan. According to FHWA officials, the significance of this

[42]When a state DOT sets DBE contract goals on individual U.S. DOT-assisted prime contracts, bidders are required to make good faith efforts to meet those set goals. 49 C.F.R. § 26.53(a). State DOTs are responsible for evaluating whether a bidder that did not meet its goal made adequate good faith efforts. DBE regulations provide state DOTs with guidance on the types of actions state DOTs can consider when conducting their evaluations.

[43]According to DBE regulations, prime contracts can be awarded to bidders even if the bidders do not meet the contract goals as long as the bidders can show documentation that they made adequate good faith efforts to do so, meaning that they took all the necessary and reasonable steps to achieve the contract goal. 49 C.F.R. § 26.53(a), appendix A.

[44]In its review, the FHWA division office found that the state DOT did not critically evaluate the documentation that the prime contractors submitted to the state DOT showing the actions the contractors had made to meet the contract goals. As a result of the review, the FHWA division office recommended that the state DOT, among other things, develop training for prime contractors on the documentation the contractors should provide to the state DOT to show good faith efforts.

is that the 2011 plan marked the first time that civil rights programs, including the DBE program, were given agencywide attention.

It is too early to determine the effectiveness of the recently implemented oversight activities described above. But each of the oversight activities could help FHWA protect against fraud in the DBE program, ensure that the DBE program is meeting its objectives, and identify areas where state DOTs may not be in compliance with the regulations. According to FHWA officials, if they find that a state DOT has fallen short in meeting any part of the DBE regulations, the FHWA division will work with the state DOT to bring the state DOT back into compliance. According to officials at FHWA's Office of Civil Rights, should a state DOT refuse to comply with any part of the regulation without seeking a waiver from the Secretary of Transportation, FHWA would then consider other options, including withholding federal funds from the state DOT pursuant to regulations.[45, 46] For example, one of the divisions we spoke with said that because of noncompliance with parts of the DBE regulations, it presented a letter of possible funds withholding to a state DOT. Subsequently, the state DOT took steps to comply with the regulations as required.[47]

FHWA Faces Fundamental Problems in Its Use of DBE Data

FHWA faces two fundamental problems with the DBE data it collects from state DOTs to assess whether state DOTs have met their DBE goals. First, actual DBE spending data reported by state DOTs cannot be meaningfully compared to state DOTs' DBE goals to measure whether goals were met. Second, the proxy data that FHWA uses to measure whether goals were met—data on committed spending on DBEs—may or may not be a reasonable proxy of state DOTs' actual spending on DBEs.

[45]49 C.F.R. § 26.101(a). *See also* 49 C.F.R. § 26.103.

[46]We have previously reported that officials of U.S. DOT's administrations rarely use available enforcement options—such as withholding federal funds and imposing civil penalties—because the options are too drastic or lengthy to bring about compliance. GAO, *Transportation Accessibility: Lack of Data and Limited Enforcement Options Limit Federal Oversight*, GAO-07-1126 (Washington, D.C.: Sept. 19, 2007).

[47]States are required to implement their DBE programs in good faith. 49 C.F.R. § 26.47(b). According to FHWA's Office of Civil Rights officials, a state DOT is operating its program in good faith if the state DOT is using "good faith efforts" to comply with DBE regulations. In situations when a state DOT is not complying with a specific regulatory requirement, the state DOT will still be operating its program in good faith if the state DOT uses its best efforts to come into compliance with the regulations with the assistance of FHWA.

As a result, FHWA does not know whether its data on committed spending can be relied on to evaluate state DOTs' progress in meeting goals or whether state DOTs would benefit from FHWA assistance to meet their goals. Also, FHWA's reporting of data on committed spending to describe progress towards DBE goals does not include statements about potential limitations of the data—namely that the data on committed spending on DBEs might not reflect actual spending. Including statements about the potential limitations of committed spending data could help FHWA increase transparency in the reporting of DBE spending data.

FHWA Data on Actual Spending on DBEs Does Not Allow for Comparison to DBE Goals

Federal internal control standards call for an agency to track major achievements, such as spending, and compare these to its goals.[48] FHWA is unable to make this comparison using data on actual spending on DBEs because the actual spending data that FHWA collects in the Uniform Reports reflect different time frames and, therefore, different data from state DOTs' DBE goals.[49] Actual spending data are based on completed contracts—some of which could have been awarded in previous fiscal years—while a state DOT's DBE goal reflects what state DOTs will expect to spend on DBEs on contracts that are awarded or committed in the current fiscal year. This difference in time frames and when contracts are awarded makes it difficult to compare the state DOTs' actual spending with its DBE goals. FHWA officials roughly estimate about 50 percent of contracts are completed in the fiscal year in which they were awarded. Actual spending for the remaining estimated 50 percent of contracts cover multiple years between award and completion, and are not included in Uniform Reports until these contracts are completed.[50] Without comparing actual spending on DBEs to a state DOT's DBE goals, FHWA may not be able to effectively track whether a state DOT has met its DBE goals as called for by internal controls.

