

# EVALUATION REPORT

## SBA's FY 2016 COMPLIANCE WITH THE IMPROPER PAYMENTS ELIMINATION AND RECOVERY ACT





# EXECUTIVE SUMMARY

Report No. 17-12

May 10, 2017

## SBA's FY 2016 COMPLIANCE WITH THE IMPROPER PAYMENTS ELIMINATION AND RECOVERY ACT

### What OIG Reviewed

This evaluation report represents the results of the Office of Inspector General's (OIG's) evaluation of the Small Business Administration's (SBA's) compliance with the Improper Payments Elimination and Recovery Act of 2010 (IPERA).

Our objectives were to (1) determine whether SBA complied with IPERA using guidelines outlined in Office of Management and Budget (OMB) Memorandum M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments*, and (2) assess progress SBA made in remediating improper payment-related recommendations.

### What OIG Found

SBA generally continued to make progress in its efforts to prevent and reduce improper payments, as summarized in the following table.

#### OIG IPERA Qualitative Assessment for FY 2016 by Program or Activity

SBA Program or Activity	Status
7(a) Loan Guaranty Purchases	Progress
7(a) Loan Guaranty Approvals	Substantial Progress
504 CDC Loan Guaranty Approvals	Substantial Progress
Disaster Direct Loan Disbursements	Implemented
Disbursements for Goods and Services	Implemented
Hurricane Sandy Disaster Relief Administrative Expenses	Implemented
Hurricane Sandy Disaster Relief Grants	Substantial Progress

In accordance with IPERA, SBA published and posted an agency financial report (AFR) on its website, conducted program-specific risk assessments, published improper payment estimates for all programs and activities identified as susceptible to significant improper payments, published extracts from the applicable programmatic corrective action plans in the AFR that reported a gross improper payment rate of less than 10 percent for six of seven areas tested for fiscal year 2016 reporting, and published and

met the annual reduction target for six of the applicable seven areas tested.

However, SBA was not compliant with IPERA reporting requirements because disbursements for goods and services had an improper payment rate that exceeded the 10 percent threshold; and 7(a) loan guaranty purchases did not meet their annual reduction target.

### OIG Recommendations

We made two recommendations to improve the effectiveness of improper payment controls over 7(a) loan guaranty purchases.

### Agency Response

SBA management agreed with the findings and recommendations of this report. Within 90 days of this report, the agency plans to take action to address both recommendations. For recommendation 1, SBA intends to submit a plan to the Senate Committee on Homeland Security and Governmental Affairs, the House Committee on Oversight and Government Reform, and OMB describing the actions that the agency will take to address its non-compliance with IPERA regarding the Section 7(a) loan guaranty purchase program. For recommendation 2, SBA intends to provide OMB and OIG its analysis to support the agency's position that 7(a) guaranty purchase recapture audits are not cost effective. We commend SBA's efforts for implementing the new controls to reduce improper payments for disbursements for goods and services. We encourage the agency to continue improving its review processes to decrease the number of improper payments.



**U.S. SMALL BUSINESS ADMINISTRATION  
OFFICE OF INSPECTOR GENERAL  
WASHINGTON, D.C. 20416**

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**Final Report Transmittal**  
Report Number: 17-12

**DATE:** May 10, 2017

**TO:** Linda E. McMahon  
Administrator

A handwritten signature in black ink, appearing to be "H. Ware", written over a light blue horizontal line.

**FROM:** Hannibal "Mike" Ware  
Acting Inspector General

**SUBJECT:** *SBA's FY 2016 Compliance with the Improper Payments Elimination and Recovery Act*

This report represents the results of our evaluation of the Small Business Administration's (SBA) fiscal year 2016 compliance with the Improper Payments Elimination and Recovery Act (IPERA). Our objectives were to (1) determine whether SBA complied IPERA using guidelines outlined in the Office of Management and Budget (OMB) Memorandum M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments*, and (2) assess the progress SBA made in remediating improper payment-related recommendations.

We previously furnished copies of the draft report and requested written comments on the recommendations. SBA management's comments are appended and were considered in finalizing the report. The report contains two recommendations that SBA agreed to address. Recommendations 1 and 2 will remain open until OIG receives documentation demonstrating that these recommendations have been addressed. Please provide us within 90 days your progress in addressing these recommendations.

We commend the agency's efforts for implementing the new controls to reduce improper payments for disbursements for goods and services. We encourage the agency to continue improving its review processes to decrease the number of improper payments.

Please contact me if you would like to discuss this report or any related issues.

cc: Mary Anne Bradfield, Chief of Staff  
Timothy Gribben, Chief Financial Officer and Associate Administrator for Performance Management  
William Manger, Associate Administrator for Capital Access  
James Rivera, Associate Administrator for Disaster Assistance  
Lori Gillen, Deputy Associate Administrator for Entrepreneurial Development  
Eric S. Benderson, Acting General Counsel  
Martin Conrey, Attorney Advisor, Legislation and Appropriations  
LaNae Twite, Director, Office of Internal Control

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## Introduction

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The Improper Payments Information Act of 2002 (IPIA) requires agencies to review and identify programs susceptible to significant improper payments, report on the amount and causes of improper payments, and develop plans for reducing improper payments.<sup>1</sup> An improper payment is any payment that should not have been made or that was made in an incorrect amount under statutory, contractual, administrative, or other legally applicable requirements. Incorrect amounts are overpayments or underpayments made to eligible recipients (including inappropriate denials of payment or service, any payment that does not account for credit for applicable discounts, payments that are for an incorrect amount, and duplicate payments). An improper payment also includes any payment made to an ineligible recipient or for an ineligible good or service, or payments for goods or services not received (except for such payments authorized by law). In addition, when an agency's review is unable to discern whether a payment was proper as a result of insufficient or lack of documentation, this payment must also be considered an improper payment.

