

REPORT ON THE MOST SERIOUS  
MANAGEMENT AND PERFORMANCE  
CHALLENGES FACING THE SMALL BUSINESS  
ADMINISTRATION IN FISCAL YEAR 2018






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

---

**Memorandum**  
Management Challenges

**DATE:** October 12, 2017

**TO:** Linda E. McMahon  
Administrator

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

**SUBJECT:** Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration in Fiscal Year 2018

In accordance with the Reports Consolidation Act of 2000, we are providing you with the Office of Inspector General's (OIG's) *Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration in Fiscal Year 2018*. The overall goal is to focus attention on significant issues with the objective of working with Agency managers to enhance the effectiveness of the Small Business Administration's (SBA's) programs and operations. We have prepared similar reports since fiscal year (FY) 2000.

Within each management challenge is a series of recommended actions to enhance the effectiveness of Agency programs and operations. Each recommended action is assigned a color score to indicate its status. The scores are as follows: green for "implemented," yellow for "substantial progress," orange for "limited progress," and red for "no progress." If a recommended action was added since last year's report, no color score was assigned, and the recommended action has been designated as "new." Actions that were scored green last year, and remained green this year, have been moved up to the "history bar" above the recommended actions. The history bar highlights any progress that the Agency has made on a challenge over the past 4 fiscal years (or as long as the challenge has existed, if shorter) by showing the number of actions that have moved to green each year. In addition, an arrow in the color box indicates that the color score went up or down from the prior year.

The following table provides a summary of the most serious management and performance challenges facing SBA in FY 2018.

**Summary of the Most Serious Management and Performance Challenges  
Facing SBA in FY 2018**

		Color Scores					
		Status at End of FY 2017				Change from Prior Year	
	Challenge	Green	Yellow	Orange	Red	Up ↑	Down ↓
1	Small Business Contracting		2	1		1	
2	IT Leadership		5	1		5	
3	Human Capital	1	1			1	
4	SBA Loan Program Risk Management and Oversight	1	3 <sup>1</sup>	1		1	
5	8(a) Business Development Program	2		1		3	
6	Ensuring Quality Deliverables and Reducing Improper Payments at SBA Loan Operation Centers	1	2			1	
7	Disaster Assistance Program		4			1	
8	Acquisition Management	4				4	
	TOTAL	9	17	4		17	0

The management challenge process is an important tool that we hope will assist the Agency in prioritizing its efforts to improve program performance and enhance its operations. We look forward to continuing to work with SBA's leadership team in addressing the Agency's most serious management and performance challenges.

---

<sup>1</sup> For Management Challenge number 4 recommendation 3, 7(a) was rated yellow, while 504 was rated orange. For simplicity, it is reflected as yellow in this table.

## Table of Contents

---

Challenge 1: Weaknesses in Small Business Contracting Programs and Inaccurate Procurement Data Undermine the Reliability of Contracting Goal Achievements.....	1
Agencies Receive Goaling Credit for Firms No Longer in the 8(a) or HUBZone Programs.....	1
Exclusions From the <i>Small Business Goaling Report</i> Impact the Overall Prime Contract Goal.....	2
Women-Owned Small Business Federal Contracting Program Susceptible to Abuse .....	2
SBA Needs the Full Range of Federal Program Enforcement Tools to Address Fraud.....	3
Challenge 2: SBA's Information Technology Leadership Capabilities Need Strengthening to Address Operational Risks and Challenges .....	4
OCIO Made Significant Progress in Deploying Key Components of FITARA.....	4
Long-Standing Weaknesses in IT Security Controls Are Being Addressed, but Accelerated Progress Is Needed to Meet Growing Cybersecurity Threats .....	4
Challenge 3: SBA Needs Effective Human Capital Strategies to Carry Out Its Mission Successfully and Become a High-Performing Organization.....	6
SBA Made Progress to Update Human Capital SOPs and Guidance.....	6
Challenge 4: SBA Needs to Improve Its Risk Management and Oversight Practices to Ensure Its Loan Programs Operate Effectively and Will Continue to Benefit Small Businesses .....	8
SBA Improved Oversight of Lending Participants .....	8
SBA Improved Portfolio Risk Management Program .....	9
Increased Risk Introduced by Loan Agents .....	9
Challenge 5: SBA Needs to Ensure That the Section 8(a) Business Development Program Identifies and Addresses the Needs of Program Participants, Only Eligible Firms Are Admitted Into the Program, and Standards for Determining Economic Disadvantage Are Justifiable.....	12
SBA Continues to Address Its Ability to Deliver an Effective 8(a) Program .....	12
Streamlined Application Process May Expose the 8(a) Program to a Higher Risk of Fraud.....	12
SBA Dollar Threshold for Economic Disadvantage Not Justified.....	13
Challenge 6: SBA Can Improve Its Loan Programs by Ensuring Quality Deliverables and Reducing Improper Payments at SBA Loan Operation Centers .....	14
SBA Improved Its Quality Control Program to Ensure Timely Implementation of Corrective Actions.....	14
Inadequate Staffing, Training, and Supervision Have Resulted in Material Underwriting Deficiencies .....	15
Improvements Are Needed in the Identification of Improper Payments.....	15
Challenge 7: Disaster Assistance Must Balance Competing Priorities to Deliver Timely Assistance and Reduce Improper Payments.....	17
Private Lender Programs Intended to Quickly Disburse Disaster Funds Not Implemented .....	17
Express Recovery Opportunity Loan Program Not Implemented .....	18