[48]GAO/AIMD-00-21.3.1.

[49]U.S. DOT's DBE regulations require state DOTs to report actual spending on DBEs on completed contracts in the Uniform Reports. The regulations also require state DOTs to track, but not report to FHWA, actual spending on all contracts (i.e., completed and ongoing). 49 C.F.R. § 26.37(c). State DOTs can use this data to monitor payments made to DBE firms during the course of a contract.

[50]The actual spending data on such multi-year contracts would be included in the Uniform Report for the reporting period in which the contract is completed. *See* 49 C.F.R. part 26, appendix B.

FHWA's Use of Committed Spending Data May Not be a Reasonable Proxy

FHWA uses committed spending on DBEs as a proxy for actual spending on DBEs to determine if state DOTs are meeting their DBE goals. According to U.S. DOT officials, FHWA's practice of using committed spending is a convention necessary to provide timely reporting; if FHWA used actual spending to determine whether DBE goals were met, it would have to wait several years for some contracts to be completed. Based on the committed spending data in the Uniform Reports, about half of the state DOTs met their DBE goals each fiscal year from fiscal years 2006 through 2010. See appendix III for the number and percentage of state DOTs meeting their DBE goals from fiscal years 2006 through 2010, based on committed spending data.

FHWA has not conducted a nationwide analysis comparing committed spending to actual spending to know whether it is a reasonable proxy for actual spending. Thus, committed spending on DBEs may or may not definitively show whether state DOTs met their DBE goals. According to FHWA and state DOT officials, committed spending could be similar to actual spending, or it could differ from actual spending. Specifically, an FHWA headquarters official told us about two cases where she personally compared committed to actual spending, and found that the committed spending was close to actual spending. The headquarters official said that in one of the two cases, she compared committed to actual spending on individual contracts and in the second case, she compared committed to actual spending on completed contracts historically, over a period of time.[51] Separately, FHWA and state DOT officials we contacted said that committed spending could be lower or higher than actual spending. For example, an FHWA official from one state we focused on said prime contractors' committed spending on DBEs may be higher than actual spending on some projects because of changes to the contract that reduce the amount of work performed by DBEs. In another state, a state DOT official said a prime contractor's committed spending on DBEs at the start of a contract may be 8 percent, but the actual spending on DBEs at the end of the contract may be only 2 percent. The official said in fiscal year 2008 the state DOT did not meet its fiscal year 2008 DBE goal because the prime contractor on a highway project spanning multiple years spent less on DBEs than committed.

[51]In the first case, the FHWA headquarters official compared the committed to actual spending when she worked for a state DOT.

FHWA's NRT also found that committed spending may not match actual spending and thus may not provide a complete picture of whether state DOTs are meeting their DBE goals. The NRT offered findings and recommendations to two of the five state DOTs that we contacted during our review pertaining to the issue of data on committed and actual spending. For example, the NRT found that one state DOT did not require a prime contractor to provide information to the state DOT on actual spending on DBEs if the contractor provides work to a DBE after the DBE goal on the contract is met. Thus, according to the NRT report, the state DOT may not accurately capture or report all actual spending to DBEs, and as a result may spend more on DBEs than committed. In another state, the NRT recommended that the state DOT compare committed to actual spending on DBEs on completed DBE subcontracts to help ensure that the DBE program was compliant at the project level. Furthermore, in addition to the NRT's findings, the U.S. DOT Office of Inspector General recommended in another state that the state DOT capture all actual spending on DBEs regardless of whether the DBE goal on a contract had already been met.

Without a nationwide analysis comparing committed spending to actual spending, FHWA cannot be certain whether committed spending reflects actual spending for DBEs in all state DOTs. Therefore, FHWA does not know whether its data on committed spending can be relied on to evaluate state DOTs' progress in meeting goals; hold state DOTs accountable for meeting their DBE goals, as emphasized in U.S. DOT's update to its regulations;[52] make program decisions based on whether state DOTs are meeting their DBE goals on an annual basis; or provide assistance to state DOTs that are not meeting their goals. Furthermore, if committed spending data on DBEs do not reflect actual spending on DBEs, then state DOTs might potentially take inappropriate action or inaction, depending on whether the data show a state DOT has met its DBE goal. For example, if the data on committed spending show a state DOT is meeting its goal, it might, as one state DOT said it does, discontinue setting DBE contract goals, which are DBE goals on

[52]To increase state DOTs' accountability for meeting overall DBE goals, among other things, U.S. DOT updated its DBE regulations to require state DOTs to analyze the reason for any differences between their DBE goals and committed spending on DBEs for that fiscal year.

individual U.S. DOT-assisted contracts.[53] If the data on committed spending do not reasonably match actual spending, however, then the state DOT might stop its use of DBE contract goals prematurely.