## Background

In accordance with the Office of Management and Budget (OMB) guidance, each Office of Inspector General (OIG) is required to annually review their agency's improper payments reporting within 180 days of issuing their performance and accountability report (PAR) or agency financial report (AFR).<sup>2</sup> In doing so, we performed a qualitative assessment of the Small Business Administration's (SBA's) progress in meeting the following criteria:

- overall assessment of agency efforts to prevent and reduce improper payments
- evaluation of whether agency corrective action plans are robust and focused on the appropriate root causes of improper payments
- evaluation of agency's performance in reducing and recapturing improper payments

OMB further requested OIGs to determine whether agencies were in compliance with the Improper Payments Elimination and Recovery Act of 2010 (IPERA). To be in compliance with IPERA, agencies must have, at a minimum, completed the following:

- published a PAR or AFR for the most recent fiscal year and posted that report and any accompanying materials required by OMB on the agency website
- conducted a program-specific risk assessment for each applicable program or activity that conforms with Section 3321 note of Title 31 U.S.C. (if required)
- published improper payments estimates for all programs and activities identified as susceptible to significant improper payments under its risk assessment (if required)
- published programmatic corrective action plans in the PAR or AFR (if required)
- published and met annual reduction targets for each program assessed to be at risk and measured for improper payments (if required and applicable)<sup>3</sup>

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<sup>1</sup> IPIA was amended by IPERA and the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA). IPERIA directed OMB to issue implementation guidance to agencies. OMB issued Memorandum M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments*, as implementation guidance to Federal agencies for IPERIA.

<sup>2</sup> OMB Memorandum M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments* (October 14, 2014).

<sup>3</sup> A program will have met a reduction target if its improper payment rate falls within +/- 0.1 percent of the reduction target set in the previous year's PAR or AFR.

- reported a gross improper payment rate of less than 10 percent for each program and activity for which an improper payments estimate was obtained and published in the PAR or AFR

If an agency does not meet one or more of these requirements, then it is not in compliance with IPERA. For agencies that are not compliant for 1 fiscal year, within 90 days of the determination of noncompliance, the agency shall submit a plan to the Senate Committee on Homeland Security and Governmental Affairs, the House Committee on Oversight and Government Reform, and OMB describing the actions that the agency will take to become compliant. For agencies that are not compliant for 2 consecutive fiscal years for the same program or activity, the Director of OMB will review the program and determine whether additional funding would help the agency come into compliance. For agencies that are not compliant for 3 consecutive fiscal years for the same program or activity, within 30 days of the determination of noncompliance, the agency will submit to Congress reauthorization proposals for each discretionary program or activity or proposed statutory changes necessary to bring the program or activity into compliance.

### **Prior Work**

Prior OIG audits have identified high percentages of disaster and business loans that were made to borrowers who were ineligible, lacked repayment ability, or did not provide sufficient documentation to justify the approval or disbursement. Certain audits further determined that the improper payment rates reported for the 7(a) Loan Program were significantly understated.

OIG's fiscal year (FY) 2015 IPERA review found that SBA continued to make progress in its efforts to prevent and reduce improper payments. More specifically, we found that SBA published and posted an AFR on its website, conducted program-specific risk assessments, published improper payment estimates for all programs and activities identified as susceptible to significant improper payments, published extracts from the applicable programmatic corrective action plans in the AFR, reported a gross improper payment rate of less than 10 percent for six of seven areas tested for FY 2015 reporting, and published and met the annual reduction target for three of the applicable seven areas tested. However, SBA was not compliant with IPERA reporting requirements; disbursements for goods and services had an improper payment rate that exceeded the 10 percent threshold; and Sections 7(a) and 504 loan guaranty approvals, Hurricane Sandy disaster relief grants, and disbursements for goods and services did not meet their annual reduction target.

### **Objectives**

Our objectives were to (1) determine whether SBA complied with IPERA using guidelines outlined in OMB Memorandum M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments*, and (2) assess progress SBA made in remediating improper payment-related recommendations. More specifically, we assessed the status of OIG's open prior year audit recommendations, which focused on the accuracy and completeness of SBA's reporting, and performance in reducing and recapturing improper payments.

## Results

SBA continued to make progress in preventing and reducing improper payments. For FY 2016, SBA again reported that it brought its Disaster Loan program's improper payment rate below 10 percent. However, we found that two of seven areas did not meet the minimum requirements for IPERA compliance.<sup>4</sup> Section 7(a) loan guaranty purchases were not compliant because they did not meet their annual reduction target, and disbursements for goods and services were noncompliant because the reported improper payment rate exceeded 10 percent (see Table 1). We have divided our review into seven sections: one for each program or activity that has been identified as susceptible to improper payments.