Maximum Allowable Fixed Debt May Be Exceeded, Limiting Borrower’s Ability to Repay Disaster Loans.....	18
Reserve Staff Require Training to Sustain Productivity During Mobilization.....	19
Improper Payment Rate Remains Above IPERA Significance Threshold.....	19
Challenge 8: SBA Needs to Effectively Manage Its Acquisition Program .....	21

## **Challenge 1: Weaknesses in Small Business Contracting Programs and Inaccurate Procurement Data Undermine the Reliability of Contracting Goal Achievements**

---

The Small Business Act established a Governmentwide goal that 23 percent of all prime contracts be awarded to small businesses each fiscal year. In its annual *Small Business Goaling Report*, the Small Business Administration (SBA) has reported since fiscal year (FY) 2013 that the Federal Government met or exceeded its goal of awarding 23 percent of Federal contracting dollars to small businesses. However, over the years, Congress has expressed concerns about the accuracy of the report. These concerns have been substantiated by SBA Office of Inspector General (OIG) audits and other Government studies that have shown widespread misreporting by procuring agencies, since many contract awards that were reported as having gone to small firms have actually been substantially performed by larger companies. Specifically, in certain circumstances SBA's regulations allow firms that are not small to be counted as small businesses. As a result, agencies continue to receive Small Disadvantaged Business and Historically Underutilized Business Zone (HUBZone) goaling credit for contracts awarded to firms no longer in SBA's preference programs. In addition, SBA has opted to exclude certain procurements such as those awarded by the Department of Defense (DoD) for overseas work from the small business goaling baseline, an exclusion that leads to overstatement of small business goaling achievements. Furthermore, SBA has not implemented a certification process for the Women-Owned Small Business Federal Contracting Program (WOSBP), which can affect the accuracy of the goaling achievements. Finally, SBA restricted how it can use the Program Fraud Civil Remedies Act of 1986 (PFCRA) for small business contracting cases, which can result in large businesses obtaining small business contracts, which falsely increases goaling numbers.

As the advocate for small business, SBA should strive to ensure that only eligible small firms obtain and perform small business awards to ensure goaling statistics portray Federal contract awards made only to small businesses. Further, SBA should ensure that procuring agencies accurately report contracts awarded to small businesses when representing their progress in meeting small business contracting goals. Counting firms in categories in which they are no longer eligible misrepresents actual small business contracting goals achievements. While some contractors may misrepresent or erroneously calculate their size, the incorrect reporting also results from errors made by Government contracting personnel, including the misapplication of small business contracting rules. Moreover, without reliable data, SBA cannot accurately measure the Federal Government's small business procurement goals achievements, which in turn weakens the ability of Congress and other Federal policymakers to determine whether the Government is maximizing contracting opportunities for small businesses.