U.S. DOT has a departmentwide working group that, according to a U.S. DOT official, considers various improvements to the administration of the DBE program, including improvements to the various reporting forms used in the DBE program. As part of its efforts, this working group is considering revising the form—the Uniform Report—that state DOTs use to report committed and actual spending on DBEs.[54] In February 2011, the members reviewing the Uniform Report held their first meeting but did not determine what changes to recommend. This working group could provide an opportunity for FHWA to identify options it can use to evaluate whether the committed spending data it uses to determine if state DOTs have met their DBE goals is a reasonable proxy for actual spending and whether this data can be relied on to measure progress towards goals. For example, on a nationwide basis, FHWA could compare committed to actual spending—using historical data on committed and actual spending on completed contracts—to determine whether committed spending reflects actual spending on DBEs.

Reporting of Committed Spending Does Not Include Statements about Potential Limitations

We have previously reported that while no data are perfect, agencies need to report any limitations of performance data to provide transparent information on government operations so that decision makers, such as members or committees of Congress and program managers, can use the information appropriately.[55] In addition, recent initiatives, such as a June 2011 Executive Order on accountable government[56] and the GPRA

[53]To help state DOTs meet their DBE goals, state DOTs can take various actions, including setting DBE goals on individual U.S. DOT-assisted contracts. The DBE regulations state that if a state DOT determines that it will exceed its DBE goal, the state DOT must reduce or eliminate the use of contract goals to the extent necessary to ensure that the use of contract goals does not result in exceeding its state DOT DBE goal. 49 C.F.R. § 26.51(f)(2).

[54]According to this U.S. DOT official, improvements related to the Uniform Report are being considered for inclusion in a Notice of Improved Rulemaking to further improve DBE program administration.

[55]GAO, *Performance Reporting: Few Agencies Reported on the Completeness and Reliability of Performance Data*, GAO-02-372 (Washington D.C.: Apr. 26, 2002).

[56]Exec. Order No. 13576, 76 Fed. Reg. 35297 (June 16, 2011).

Modernization Act of 2010 (GPRAMA)[57] have placed increased emphasis on transparency, including enhancing the transparency of federal spending. Transparency of DBE spending data is important because it helps stakeholders oversee and monitor progress of the DBE program. However, FHWA's reporting of data on committed spending to describe progress towards DBE goals does not include statements about potential limitations of the data—namely that the data on committed spending on DBEs might not reflect actual spending. For example, in a March 2009 hearing on the DBE program,[58] U.S. DOT reported to the House of Representatives Committee on Transportation and Infrastructure that DBEs were awarded $3.3 billion in contracts, representing more than 11 percent of the total federal amount provided through U.S. DOT-assisted contracts in fiscal year 2008.[59, 60] In this example, U.S. DOT did not explicitly state that "awarded contracts" (committed spending) might not be the same as actual spending, and that it was using "awarded contracts" as a convention to facilitate reporting. Including statements about potential limitations of committed spending data in the information it provides to decision makers, including Congress, could help FHWA increase transparency in the reporting of DBE spending data.

[57]Pub. L. No. 111-352, 124 Stat. 3866 (2011). GPRAMA was enacted in January 2011 and amends the Government Performance and Results Act of 1993, Pub. L. No. 103-62, 107 Stat. 285 (1993). Specifically, GPRAMA requires U.S. DOT and other federal agencies to disclose more information about the accuracy and validity of performance information (by Feb. 27, 2012), including the sources for their data and actions to address limitations of the data. For more information about GPRAMA, see GAO, *Managing for Results: GPRA Modernization Act Implementation Provides Important Opportunities to Address Government Challenges*, GAO-11-617T (Washington, D.C.: May 10, 2011).

[58]U.S. DOT's Disadvantaged Business Enterprise Program, Hearing Before the Committee on Transportation and Infrastructure, House of Representatives, March 26, 2009.

[59]The $3.3 billion reflects awards to DBEs performing work on all U.S. DOT-assisted contracts (i.e., FHWA-, FAA-, and FTA-assisted contracts). Although the $3.3 billion is for all U.S. DOT-assisted contracts, this dollar amount is relevant for our report—which focuses on only FHWA—because it includes awards to DBEs on FHWA-assisted contracts.

[60]23 U.S.C. § 101 requires that U.S. DOT expend at least 10 percent of specified U.S. DOT-assisted funds on DBEs, unless the Secretary of Transportation determines otherwise.