**Table 1. Summary of SBA's IPERA Compliance**

Program or Activity	Posted materials	Assessed risk <sup>5</sup>	Published estimates for susceptible programs	Published programmatic corrective action plans	Published and met annual reduction target	Reported rate of less than 10 percent	Overall FY 2016 Results
Section 7(a) Loan Guaranty Purchases	☑	☑	☑	☑	■	☑	■
Section 7(a) Loan Guaranty Approvals	☑	☑	☑	☑	☑	☑	☑
Section 504 CDC Loan Guaranty Approvals	☑	☑	☑	☑	☑	☑	☑
Disaster Direct Loan Program	☑	☑	☑	☑	☑	☑	☑
Disbursements for Goods and Services	☑	☑	☑	☑	☑	■	■
Hurricane Sandy Disaster Relief Administrative Expenses	☑	☑	☑	☑	☑	☑	☑
Hurricane Sandy Disaster Relief Grants	☑	☑	☑	☑	☑	☑	☑

Legend: ☑ Compliant with IPERA reporting requirements  
 ■ Not compliant with IPERA reporting requirements

<sup>4</sup> OIG is reporting on the results of seven sections as opposed to nine reflected in the AFR because we combined Hurricane Sandy Disaster Relief Administrative Expenses (travel, charge card, and payroll) into one section.

<sup>5</sup> All reporting segments have been deemed as susceptible to significant improper payments and are already reporting an estimate. Therefore no risk assessment is required in accordance with OMB Memorandum M-15-02.

## Section 1: Section 7(a) Loan Guaranty Approvals

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### Background

The agency's largest lending program, the 7(a) Loan Program, is SBA's principal vehicle for providing small businesses with access to credit that cannot be obtained elsewhere. This program relies on numerous outside parties (e.g., borrowers, loan agents, and lenders) to complete loan transactions, with at least 78 percent of the loans being made by lenders to whom SBA has delegated loan-making authority. Additionally, SBA has centralized many loan functions and reduced the number of staff performing these functions, placing more responsibility on and giving greater independence to its lenders. Under the 7(a) Loan Program, SBA guarantees up to 90 percent of the principal amount of loans made by banks and other lending institutions to small businesses not able to obtain credit elsewhere. In FY 2016, SBA guaranteed approximately \$24.1 billion in 7(a) loan approvals.

### OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate for 7(a) loan guaranty approvals decreased from 5.59 percent (\$848.1 million) in FY 2015 to 0.96 percent (\$166.8 million) in FY 2016. The most prevalent root cause for 7(a) loan approval improper payments stemmed from the participating lenders' inability to authenticate borrowers' eligibility at loan origination.

SBA noted that the significant decrease from the FY 2015 rate was partially due to not having identified any large improper 7(a) guaranty loan approvals in FY 2016, which was not typical in their testing. However, our review determined that SBA had identified a \$3.75 million improper 7(a) guaranty loan approval, the highest guaranty amount under SBA policy.<sup>6</sup> Additionally, SBA disclosed that the FY 2016 rate was an anomaly, based on the same assertion about the lack of large improper payments, in order to justify the FY 2017 reduction target of 3.9 percent, which is more than four times the FY 2016 rate. Due to the inaccuracy of the AFR disclosures, we downgraded the accuracy and completeness of agency reporting rating from "implemented" in FY 2015 to "substantial progress" for FY 2016.

Further, OMB designated SBA's 7(a) loan guaranty approvals program as high priority in FY 2015 and approved SBA's supplemental measures plan to reduce improper payments. In the FY 2016 AFR, SBA stated that the main tool in reducing improper payments was SBA One, an automated program designed to streamline the 7(a) lending process. We will continue to monitor SBA's progress in reducing 7(a) loan improper payments through lender training and the implementation of SBA One. Table 2 summarizes OIG's evaluation of agency efforts.

**Table 2. OIG's Evaluation of Agency Efforts**

OMB Criteria	Status at End of 2016
Overall assessment of agency efforts	Substantial Progress
Accuracy & completeness of agency reporting	Substantial Progress
Performance in reducing/recapturing improper payments	N/A <sup>7</sup>
Quality of corrective action plans	Substantial Progress

<sup>6</sup> The maximum dollar amount outstanding of SBA's guaranty to any one business (including affiliates) should not exceed \$3,750,000, except when the loan is approved under a program that specifically permits higher amounts.

<sup>7</sup> SBA has determined that the 7(a) loan approval program is not subject to recapture audits because no payment is made at the time of approval.

## AFR Review

Our review of the AFR found that SBA was fully compliant with IPERA reporting requirements. Table 3 summarizes OIG's review of the AFR.

**Table 3. OIG's Review of the AFR**

<b>OMB Reporting Requirement</b>	<b>Status at End of 2016</b>
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Compliant
Reported rate of less than 10 percent	Compliant

## Section 2: Section 7(a) Loan Guaranty Purchases

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### Background

When a loan goes into default, SBA reviews the lender's actions on the loan to determine whether it is appropriate to pay the lender the guaranty, which SBA refers to as a "guaranty purchase." Under its regulations, SBA is released from liability on the guaranty, in whole or in part, within SBA's exclusive discretion, if the lender fails to comply materially with any SBA loan program requirement or does not prudently make, close, service, or liquidate the loan. The guaranty purchase review is SBA's primary control for ensuring lender compliance and preventing improper payments. In FY 2016, SBA purchased approximately \$589 million in 7(a) loan guaranties.

### OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate for 7(a) loan guaranty purchases increased from 0.90 percent (\$7.9 million) in FY 2015 to 2.32 percent (\$13.4 million) in FY 2016. SBA stated that an enhanced test plan including an updated loan review checklist, which required a detailed analysis of creditworthiness (including repayment ability) on early defaulted 7(a) loans, was the reason for the increase in the improper payment rate. The primary root causes for 7(a) loan guaranty purchase improper payments were administrative or process errors made by the agency. SBA formalized a corrective action plan, which included collaboration with the Office of Credit Risk Management (OCRM), internal training, and recovery of unjustified expenses.