### **Agencies Receive Goaling Credit for Firms No Longer in the 8(a) or HUBZone Programs**

In [Report 14-18](#), we identified over \$400 million in FY 2013 contract actions that may have been awarded to ineligible firms. We also found that over \$1.5 billion dollars in FY 2013 contract actions were included towards small business contacting goals, even though the firms were no longer in the 8(a) Business Development or HUBZone programs. Furthermore, we determined that of approximately \$3.1 billion in contracts awarded to the top 100 firms in the 8(a) program in FY 2016, approximately \$1.5 billion was awarded to firms no longer in the program. SBA revised its regulations in 2004 to permit procuring agencies to claim small disadvantaged business and HUBZone goaling credit on certain contract actions, even after firms have left the program. SBA added these regulations in order to codify the existing "practice" of the agencies to include these firms even though they were no longer in a program. According to SBA officials, if they remove this provision, Federal agencies would be reluctant to use SBA programs, or would be required to award

new contracts in order to obtain small disadvantaged business credit. They also believe that by awarding new contracts, agencies would incur additional administrative costs, and doing so would be inefficient and would not benefit the Government or businesses. However, more proactive acquisition planning by the agencies would help offset inefficiencies in the procurement cycle.

Citing administrative inconvenience as the rationale to include firms no longer in a program undermines one of the main missions of SBA which is to help Americans start, build, and grow businesses. Counting firms no longer in the 8(a) and HUBZone programs weakens the very intent of these programs and does not maximize opportunities for all small businesses. Additionally, by counting firms no longer in the 8(a) and HUBZone programs, SBA cannot accurately reflect or measure true program impact. Federal agencies contracting officers also have little incentive to award 8(a) or HUBZone set-aside contracts to new firms if they can attain goals by counting previously awarded contracts to firms no longer in a program.

### **Exclusions From the *Small Business Goaling Report* Impact the Overall Prime Contract Goal**

SBA's goaling guidelines exclude certain types of contracts from the overall dollar baseline used to calculate achievement of small business goals. For example, the goaling guidelines exclude contracts that were both awarded and performed abroad and those performed entirely abroad. In addition, the National Defense Authorization Act for FY 2017 authorized SBA to remove certain DoD contracts from the procurement baseline when reporting Governmentwide small business contracting goals and achievements. As a result, SBA excludes these contracts notwithstanding the fact that in FYs 2008 and 2015, SBA's own Office of General Counsel stated that "the Small Business Act, including its goaling provisions, applies to acquisitions conducted by Federal agencies overseas and the Act applies to Federal procurements contracts performed overseas." Although the DoD can remove certain contracts from the baseline for DoD-specific reporting requirements, the congressional mandate does not exclude these categories of prime contracts from the Governmentwide goal of 23 percent.

These exclusions, which are not mandated by statute, weaken the ability of Congress and other Federal policymakers to determine whether the Government is maximizing contracting opportunities for small businesses and meeting small business goals. In our opinion, by excluding certain types of contracts from the goaling baseline, SBA overstates the Federal Government small business goal achievements. Including the appropriate universe of Federal procurement opportunities into the goaling guidelines baseline will ensure policymakers and other interested parties receive the most accurate picture of small business participation in Federal contracting.

### **Women-Owned Small Business Federal Contracting Program Susceptible to Abuse**

SBA's WOSBP provides greater access to Federal contracting opportunities to women-owned small businesses (WOSBs) and economically-disadvantaged WOSBs that meet the WOSBP requirements. OIG and Government Accountability Office (GAO) have both reported weaknesses in SBA's controls that would ensure only eligible firms receive WOSBP set-aside contracts.

The National Defense Authorization Act for 2015 granted contracting officers the authority to award sole-source awards to firms in WOSBP and required firms to be certified by a Federal agency, a State government, the Administrator, or a national certifying entity approved by the Administrator. However, SBA implemented the sole-source authority provision first without a certification program. We believe allowing sole-source contracting authority in WOSBP, without implementing the contemporaneously required certification program, was inconsistent with SBA's statutory authorization. In the meantime, this continues to be a risk that exposes the program to abuse by having firms incorrectly self-certify as a woman-owned small business, which overstates

goalings for women-owned firms. SBA began addressing this shortcoming in FY 2017 by drafting a proposed rule for implementing a certification process for the WOSBP. Currently, SBA’s Office of General Counsel is reviewing the proposed rule after which it will be provided to the Administrator for review.