FHWA Oversight of Certifying Organizations

U.S. DOT and three of its operating administrations—FHWA, FTA, and FAA—oversee, review, and monitor the certification activities of all the organizations that certify DBEs in a state.[61] Officials we interviewed from U.S. DOT's and FHWA's Offices of Civil Rights described an oversight approach in which the oversight of the certification activities of the organizations that certify DBEs is delegated to one of the administrations—depending on which administration provides federal funding to the organization.[62] For example, FHWA is responsible for overseeing the certification activities of state DOTs—which primarily certify DBEs that work on highway projects—because these state DOTs receive federal-aid highway funds. FTA and FAA are responsible for overseeing certifying organizations, such as state transit agencies and local airport authorities, that receive federal transit and aviation funds, respectively. Defining roles and responsibilities in this way can help federal agencies effectively oversee programs, particularly when multiple federal entities are involved in oversight.[63] In addition to FHWA's, FAA's, and FTA's responsibilities for certification oversight, officials from U.S. DOT's Office of Civil Rights said that their role, prior to the 2011 update to the DBE regulations, was and continues to be to review and make decisions on DBE certification appeals.[64] According to officials, under the updated DBE regulations that went into effect in February 2011, U.S. DOT's Office of Civil Rights will have additional responsibilities to enforce and oversee DBE certifications.[65]

FHWA officials we interviewed said that their responsibilities for overseeing state DOT DBE programs included overseeing the state

[61]Some states have multiple organizations within the state—such as state DOTs, state and local transit agencies, and local airport authorities—that certify DBEs.

[62]In cases where a certifying organization receives funding from more than one administration, such as a city or county government, each of the administrations providing the funding can oversee the certifying organization's activities, either concurrently or independently.

[63]GAO/AIMD-00-21.3.1. See also GAO, *Department of Energy: Improved Oversight Could Better Ensure Opportunities for Small Business Subcontracting*, GAO-05-459 (Washington, D.C.: May 13, 2005).

[64]Specifically, U.S. DOT's Office of Civil Rights reviews DBE certification appeals when a firm requests that the office review a certifying organization's decision to deny or remove the firm from being certified. *See* 49 C.F.R. § 26.89.

[65]76 Fed. Reg. 5083 (Jan. 2011).

DOTs' certification activities. As discussed earlier in this report, FHWA oversees state DOTs' implementation of the DBE program—including how state DOT's certify DBEs—using risk assessments and program reviews. For example, in conducting their annual risk assessments, FHWA's Office of Civil Rights and FHWA division offices consider risks related to the DBE program, including how state DOTs certify DBEs. Furthermore, in the 2010 and 2011 program reviews, FHWA division offices assessed whether state DOTs were following U.S. DOT's regulatory eligibility requirements and certification procedures when they certified DBEs. In addition to these activities, U.S. DOT's Inspector General's Office (IG) has a role in overseeing DBE certifications. In April 2011, the IG announced that it would conduct an audit of the DBE program, and officials from the IG indicated that they plan to review certifications of DBEs as part of this audit.

In addition to risk assessments and program reviews, all five FHWA division offices we focused on conducted additional oversight activities to oversee the certification activities of state DOTs. As is the case with the oversight of other aspects of the DBE program and other federal-aid highway programs, FHWA divisions use their discretion to determine how much and how often to carry out these additional oversight activities. For example, one FHWA division participates in annual reviews of the state's DBE certification processes, procedures, and activities—which includes conducting spot-checks of selected certification files and interviewing personnel engaged in managing, supervising, and performing certification activities.[66] Another division official said that because DBE certifications are not a high-risk area in his state, he oversees the state DOT's certification activities when there are questions or concerns with a specific certification decision.

Furthermore, FHWA officials in three of the four states that have multiple certifying organizations said that they rely on FAA and FTA to oversee the certification activities of organizations other than the state DOT (such as transit agencies and airport authorities).[67] FTA's and FAA's oversight of

[66]In this example, the state DOT has entered into an interagency agreement with another agency in the state to perform DBE certifications.

[67]In the fourth state with multiple certifying organizations, an FHWA division official said that his office shares its responsibility for overseeing the certification activities of state and local airport and transit organizations with FAA and FTA.

these organizations is relevant for federal-aid highway projects because these organizations certify DBEs that can work on highway projects. For example, officials from one certifying organization we interviewed said that while it is a transit agency, about 40 percent of the DBEs it certifies could work on transit projects as well as other types of projects, such as highway projects, because the skills needed for transit and highway projects are similar. According to U.S. DOT officials, it is common for a DBE to work on more than one type of project, such as on airport and highway projects. In general, FAA and FTA officials we obtained information from said that they conduct compliance reviews to oversee the certification activities of these other organizations. See appendix IV for more information on the actions FAA and FTA take to oversee the certification activities of the organizations they are responsible for overseeing.