Our assessment determined that SBA's FY 2016 AFR disclosures related to payment recapture audits were incomplete and inconsistent. OMB requires agencies to report the results of payment recapture audits in its AFR. While SBA noted in its FY 2016 AFR that a payment recapture audit was conducted, the results were not included. Also, in our interviews with SBA officials, they indicated that a formal payment recapture audit was not conducted, as they believe it would not be cost effective. Upon making this determination, SBA was required to notify OMB and OIG and provide the analysis used to make the decision.

For FY 2016, we have rated the 7(a) guaranty purchase program as "progress." Although SBA is identifying improper payments, SBA did not include the required disclosures for their 7(a) guaranty purchase recapture audits as established by OMB. Table 4 summarizes OIG's evaluation of agency efforts.

**Table 4. OIG's Evaluation of Agency Efforts**

OMB Criteria	Status at End of 2016
Overall assessment of agency efforts	Progress
Accuracy & completeness of agency reporting	Progress
Performance in reducing/recapturing improper payments	Improvement Needed
Quality of corrective action plans	Implemented

### AFR Review

Our review of the AFR found that SBA was compliant with most IPERA reporting requirements. However, the improper payment rate increased from 0.90 percent in FY 2015 to 2.32 percent in FY 2016, and SBA did not meet its planned reduction target of 1.0 percent for the program. Table 5 summarizes OIG's review of the AFR.

OIG periodically conducts audits to assess the accuracy of the agency-reported improper payment rate. OIG currently is assessing the accuracy of the SBA 7(a) Loan Program’s FY 2015 improper payment rate and expects to report our results of this audit in FY 2017.

**Table 5. OIG’s Review of the AFR**

OMB Reporting Requirement	Status at End of 2016
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Not Compliant
Reported rate of less than 10 percent	Compliant

### Recommendations

We recommend that the Director of the Office of Financial Program Operations:

1. Submit to the Senate Committee on Homeland Security and Governmental Affairs, the House Committee on Oversight and Government Reform, and OMB, within 90 days of this report, a plan for the 7(a) guaranty purchase program that includes the following:
  - (a) measurable milestones for becoming compliant with IPERA
  - (b) designation of an accountable senior agency official
  - (c) the establishment of an accountability mechanism, describing the actions the agency will take to become compliant
2. Provide OMB and OIG a complete analysis to justify and support the agency’s position that 7(a) guaranty purchase recapture audits are not cost effective

### Analysis of Agency Response

SBA management provided formal comments that are included in their entirety in Appendix III. SBA management agreed with our recommendations, and its planned actions resolve both of our recommendations. SBA asserted that improved financial performance through the reduction of improper payments continues to be a key financial management focus of the Federal Government. SBA management also stated that they continually develop strategies to reduce improper payments for responsible stewardship of public assets.

### Summary of Action Necessary to Close the Report

The following provides the status of each recommendation and the necessary actions to either resolve or close the recommendation.

Recommendation 1: **Resolved.** SBA concurred that its 7 (a) guaranty loan purchases failed to meet its annual reduction target for 1 year and is subject to the requirements outlined in the recommendation. The Office of Financial Program Operations management stated it will comply within 90 days of the date this report is published. This recommendation can be closed upon SBA providing evidence supporting that it submitted to congressional committees and OMB a plan outlining how it will become compliant with IPERA.

Recommendation 2: **Resolved.** Within 90 days of the date the report is published, the Office of Financial Program Operations will provide OMB and OIG its analysis to support the agency's position that 7(a) guaranty purchase recapture audits are not cost effective.

## Section 3: Section 504 CDC Loan Guaranty Approvals

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### Background

SBA's 504 Loan Program provides small businesses with long-term, fixed-rate financing to purchase land, buildings, machinery, and other fixed assets. Economic development organizations, approved by SBA, are known as certified development companies (CDCs). CDCs package, close, and service these loans, which are funded through a variety of private sector lenders, proceeds from selling SBA-guaranteed debentures, and borrower equity investment. Of the total project costs, a third-party lender provides at least 50 percent of the financing, the CDC provides up to 40 percent of the financing through a 100 percent SBA-guaranteed debenture, and the applicant provides at least 10 percent of the financing. In FY 2016, SBA guaranteed approximately \$4.7 billion in 504 loan approvals.

### OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate for 504 CDC loan guaranty approvals decreased from 3.78 percent (\$158.2 million) in FY 2015 to 2.60 percent (\$119.6 million) in FY 2016. The most prevalent root cause for improper payments in FY 2016 was from the CDC's failure to verify eligibility data. SBA implemented a corrective action plan to reduce and/or eliminate the occurrence of future improper payments. Plans to reduce improper payments include internal and external training as well as collaboration with OCRM to ensure deficiencies are incorporated into OCRM's risk-based reviews.

For FY 2016, we have rated the 504 CDC loan guaranty approvals program as "substantial progress." Following significant increases in FY 2013 to FY 2015, the improper payment rate decreased from FY 2015 to FY 2016. In order to confirm the effectiveness of the implemented corrective actions, SBA OIG expects to see sustained progress in reducing the improper payment rate. Table 6 summarizes OIG's evaluation of agency efforts.

**Table 6. OIG's Evaluation of Agency Efforts**

OMB Criteria	Status at End of 2016
Overall assessment of agency efforts	Substantial Progress
Accuracy & completeness of agency reporting	Implemented
Performance in reducing/recapturing improper payments	N/A <sup>8</sup>
Quality of corrective action plans	Substantial Progress

### AFR Review

Our review of the AFR found that SBA was fully compliant with IPERA reporting requirements. Table 7 summarizes OIG's FY 2016 review of the AFR.

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<sup>8</sup> SBA has determined that the 504 Loan Program is not subject to recapture audits because no payment is made at the time of approval.