### **SBA Needs the Full Range of Federal Program Enforcement Tools to Address Fraud**

Having a robust enforcement program is crucial to deterring fraud in small business programs, and by extension, ensuring reliability of reported goaling numbers. Agencies need to have, and use, the full range of available remedies to protect federal procurement effectively. The Program Fraud Civil Remedies Act of 1986 (PFCRA), for example, was enacted to address smaller dollar value frauds. SBA has, however, restricted how it can use the PFCRA for small business contracting cases. The Agency should modify its PFCRA regulations so that SBA can pursue any small business contracting program violations, subject to the PFCRA’s jurisdictional limits, under that statute. SBA has started preliminary discussions about implementing this change, but it has not yet proposed a rule. Independent of the PFCRA changes recommended above, SBA has increased its PFCRA penalty level, along with several other civil penalties, as mandated by the Federal Civil Penalties Inflation Adjustment Improvements Act of 2015.

Number of Actions Accomplished (Green Status) During Last 4 Fiscal Years (Challenge first reported in FY 2005)	2013: 0	2014: 1	2015: 0	2016: 1
Recommended Actions for FY 2018				Status at end of FY 2017
1. Strengthen controls to ensure the accuracy of the Federal Government’s annual small business procurement goals achievements reported in the <i>Small Business Goaling Report</i> .				<b>Yellow</b>
2. Implement a certification process for WOSBP.				<b>Yellow↑</b>
3. Revise SBA’s Program Fraud Civil Remedies Act regulations so that SBA can pursue violations of its Federal contracting programs and demonstrate a capacity for taking enforcement actions under that statute.				<b>Orange</b>

**Green**-Implemented    **Yellow**-Substantial Progress    **Orange**-Limited Progress    **Red**-No Progress



## **Challenge 2: SBA's Information Technology Leadership Capabilities Need Strengthening to Address Operational Risks and Challenges**

---

During the past year, the Office of the Chief Information Officer (OCIO) made significant progress in improving its oversight of information technology (IT) investments and deploying other key components of the Federal Information Technology Acquisition Reform Act (FITARA). Policies and related governance protocols have been revised to ensure OCIO plays a major role in the entire IT investment cycle, from strategic planning to implementation. Critical OCIO human resources have been augmented with the hiring of a Deputy CIO and nine other key IT personnel. Consequently, OCIO is more effectively applying governance principles to better assess, communicate, and mitigate risk throughout the enterprise.

However, like most Federal agencies, SBA continues to experience a growing risk of outside cybersecurity threats. In FY 2016, one SBA program office experienced a ransomware incident that adversely affected its operations; the OCIO prepared an After Action Review outlining causes, lessons learned, and future changes concerning this incident on May 26, 2017. These IT security threats increase the importance of improving risk management procedures, continuously monitoring internal networks, deploying effective incident response strategies, and implementing effective contingency plans.

### **OCIO Made Significant Progress in Deploying Key Components of FITARA**

FITARA was enacted in December 2014. The goal of this legislation was to realize long-term cost savings through improved IT risk management, transparency, and more effective IT investment oversight. During this past year, OCIO incorporated many of the FITARA requirements into its organizational structure. Some examples include re-initiation of the Investment and Architecture Review Boards, issuance of an Agency-wide standard operating procedure (SOP) that outlines the CIO role in IT acquisitions and periodic meetings of its IT investment oversight governance board, the Business Technology Investment Council. In addition, the digital service system development group was realigned to report directly to OCIO, providing improved oversight of this group's development efforts.

In order to realize the long-term cost savings and operational benefits of FITARA, OCIO needs to improve implementation of key baseline criteria outlined in the legislation. For example, human resource planning, investment oversight, and enterprise architecture need to be implemented on an enterprise-wide basis. In addition, OCIO's investment transparency needs to be improved through improved project planning, i.e., periodic updates of project activity against pre-established baselines, and consistent and timely reporting of project results.