Conclusions

U.S. DOT's DBE program has existed for more than 30 years and provided billions of dollars to DBEs across the country. FHWA's oversight of how state DOTs implement their DBE programs is critical for ensuring that the programs are implemented according to U.S. DOT's DBE regulations. FHWA has taken several steps, some of which have been recently implemented, which could help ensure state DOTs' compliance with DBE regulations. However, FHWA faces fundamental problems in the data it uses to oversee DBE participation. Knowing whether a program is meeting its goals and ensuring that data accurately reflects federal dollars spent is a primary responsibility of oversight. Without addressing its fundamental data problems, FHWA cannot effectively make program decisions and implement DBE regulations. For example, if the extent to which state DOTs are meeting their goals is unclear, FHWA will not be able to effectively hold state DOTs accountable for meeting their DBE goals, as emphasized in U.S. DOT's update to its regulations. Further, without addressing its data problems, FHWA cannot be sure that the data that shows that about half of the state DOTs are meeting their DBE goals from fiscal years 2006 through 2010 is accurate. U.S. DOT's working group that considers various improvements to the administration of the DBE program provides FHWA with an opportunity to identify options it can use to evaluate whether the committed spending data it uses to determine if state DOTs have met their DBE goals is a reasonable proxy for actual spending and whether this data can be relied on to measure progress towards goals. Additionally, including statements about the potential limitations of committed spending data in information it provides to decision makers could help FHWA increase transparency in the reporting of DBE spending data.

Recommendations for Executive Action

To know whether its data on committed spending can be relied on to determine state DOTs' progress in meeting goals, to enhance FHWA's ability to know whether state DOTs meet their DBE goals, and to help increase transparency in the reporting of spending on DBEs, the Secretary of Transportation should direct the FHWA Administrator to take the following two actions:

1. Evaluate whether its committed spending data is a reasonable proxy for determining whether state DOTs are meeting their DBE goals.

2. In the information it provides to decision makers, including Congress, include statements about potential limitations of the data it uses to determine state DOTs' progress towards goals.

Agency Comments and Our Evaluation

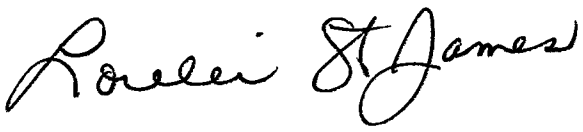
We provided a draft of this report to the Department of Transportation for review and comment. We received e-mail and oral comments on the draft report from U.S. DOT through the department's liaison. Our draft report recommended that (1) FHWA identify and use data that are reliable and accurately reflect whether state DOTs have met their DBE goals, and (2) FHWA clearly note in reports to decision makers, including Congress, that FHWA's data might not represent actual DBE spending until FHWA identifies and uses reliable data. U.S. DOT's comments on our draft recommendations covered two broad areas: the reliability of committed spending data and data limitations. Specifically, U.S. DOT commented that the committed spending data that FHWA is using is the most reliable and accurate data available to determine on a timely basis whether state DOTs are meeting their DBE goals. U.S. DOT also commented that the information presented in our report on committed spending does not relate to the reliability of the committed spending data but rather relates to the reporting of these data. However, as stated in our report, FHWA may or may not be able to rely on committed spending data to measure progress towards goals because FHWA does not know whether committed spending is a reasonable proxy for actual spending. We clarified our first recommendation to better reflect the need for FHWA to evaluate if the proxy data can be relied on to determine whether state DOTs are meeting their DBE goals. U.S. DOT agreed to consider our modified recommendation. Regarding the second recommendation, U.S. DOT officials commented that ensuring that the appropriate methodological disclosures are included in their reporting was not enough of an issue to warrant a recommendation. As we note in our report, including statements about the potential limitations of spending data is important because it improves transparency of the data so that decision makers can oversee and monitor progress of the DBE program

appropriately. Consequently, we retained this recommendation with slightly revised language. U.S. DOT officials noted that they would re-evaluate their disclosures with regard to the data used to determine if DBE goals are met. Finally, U.S. DOT provided technical comments, which we incorporated as appropriate throughout the report.

As agreed with your office, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to the U.S. Department of Transportation and other interested parties. In addition, the report is available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions about this report, please contact me at (202) 512-2834 or stjamesl@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix V.

Sincerely yours,



Lorelei St. James
Director, Physical Infrastructure Issues

Appendix I: Objectives, Scope, and Methodology

This report focuses on the Federal Highway Administration's (FHWA) oversight of the U.S. Department of Transportation's (DOT) Disadvantaged Business Enterprise (DBE) program on federally assisted highway projects.[1] Specifically, the objectives of this report were to examine how FHWA (1) oversees state DOTs to ensure that they are implementing their DBE programs in accordance with applicable regulations, (2) assesses whether state DOTs have met their DBE goals, and (3) oversees organizations that certify DBEs that work on federal-aid highway projects.