**Table 7. OIG's Review of the AFR**

<b>OMB Reporting Requirement</b>	<b>Status at End of 2016</b>
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Compliant
Reported rate of less than 10 percent	Compliant

## Section 4: Disaster Direct Loan Program

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### Background

The Disaster Direct Loan Program plays a vital role in the aftermath of disasters by providing long-term, low-interest loans to affected homeowners, renters, businesses, and nonprofit organizations. SBA offers home and business loans to compensate for physical damages and also offers loans to businesses to compensate for economic damages. This program is particularly vulnerable to fraud and unnecessary losses because loan transactions are expedited in order to provide quick relief to disaster survivors. In FY 2016, SBA approved \$1.4 billion in disaster assistance loans.

### OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate for disaster direct loan disbursements has continued to decrease. In FY 2015, the rate was 8.13 percent (\$24.6 million). For FY 2016, SBA reported an improper payment rate of 5.32 percent (\$18.4 million). The improper payment rate achieved was lower than the agency's 7.3 percent FY 2016 reduction target and below the 10 percent improper payment rate necessary to comply with IPERA requirements. We did note, however, that the improper payment rate and amount reported for FY 2016 was slightly overstated. We found that the improper payment rate and amount should have been reported as 5.22 percent (\$18 million) in FY 2016. The difference was due to a minor data input error that was not significant enough to warrant a restatement by the agency.

SBA's corrective action plan for the Disaster Direct Loan Program has been effective in reducing the improper payment rate. Specifically, SBA conducted training for the disbursement staff at the Processing and Disbursement Center (PDC) regarding acceptable documentation for the various types of insurance coverage. Additionally, SBA continues to perform independent reviews on all disbursements equal to or greater than \$100,000 to identify and prevent improper payments prior to loan disbursement. SBA also continues to conduct multilayered reviews of loan approvals and disbursements on a random basis, by teams within the two major departments of the PDC, to identify and reduce improper payments.

SBA also includes improper payment reduction as a rating factor in the annual performance evaluations of all loan processing staff, including loan officers, attorneys, and PDC management officials. Finally, the Office of Disaster Assistance's Management and Quality Control teams continue to hold biweekly meetings to discuss ongoing improper payment issues and develop strategies on how to resolve the issues and prevent future improper payments. For FY 2016, we have rated the Disaster Direct Loan program as "implemented." Table 8 summarizes OIG's evaluation of agency efforts.

**Table 8. OIG's Evaluation of Agency Efforts**

OMB Criteria	Status at End of 2016
Overall assessment of agency efforts	Implemented
Accuracy & completeness of agency reporting	Implemented
Performance in reducing/recapturing improper payments	N/A <sup>9</sup>
Quality of corrective action plans	Implemented

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<sup>9</sup> SBA has determined that payment recapture audits for this program would not be cost effective.

## AFR Review

Our review of the AFR found that SBA was fully compliant with the IPERA reporting requirements. Table 9 summarizes OIG's review of the AFR.

OIG periodically conducts reviews to assess the accuracy of the agency-reported improper payment rate. OIG currently is assessing the accuracy of the Disaster Direct Loan Program's FY 2015 improper payment rate and expects to report its results in FY 2017.

**Table 9. OIG's Review of the AFR**

OMB Reporting Requirement	Status at End of 2016
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Compliant
Reported rate of less than 10 percent	Compliant

## Section 5: Disbursements for Goods and Services

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### Background

SBA awards contracts for goods and services to assist in carrying out its mission. SBA made 2,838 disbursements for goods and services totaling approximately \$112 million between April 1, 2015, and March 31, 2016.

### OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate decreased from 13.52 percent (\$14.3 million) in FY 2015 to 10.35 percent (\$11.6 million) in FY 2016. In the FY 2016 AFR, SBA attributed the root cause of the improper payments to administrative and documentation errors, such as the following: accounts paid were not the accounts registered in the System for Award Management (SAM), invoices did not agree with the contract terms, and task orders did not match the contract terms. SBA developed and completed detailed corrective action plans addressing the root causes of identified improper payments. For example, the agency developed a checklist in February 2016 to strengthen both pre- and post-award verification processes and distributed it to all contracting officers, contracting officer representatives, and payment processors. Additionally, the agency implemented an automated interface between the financial system and SAM in January 2016. While SBA improved its controls over contract disbursements, it continues to identify administrative and documentation errors. As a result, we rated SBA as "implemented" for FY 2016. Table 10 summarizes OIG's evaluation of agency efforts.

**Table 10. OIG's Evaluation of Agency Efforts**

OMB Criteria	Status at End of 2016
Overall assessment of agency efforts	Implemented
Accuracy & completeness of agency reporting	Implemented
Performance in reducing/recapturing improper payments	N/A <sup>10</sup>
Quality of corrective action plans	Implemented

### AFR Review

Our review of the AFR found that SBA was compliant with most IPERA reporting requirements. However, for a second consecutive year, SBA's improper payment rate exceeded the 10 percent level necessary to comply with IPERA requirements. In accordance with OMB criteria, the OMB Director will review SBA's disbursements for goods and services to determine whether additional funding would help the agency come into compliance. Table 11 summarizes OIG's review of the AFR.

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<sup>10</sup> SBA has determined that payment recapture audits for this program would not be cost effective.