### **Long-Standing Weaknesses in IT Security Controls Are Being Addressed, but Accelerated Progress Is Needed to Meet Growing Cybersecurity Threats**

Our evaluations of SBA's systems and networks indicate significant improvement in information security and continuous monitoring practices, contractor systems, configuration management, and identity and access management. This improvement reflects an IT control enhancement program initiated by the Agency. During this fiscal year, the Agency closed at least 34, or approximately 6 percent, of its outstanding IT recommendations. Notwithstanding these efforts, significant vulnerabilities remain. The results of our annual evaluations of SBA's systems and networks indicate there are approximately 23 open recommendations, some dating back to FY 2011. Also, many are indicative of enterprisewide vulnerabilities or risks requiring infrastructure investment

or more effective monitoring of contractor hosted systems. These general control areas include the following:

- Information security and continuous monitoring that require validation of compliance with security requirements through auditing, periodic reviews, and implementing continuous monitoring strategies.
- Risk management, contingency planning, and incident response that monitors the selection, implementation, and assessment of security controls, and authorization to operate both internal and hosted systems.
- Configuration management and identity and access management controls that document and manage baselines establish a comprehensive personally identifiable information data loss prevention program, and require full implementation of system access procedures.

OCIO has made significant progress by initiating continuous diagnostic and mitigation capabilities in the cloud and will complete Phase 1 deployment in FY 2017. However, to show significant improvement in these areas, OCIO should resolve existing vulnerabilities and continue to implement risk management and system improvement initiatives such as continuous diagnostic and mitigation deployment, the Advanced Threat Protection pilot, data loss prevention for email traffic, data rights management for email and attachments, and its cloud migration strategy.

Number of Actions Accomplished (Green Status) During Last 4 Fiscal Years (Challenge first reported in FY 1999, revised in FY 2016)	2013-1	2014-0	2015-0	2016-0
Recommended Actions for 2018				Status at End of 2017
1. Establish an OCIO human resource planning process that allows full deployment of FITARA.				<b>Yellow↑</b>
2. The OCIO performs independent oversight of IT investments consistent with guidance.				<b>Yellow↑</b>
3. The OCIO facilitates enterprise architecture and demonstrates accountability for IT investments.				<b>Yellow↑</b>
4. The OCIO establishes and implements information security and continuous monitoring practices, and contractor systems policies and standards to ensure ongoing effectiveness of information systems.				<b>Yellow↑</b>
5. The OCIO maintains effective risk management, contingency planning, and incident response practices to minimize vulnerabilities.				<b>Orange</b>
6. The OCIO establishes configuration management and identity and access management controls and procedures.				<b>Yellow↑</b>

**Green**-Implemented    **Yellow**-Substantial Progress    **Orange**-Limited Progress    **Red**-No Progress

### **Challenge 3: SBA Needs Effective Human Capital Strategies to Carry Out Its Mission Successfully and Become a High-Performing Organization**

---

Over a decade ago, we identified human capital management as a top challenge for SBA. Since that time, SBA has made substantial progress to address this long-standing challenge. Specifically, during FY 2016 SBA completed a skills assessment, last performed in 2006, that focused on core and leadership competencies. As a result, the Office of Human Resources Solution (OHRS) issued a new Strategic Workforce Plan for 2017–2020 with strategies and metrics to address challenges, recruit and retain the right workforce, and track progress. In conjunction, OHRS issued a 2017–2018 Talent Development Plan designed to address the unique developmental needs of SBA’s program offices workforce and address skills gaps in SBA’s mission critical positions. As part of its talent development plans, SBA participates in Governmentwide rotational programs to develop future leaders and actively recruits candidates through the Presidential Management Fellows Program. Additionally, OHRS continues to follow the 2013–2016 Leadership Succession Plan to transfer knowledge for key positions. These plans are essential for obtaining and maintaining a workforce with the skills necessary to achieve SBA’s mission.

Although substantial progress has been made, SBA has not fully implemented our recommendation to update human resources guidance. OIG believes it is necessary to update and establish critical procedures in support of its long-term goals and objectives and Governmentwide human capital management initiatives to become a high-performing organization. In FY 2015, GAO reported that the reason SBA has not mitigated this and other management challenges is, in part, due to the lack of sustained priority attention over time and frequent turnover of leadership.

#### **SBA Made Progress to Update Human Capital SOPs and Guidance**

In FY 2017, OHRS continued to make significant progress in updating and establishing SOPs for human capital management as recommended by OIG in this long-standing management challenge. OHRS published its Discipline and Adverse Actions, Senior Executive Service Management, and Senior Leaders SOPs. Additionally, OHRS submitted three SOPs to SBA’s clearance process and are finalizing a draft to update the last remaining human resource SOP it had identified as critical.