To address all three of our objectives, we reviewed relevant laws, regulations, U.S. DOT and FHWA documents on the DBE program, and GAO and other reports. Specifically, we reviewed the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU)[2] and other relevant legislation, such as the Surface Transportation Assistance Act of 1982 (STAA),[3] which authorized U.S. DOT's DBE program. In addition, we reviewed the GPRA Modernization Act of 2010 (GPRAMA)[4] and Executive Order 13576 on delivering an efficient, effective, and accountable government.[5] We also reviewed U.S. DOT's regulations on the DBE program that describe state DOTs' requirements for implementing the DBE program, as well as proposed and final rules that U.S. DOT published in the *Federal Register* which recently amended DBE regulations.[6] We also reviewed and analyzed U.S. DOT, FHWA Office of Civil Rights, and FHWA division office documents on the DBE program, including procedures and guidance on DBE goals, certifications, DBE program implementation, and oversight of the DBE program. Furthermore, we reviewed and analyzed prior GAO reports and other reports on the DBE program, oversight, and accountability in the federal government, including GAO standards and

[1]This report focuses on FHWA's oversight of projects receiving federal-aid highway funds, including American Recovery and Reinvestment Act of 2009 (Recovery Act) funds.

[2]Pub. L. No. 109-59, 119 Stat. 1144 (2005).

[3]Pub. L. No. 97-424, § 105(f), 96 Stat. 2097, 2100 (1983), as amended at 23 U.S.C. § 101 note.

[4]Pub. L. No. 111-352, 124 Stat. 3866 (2011). GPRAMA amends the Government Performance and Results Act of 1993, Pub. L. No. 103-62, 107 Stat. 285 (1993).

[5]Exec. Order No. 13576, 76 Fed. Reg. 35297 (June 16, 2011).

[6]75 Fed. Reg. 25815 (May 2010), 76 Fed. Reg. 5083 (Jan. 2011).

guidance on internal controls. We used some of these reports to assess FHWA's oversight of the DBE program.

Furthermore, we conducted semistructured interviews on topics related to our objectives. In particular, we reviewed documentation and interviewed officials from U.S. DOT and FHWA in headquarters, including officials from U.S. DOT's Office of General Counsel, U.S. DOT's Office of Civil Rights, and FHWA's Office of Civil Rights. In addition, we conducted semistructured interviews with representatives from associations, including the American Association of State Highway and Transportation Officials, Associated General Contractors of America, American Road & Transportation Builders Association, Conference of Minority Transportation Officials, and National Association of Minority Contractors. We interviewed officials from these associations because they are national associations knowledgeable about the DBE program, and because these national associations represent various stakeholders involved in the DBE program, such as state DOT officials and contractors. We also reviewed documentation from and interviewed officials in five states: Florida, Minnesota, Missouri, Washington, and Wisconsin.[7] We judgmentally selected these states to obtain variation in geographic location, state population, state DOT use of race-conscious and/or race-neutral methods to meet DBE goals, whether state DOTs met their overall DBE goals, and number of certifying organizations within the states. We also considered whether the state used a disparity study to determine its DBE participation goal,[8] whether the state was involved in litigation regarding the DBE program, whether the state was located within the jurisdiction of the U.S. Court of Appeals for the Ninth Circuit,[9] and recommendations from stakeholders who are familiar with the DBE program. We visited Florida because it was the only state mentioned by

[7]Since these states were selected as a nonprobability sample, the information we gathered from officials in these states cannot be generalized to all states.

[8]State DOTs must set DBE goals based on, in part, the availability of DBEs in the relevant market area. Although not required by U.S. DOT's DBE regulations, some states conduct a study—called a disparity study—to demonstrate the availability of DBEs.

[9]We considered state DOTs located within the jurisdiction of the U.S. Court of Appeals for the Ninth Circuit as part of our state selection criteria because stakeholders we interviewed said that the court's decision—in *Western States Paving Co. v. Washington State Department of Transportation*, 407 F.3d 983 (9th Cir. 2005)—had a significant impact on how state DOTs located in the Ninth Circuit implemented U.S. DOT's DBE program. The court held that that Washington's DBE program was not narrowly tailored because the evidence supporting past discrimination was inadequate.

stakeholders that met its goal by using only race-neutral methods. In each of the selected states, we interviewed FHWA division officials and state DOT Civil Rights and DBE Program managers. Finally, in Florida, Wisconsin, and Washington, we interviewed prime contractors and DBE firms, or organizations in the state that represented the DBE firms.

In addition to these efforts, to describe how FHWA oversees state DOT DBE programs to ensure that the state DOTs are complying with DBE regulations, we reviewed and analyzed information related to FHWA's oversight activities.[10] For example, we obtained and reviewed documentation from FHWA's Office of Civil Rights and FHWA divisions on FHWA's risk assessment process and DBE program reviews. We also conducted semistructured interviews with the National Review Team (NRT) that FHWA established to assess DBE program implementation on Recovery Act projects.[11] We also reviewed the findings of the NRT's review, which provided a programmatic assessment of oversight at a national level while also providing insights for the specific states we selected for this review. We also reviewed the Action Plans from our five selected states to see how those divisions explained how they oversee state DOT DBE programs.