**Table 11. OIG’s Review of the AFR**

<b>OMB Reporting Requirement</b>	<b>Status at End of 2016</b>
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Compliant
Reported rate of less than 10 percent	Not Compliant

### **Analysis of Agency Response**

Although a response was not required, the Office of the Chief Financial Officer (OCFO) provided general comments pertaining to the section on disbursements for goods and services. The Associate Administrator for Performance Management and Chief Financial Officer emphasized the new controls OCFO has implemented that will assist in preventing improper payments for goods and services. The Associate Administrator stated that they have interfaced the System for Award Management (SAM) with SBA’s financial system, Joint Accounting and Administrative Management System (JAAMS). He noted that while the interface between the two systems was in place for over a year, the scope of our review would have only encompassed 3 months of the benefits realized by this interface. In addition, the Associate Administrator stated that OCFO

- implemented a pre- and post-review process of contracts before award,
- instituted a “HOLD” process that performs several checks on invoices that are ready for payment,
- created a supplier issue report to identify issues in supplier records, and
- tasked the Accounts Payable team to finalize OCFO internal audit procedures over payments and identify training needs.

We commend OCFO’s efforts for implementing the new controls to reduce improper payments for disbursements for goods and services. We encourage OCFO to continue improving its review processes to decrease the number of improper payments.

## Section 6: Hurricane Sandy Disaster Relief Administrative Expenses

### Background

The Disaster Relief Appropriations Act of 2013 (DRAA) provided SBA with a \$260 million appropriation to provide administrative expenses necessary to make and service disaster assistance direct loans. All programs and activities that received DRAA funding were considered susceptible to significant improper payments, regardless of any previous improper payment risk assessment results, and are required to report an improper payment estimate. The agency classified Hurricane Sandy disaster relief administrative expenses into three categories for measurement and reporting purposes: payroll, travel, and purchase cards. For FY 2016, the agency measured and reported improper payments for Hurricane Sandy disaster relief administrative expenses.

### OIG's Qualitative Assessment of Agency Efforts

SBA continued to operate a robust process to measure and report improper payments, producing improper payment rates well below the threshold needed to be compliant with IPERA requirements (see Table 12). The test plans for each area were detailed and complete, and they were fully executed in the sampling and testing processes.

**Table 12. Administrative Outlays and Improper Payment Rates**

Program	Outlays	Improper Payment Rate
Administrative Expenses – Payroll	\$27.1 million	0.24 percent
Administrative Expenses – Travel	\$0.3 million	0.06 percent
Administrative Expenses – Purchase Cards	\$0.2 million	0.61 percent

Additionally, testers in each area were experienced in the subject matter. As a result, for FY 2016 we have rated SBA as “implemented” for the three categories of Hurricane Sandy disaster relief administrative expenses. Table 13 summarizes OIG's evaluation of agency efforts.

**Table 13. OIG's Evaluation of Agency Efforts**

OMB Criteria	Status at End of 2016
Overall assessment of agency efforts	Implemented
Accuracy and completeness of agency reporting	Implemented
Performance in reducing/recapturing improper payments	N/A <sup>11</sup>
Quality of corrective action plans	N/A <sup>12</sup>

<sup>11</sup> SBA has determined that payment recapture audits for payroll and travel would not be cost effective. Purchase card outlays were less than the \$1 million threshold to require a recapture program.

<sup>12</sup> Improper payments did not exceed the 1.5 percent and \$10 million threshold for reporting a corrective action plan.

## AFR Review

Our review of the AFR found that SBA was fully compliant with IPERA reporting requirements. Table 14 summarizes OIG's review of the AFR.

**Table 14. OIG's Review of the AFR**

OMB Reporting Requirement	Status at End of 2016
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	N/A <sup>13</sup>
Met annual reduction target	Compliant
Reported rate of less than 10 percent	Compliant

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<sup>13</sup> Improper payments did not exceed the 1.5 percent and \$10 million threshold for reporting a corrective action plan.

## Section 7: Hurricane Sandy Disaster Relief Grants

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### Background

The Disaster Relief Appropriations Act of 2013 (DRAA) also provided SBA with a \$20 million appropriation to provide technical assistance to small businesses recovering from Hurricane Sandy.<sup>14</sup> Within SBA, the Office of Entrepreneurial Development (OED) managed these grants. OED oversees a nationwide network of programs and services that support the training and counseling needs of small businesses. OED's resource partners include small business development centers, women's business centers, and the SCORE Association.

### OIG's Qualitative Assessment of Agency Efforts

SBA reviewed 100 percent of the 38 Hurricane Sandy disaster relief payments for the total dollar amount of \$5.6 million. However, the documentation that SBA provided to OIG did not show that SBA reviewed three payments, which accounted for 28 percent of the dollar amount. We conducted a walk-through of each of these three payments and found no exceptions.

This year, for the first time, SBA began including all administrative and documentation errors in the improper payment rate calculation. SBA's improper payment rate decreased from 3.02 percent (\$130,000) in FY 2015 to 0.074 percent (\$4,000) in FY 2016. As a result, for FY 2016, we have rated SBA as "substantial progress" regarding payments related to Hurricane Sandy disaster relief grants.

However, because the documentation SBA provided OIG was incomplete, we rated SBA's accuracy and completeness of agency reporting as "needs improvement." Table 15 summarizes OIG's evaluation of agency efforts.

**Table 15. OIG's Evaluation of Agency Efforts**

OMB Criteria	Status at End of 2016
Overall assessment of agency efforts	Substantial Progress
Accuracy & completeness of agency reporting	Needs Improvement
Performance in reducing/recapturing improper payments	N/A <sup>15</sup>
Quality of corrective action plans	N/A <sup>16</sup>

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<sup>14</sup> Sequestration resulted in the agency receiving \$19 million.

<sup>15</sup> This step is not applicable. Hurricane Sandy technical assistance grants would not benefit from a recapture audit because the payments identified were due to administrative errors.

<sup>16</sup> SBA was not required to develop corrective action plans because the improper payments totaled less than \$10 million.

## AFR Review

Our review of the AFR found that SBA was fully compliant with IPERA reporting requirements. Table 16 summarizes OIG's review of the AFR.

**Table 16. OIG's Review of the AFR**

OMB Reporting Requirement	Status at End of 2016
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	N/A <sup>17</sup>
Met annual reduction target	Compliant
Reported rate of less than 10 percent	Compliant

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<sup>17</sup> SBA did not develop corrective action plans because the improper payments totaled less than \$10 million.

## **Appendix I: Objective, Scope, and Methodology**

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This report presents the results of our evaluation of SBA's FY 2016 progress in reducing improper payments. Our objectives were to (1) determine whether SBA complied with IPERA using guidelines outlined in OMB Memorandum M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments*, and (2) assess SBA's progress in remediating improper payment-related recommendations. To perform the evaluation, our scope included an assessment of improper payments that SBA reported for 7(a) loan guaranty purchases, 7(a) loan guaranty approvals, 504 CDC loan guaranty approvals, disaster direct loan disbursements, disbursements for goods and services, and Hurricane Sandy disaster relief grants and administrative funds.

To answer our objectives, we assessed the controls SBA implemented to address prior-year OIG recommendations and evaluated whether SBA addressed required provisions, and we reviewed SBA documentation and plans to assess compliance with identified controls and IPERA provisions. We also assessed the agency's efforts to prevent and reduce improper payments and reviewed the accuracy and completeness of improper payment disclosures in the AFR, as specified in OMB guidance. Moreover, we assessed progress the agency had made against the baseline we established in 2011. Our review did not assess whether specific program-reported rates were accurate.

We conducted this evaluation in accordance with the Council of Inspectors General on Integrity and Efficiency's *Quality Standards for Inspection and Evaluation*. These standards require that we plan and perform the evaluation to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our objectives. We believe that the evidence obtained provides a reasonable basis for our conclusions based on our objectives.

### **Use of Computer-Processed Data**

We relied on information provided by SBA officials that was extracted from SBA's Electronic Loan Information Processing System, Disaster Credit Management System, Oracle Federal Financial System, PRISM Contract Management System, Guaranty Purchase Tracking System, and E-Tran. Previous OIG and independent public accountant audits have verified that the information maintained in those systems is reliable. In addition, we conducted limited reliability tests on certain data contained in the universe. For example, we verified that the data was within the scope of our requests and did not include any data errors. We believe this information is reliable for the purposes of this evaluation.

## **Prior Coverage**

Between September 2016 and August 2011, OIG issued the following reports related to the agency's controls over improper payments:

*The OIG High Risk 7(a) Loan Review Program Recommends \$3.2 Million in Recoveries* (Report 16-22, September 30, 2016)

*SBA Loan Number 6439845000* (Report 16-19, August 16, 2016)

*SBA's FY 2015 Progress in Reducing Improper Payments* (Report 16-15, May 13, 2016)

*SBA Loan Number 4949845001* (Report 16-11, March 17, 2016)

*SBA's FY 2014 Compliance with the Improper Payments Elimination and Recovery Act* (Report 15-11, May 15, 2015)

*The OIG High Risk 7(a) Loan Review Program Recommends \$1.8 Million in Recoveries* (Report 15-09, March 20, 2015)

*SBA's Progress in Complying with the Improper Payments Elimination and Recovery Act* (Report 14-11, April 10, 2014)

*Purchase Reviews Allowed \$3.1 Million in Improper Payments on 7(a) Recovery Act Loans* (Report 14-09, January 29, 2014)

*Purchase Reviews Allowed \$4.6 Million in Improper Payments on 7(a) Recovery Act Loans* (Report 13-16R, June 14, 2013)

*Evaluation of SBA's Progress in Reducing Improper Payments in FY 2012* (Report 13-13, March 14, 2013)

*The Small Business Administration's Improper Payment Rate for 7(a) Guaranty Purchases Remains Significantly Understated* (Report 13-07, November 15, 2012)

*A Detailed Repayment Ability Analysis is Needed on High-Dollar Early-Defaulted Loans to Prevent Future Improper Payments* (Report 12-18, August 16, 2012)

*High-Dollar Early-Defaulted Loans Require an Increased Degree of Scrutiny and Improved Quality Control at the National Guaranty Purchase Center* (Report 12-11R, March 23, 2012)

*SBA Generally Meets IPERA Reporting Guidance but Immediate Attention Is Needed to Prevent and Reduce Improper Payments* (Report 12-10, March 15, 2012)

*Origination and Closing Deficiencies Identified In 7(a) Recovery Act Loan Approvals* (ROM 11-07, September 30, 2011)

*Material Deficiencies Identified in Five 7(a) Recovery Act Loans Resulted in \$2.7 Million of Questioned Costs* (ROM 11-06, August 25, 2011)