To determine how FHWA assesses whether state DOTs have met their DBE goals, we reviewed and analyzed FHWA's national data on state DOTs' committed and actual spending and how FHWA determined whether state DOTs achieved their DBE goals over a 5-year period (fiscal years 2006 through 2010) for state DOTs in all 50 states, the District of Columbia, and Puerto Rico.[12] FHWA officials said they compiled the national data from state DOTs' *Uniform Report of DBE Awards or Commitments and Payments* (commonly referred to as the Uniform Report). To help ensure the accuracy of the national data, we conducted selected quality checks of the data and we discussed and resolved any

[10]We did not assess the effectiveness of FHWA's oversight efforts since some of FHWA's oversight efforts were recently initiated and it would be too soon to determine the effectiveness of such efforts.

[11]Although the NRT's review focused on Recovery Act projects, the data and analyses gathered by the team were useful for our review because DBE requirements are the same for Recovery and non-Recovery Act projects.

[12]For this report, we use the term "state DOTs" to refer to state DOTs in all 50 states, the District of Columbia, and Puerto Rico.

inconsistencies in the data we identified with the appropriate agency officials. We also compared FHWA's national data to the data in the Uniform Reports for the five state DOTs that we contacted, and resolved inconsistencies with FHWA and the state DOTs. Given our review of the data provided to us by FHWA, we identified problems with the data FHWA uses to assess whether state DOTs achieved their DBE goals. These issues are discussed in this report. Even so, our review of FHWA's national data provided us with a perspective on how FHWA compiled and used these data. Additionally, because data on actual spending on DBEs cannot be used to determine if state DOTs met their DBE goals, in appendix III, we determined the number and percentage of state DOTs meeting overall DBE goals based on committed spending data on DBEs for all state DOTs to illustrate orders of magnitude. We did not evaluate the appropriateness of the state DOT DBE goals.

Finally, to determine how FHWA oversees organizations that certify DBEs, we obtained information or interviewed officials from U.S. DOT's and FHWA's Offices of Civil Rights, and the Federal Aviation Administration's (FAA) and Federal Transit Administration's (FTA) Offices of Civil Rights. Although our report focuses on FHWA's oversight of the DBE program, we obtained information from officials at FAA and interviewed an official from FTA since DBEs can be certified to work on highway, airport, and transit projects, and since FAA and FTA, in addition to FHWA, can be involved in overseeing the certifications of DBEs that work on federal-aid highway projects. We did not examine FAA's or FTA's oversight of the DBE program on federally funded airport and transit projects, or airport concessions contracts. We reviewed how FHWA oversaw the certification activities of the organizations in the state. In addition, in each of the states selected, we interviewed state or local officials from at least two organizations that certify DBEs within each state, if such existed—such as state transit agencies and local airport authorities. We judgmentally selected the certifying organizations based on their geographic location, whether they certified DBEs that work on highway projects, and whether the organization was a state DOT.

We conducted this performance audit from September 2010 to October 2011 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Summary of Key DBE Regulatory Eligibility Requirements

To be a Disadvantaged Business Enterprise (DBE), firms must meet certain regulatory eligibility requirements concerning socially and economically disadvantaged status, business size, ownership, and control. Table 1 summarizes the key elements of each of the eligibility requirements.

Table 1: Summary of Key DBE Eligibility Requirements

Eligibility requirement	Key elements of eligibility requirement
Socially and economically disadvantaged status	Each owner of the firm must be socially and economically disadvantaged. Members of the following groups are presumed to be socially and economically disadvantaged, unless proven otherwise: Black Americans, Hispanic Americans, Native Americans, Asian-Pacific Americans, Subcontinent Asian Americans, women, or other groups as designated by the U.S. Small Business Administration (SBA). Furthermore, each owner of the firm must have a personal net worth that does not exceed $1.32 million.[a]
Business size	Each DBE firm must be an existing small business as defined by SBA size standards,[b] and each fiscal year cannot have average annual gross receipts over the 3 previous fiscal years that exceed the small business size cap associated with the type of work it performs and in no case may exceed an overall U.S. Department of Transportation-specific cap (currently $22.41 million).[c]
Ownership	A DBE firm must be at least 51 percent owned by socially and economically disadvantaged individuals.[d]
Control	A DBE owner must possess the power to control the management and policies of the firm, and make day-to-day and long-term decisions on the firm's management, policy, and operations. A DBE firm must not be subject to any restrictions (e.g., corporate charter provisions or voting powers attached to different classes of stock) that would limit the socially and economically disadvantaged owners from making any business decisions of the firm. Any delegations of authority must be revocable. Additionally, the DBE firm must be an independent business, meaning that the viability of the business cannot depend on its relationship with another firm or firms. Furthermore, a DBE owner must have managerial and technical competence and experience directly related to the type of business in which the firm is engaged and the firm's operations. And finally, a DBE owner cannot engage in outside employment or other business that conflicts with the management of the firm or prevent sufficient time to be devoted to the firm.[e]

Source: GAO Summary of eligibility requirements in 49 C.F.R. part 26.