## Appendix II: Status of Open Prior Year Recommendations

OIG Report	Recommendation	Management Decision Date	Final Action Date
<b>16-22, The OIG High Risk 7(a) Loan Review Program Recommends \$3.2 Million in Recoveries (September 30, 2016)</b>	1. Evaluate the time NGPC loan specialists have to review complex early-defaulted loans involving change of ownership transactions.	Overdue to OIG	Overdue to OIG
<b>16-19, SBA Loan Number 6439845000 (August 16, 2016)</b>	1. Bring the loan into compliance or seek recovery of the guaranty paid by SBA of \$850,791 from (see report for the bank name).	8/23/2016	7/25/2017
<b>16-11, SBA Loan Number 4949845001 (March 17, 2016)</b>	1. Bring the loan into compliance or seek recovery of the guaranty paid by SBA of \$2,046,465 from (see report for the bank).	3/10/2016	3/14/2017 Overdue to OIG
<b>15-09, The OIG High Risk 7(a) Loan Review Program Recommends \$1.8 Million in Recoveries (March 20, 2015)</b>	3. Require credit union to bring loan into compliance or seek recovery of \$471,905, less liquidation amounts, on the guaranty paid by SBA for the loan to the borrower (see report for the credit union and borrower).	3/23/2015	4/2/2016 Overdue to OIG

## SBA's Response to Evaluation Report



U.S. SMALL BUSINESS ADMINISTRATION  
WASHINGTON, D.C. 20416

To: Hannibal "Mike" Ware  
Acting Inspector General

From: Timothy Gribben  
Associate Administrator for Performance Management and Chief Financial Officer

William Manger  
Associate Administrator for Capital Access

James Rivera  
Associate Administrator for Disaster Assistance

Lori Gillen  
Deputy Associate Administrator for Entrepreneurial Development

Date: April 28, 2017

Subject: Comments on OIG Draft Audit Report "SBA's FY 2016 Compliance with the Improper Payment Elimination and Recovery Act"

The Small Business Administration (SBA) appreciates the opportunity to review and respond to the draft report "SBA's FY 2016 Compliance with the Improper Payment Elimination and Recovery Act".

Improved financial performance through the reduction of improper payments continues to be a key financial management focus of the Federal government. SBA management continually develops strategies to reduce improper payments for responsible stewardship of public assets.

SBA offers the following comments in response to your audit recommendations:

**Recommendation #1:** We recommend that the Office of Financial Program Operations submit to the Senate Committee on Homeland Security and Governmental Affairs, the House Committee on Oversight and Governmental Reform, and OMB, within 90 days of this report, a plan for the 7(a) guaranty purchase program that includes the following: a) measurable milestones for becoming compliant with IPERA; b) designation of an accountable senior agency official; (c) the establishment of an accountability mechanism, describing the actions the agency will take to become compliant.

**Agency Response:** SBA concurs that the 7(a) guaranty purchase loan program failed to meet its annual reduction target within .1 percentage point for one year and is subject to the requirements outlined in the recommendation and will comply within 90 days of the date the report is published as required.

The Office of Financial Program Operations (OFPO) would like to emphasize that the 7(a) guaranty purchase program has maintained a relatively low improper payment rate for the past several years,

reporting estimated improper payment rates of 1.75%, 0.9%, and 2.32% in FY 2014, FY 2015, and FY 2016, respectively. While we acknowledge the increase from the previous fiscal year, it is our assertion that this was the result of an enhanced test plan, including the implementation of a robust loan review checklist, requiring a detailed analysis of creditworthiness (including repayment ability) on early defaulted 7(a) loans. Nevertheless, OFPO is committed to reducing improper payments and meeting future reduction targets.

**Recommendation #2:** We recommend that the Director of the Office of Financial Program Operations provide OMB and OIG a complete analysis to justify and support the agency's position that 7(a) guaranty purchase recapture audits are not cost effective.

**Agency Response:** SBA concurs with the recommendation and will provide OMB and OIG its analysis to support the agency's position that 7(a) guaranty purchase recapture audits are not cost effective within 90 days of the date the report is published.

OFPO would like to emphasize that the process and results of a payment recapture audit were not disclosed in the FY 2016 Agency Financial Report for the 7(a) guaranty purchase program as a formal recapture audit was not conducted. The determination to discontinue this effort was made at the conclusion of the FY 2015 recapture audit as it did not prove to be cost effective; however, recognizing the benefits a recapture audit can serve, OFPO decided to maintain the spirit of the audit and incorporated various components into its Quality Control Program. Based on our interpretation of the AFR requirements, it was our understanding that the disclosures made within the FY 2015 AFR served as sufficient notification to discontinue conducting and reporting formal payment recapture audits for the 7(a) guaranty purchase program.

**Additional Agency Comments:**

The Office of the Chief Financial Officer (OCFO) would like to emphasize that the payment data examined for improper payments relating to the disbursements for goods and services was from 4/1/2015 to 3/31/2016. During this range, the SBA implemented several new controls that will assist in preventing improper payments.

The System for Award Management (SAM) is now directly interfaced to SBA's financial system, JAAMS. SAM interfaces with JAAMS and provides accurate, up-to-date information on vendors. SAM provides the Data Universal Numbering System (DUNS) number, tax identification number, banking information, and address for vendors. The benefits of this connection between SAM and JAAMS would have only been realized for three months of the review period.

The vast majority of SBA's improper payments resulted from documentation errors. The OCFO has implemented process improvements identified in the following paragraphs to ensure these types of errors are minimized for future payments.

Implementation of a pre and post review process of contracts before award.

Implementation of a "HOLD" process which performs several checks on invoices ready to be paid. Invoices that meet any of the hold criteria are placed on a scheduled payment hold. The hold remains in place until it is released by an approver on the Accounts Payable team. When a supplier record is expired in SAM, invoices associated with that supplier are placed on hold. The supplier is contacted with a request to update SAM.

A Supplier Issue report was created to identify issues in supplier records. The objective is to identify incomplete/inaccurate supplier records for clean-up thus preventing payment issues.

Additionally, the Accounts Payable team is in the process of finalizing internal audit procedures over their payments and identifying training needs within the section.