[a]49 C.F.R. §§ 26.61, 26.67. See 49 C.F.R. appendix E. Firms owned and controlled by those who are not presumed to be socially and economically disadvantaged (including individuals whose presumed disadvantaged has been rebutted) may qualify for the program if the owner can demonstrate, by a preponderance of the evidence, social and economic disadvantage. However, no individual whose personal net worth exceeds $1.32 million may be considered economically disadvantaged. *Id.* In February 2011, U.S. DOT increased the personal net worth cap from $750,000 to $1.31 million. 76 Fed. Reg. 5083 (Jan. 2011).

[b]13 C.F.R. part 121.

[c]49 C.F.R. § 26.65.

[d]49 C.F.R. § 26.69(b).

[e]49 C.F.R. § 26.71.

Appendix III: Number and Percentage of State DOTs Meeting DBE Goals Based on Committed Spending Data from Uniform Reports, Fiscal Years 2006 through 2010

The U.S. Department of Transportation's (DOT) Disadvantaged Business Enterprise (DBE) regulations require that each state DOT set an annual goal for DBE participation in federal-aid highway projects, expressed as the percent of federal-aid highway funds it will expect to spend on DBEs for contracts that are awarded or committed in a fiscal year. The regulations also require that all state DOTs report to the Federal Highway Administration (FHWA) the total amount of federal funds they commit to spend on DBEs using a form called the *Uniform Report of DBE Awards or Commitments and Payments* (commonly referred to as the Uniform Report). FHWA uses this data on committed spending on DBEs to determine whether state DOTs are meeting their DBE goals each fiscal year. Based on the committed spending data in the Uniform Reports, about half of the state DOTs met their DBE goals each fiscal year from fiscal years 2006 through 2010. See table 2.

Table 2: Number and Percentage of State DOTs Meeting DBE Goals Based on Committed Spending Data from Uniform Reports, Fiscal Years 2006 through 2010

Fiscal year	Number of state DOTs that met their DBE goal	Percentage of state DOTs that met their DBE goal
2006	23	44%
2007	24	46
2008	19	37
2009	19	37
2010	24	46

Source: GAO analysis of FHWA data.

Appendix IV: How FAA and FTA Oversee the Certifying Organizations for Which They Are Responsible

The Federal Aviation Administration (FAA) and the Federal Transit Administration (FTA) oversee the certification activities of organizations they provide funding to, such as airport and transit organizations. While this report does not focus on these administrations' oversight of Disadvantaged Business Enterprise (DBE) certifications, we obtained information from officials at FAA and interviewed an FTA official to obtain a general understanding of their involvement in overseeing DBE certifications. Some of their oversight activities are described in the following sections.

FAA

FAA officials said that they oversee the certification activities of airport authorities when they conduct compliance reviews of these authorities. These compliance reviews can include an analysis of an airport authority's responsibilities for DBE certifications or the airport authority's capacity as a certifying organization. FAA officials also indicated that they may also ask the airport authorities and other certifying organizations in the state to review particular certification decisions or procedure as a result of a complaint, investigation, compliance review, U.S. Department of Transportation Office of Inspector General finding, or court determination.

FTA

An FTA official we interviewed explained that although FTA usually does not oversee the certification activities of any organizations that certify DBEs, including certification decisions made by transit agencies, it provides technical assistance to the organizations on certification issues.[1] In addition, FTA reviews the DBE program during its triennial reviews[2] and, when funding is available, conducts certification compliance reviews. In 2009, FTA began conducting compliance reviews of each state's certification procedures and standards to ensure that their activities align

[1]According to this FTA official, U.S. DOT's Office of Civil Rights and Office of General Counsel are responsible for overseeing the certification activities of all certifying agencies, including those that receive transit funds, because DBE certifications have an agencywide impact.

[2]FTA's triennial reviews evaluate the extent to which recipients of federal transit funds are meeting federal requirements. The triennial review covers 23 areas, including procurement, financial management, drug and alcohol programs, and the DBE program. In 2009, we evaluated FTA's triennial review program. See GAO, *Public Transportation: FTA's Triennial Review Program Has Improved, but Assessments of Grantees' Performance Could Be Enhanced*, GAO-09-603 (Washington, D.C.: June 30, 2009).

with the U.S. Department of Transportation's DBE regulations on certifications. According to an FTA official, FTA has completed between six to ten certification compliance reviews to date and has plans to conduct more reviews in subsequent years.

Appendix V: GAO Contact and Staff Acknowledgments

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Staff Acknowledgments

In addition to the contact named above, Catherine Colwell, Assistant Director; Lauren Calhoun; Colin Fallon; Roshni Davé; Peter Del Toro; Leia Dickerson; Joseph Fread; Sara Ann W. Moessbauer; Josh Ormond; Lisa Shibata; and Sandra Sokol made key contributions to this report.

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