In addition to updating and establishing SOPs, OHRS took steps to update its internal policies with more comprehensive guidance for Executive Resources personnel. Specifically, OHRS disseminated updated guidance to all OHRS personnel and developed a desk guide as an action to remedy the improper pay setting practices identified in a series of three OIG management advisories (Reports [16-20](#), [17-08](#), and [17-16](#)). These guides, if utilized correctly, provide OHRS staff with integral knowledge needed to achieve its mission.

Number of Actions Accomplished (Green Status) During Last Four Fiscal Years (Challenge first reported in FY 2001, revised FY 2007)	2013: 1	2014: 0	2015: 1	2016: 0
Recommended Actions for FY 2018				Status at end of FY 2017
1. Ensure the Agency has an effective, comprehensive workforce and succession plan that aligns talent needs and capabilities with SBA's FY 2011-2016 strategic plan. SBA's workforce and succession planning goals should reflect the need to recruit and retain the appropriate talent, and should establish appropriate metrics to gauge SBA's success at having the right people, in the right jobs, at the right time.				Green ↑
2. Ensure that human capital management SOPs are updated and appropriately structured to support the Agency's long-term goals and objectives and Governmentwide human capital management initiatives.				Yellow
<b>Green</b> -Implemented <b>Yellow</b> -Substantial Progress <b>Orange</b> -Limited Progress <b>Red</b> -No Progress				

## **Challenge 4: SBA Needs to Improve Its Risk Management and Oversight Practices to Ensure Its Loan Programs Operate Effectively and Will Continue to Benefit Small Businesses**

---

SBA's Office of Credit Risk Management (OCRM) manages credit risk for a nearly \$142 billion loan portfolio originated by over 2,500 active lenders and Certified Development Companies (CDCs) that have various degrees of expertise regarding SBA loan program requirements. The majority of SBA loans are originated by lenders with delegated approval authority, resulting in limited SBA oversight and quality control reviews until a default occurs. Many lenders rely on the services of "for-fee" and other third-party agents to assist in the origination, closing, servicing, and liquidation of SBA loans.

Previous OIG audits identified that SBA did not recognize significant lender weaknesses, develop an effective portfolio risk management program, or effectively identify and track third-party agent involvement in its 7(a) and 504 loan portfolios. Since the audits, SBA has significantly improved its oversight of lenders and made progress in implementing a portfolio risk management program. However, SBA made limited progress in identifying and tracking third-party agents.

While SBA improved its oversight of lenders and the risk management program, SBA still faces challenges demonstrating that identified lender weaknesses are addressed by monitoring and verifying lenders' corrective actions. Also, SBA needs to show that the portfolio risk management program is used to support risk-based decisions and implement additional controls to mitigate risks. Moreover, SBA needs to develop an effective method for tracking loan agents, update regulations on loan agents, and implement a loan agent registration system.

### **SBA Improved Oversight of Lending Participants**

The risks inherent in delegated lending require an effective oversight program to monitor compliance with SBA policies and procedures and take corrective actions when a material noncompliance is detected. However, in a September 2012 audit report ([Report 12-20R](#)), OIG found that SBA did not always recognize the significance of lender weaknesses or determine the risks lender weaknesses posed to the Agency during its onsite reviews. The report also found that SBA did not link the risks associated with the weaknesses to the lenders' corresponding risk ratings and assessments of operations. Further, SBA did not require lenders to correct performance problems that could have exposed SBA to unacceptable levels of financial risk.

Since the time of the audit, SBA improved its oversight of lending participants. In FY 2013, SBA developed risk profiles and lender performance thresholds, developed a select analytical review process to allow for virtual risk-based reviews, updated its lender risk rating model to better stratify and predict risk, and conducted test reviews under the new risk-based review protocol. During FYs 2014 and 2015, OCRM revised its review methodologies for 7(a) and 504 program lenders and engaged contractor support to expand on its corrective action follow-up process. During FY 2016, OCRM stated that it successfully reviewed 281 corrective action follow-up assessments and issued its FY 2017 Risk Management Plan. In FY 2017, SBA monitored and verified implementation of corrective actions to ensure effective resolution prior to closeout. As a result, SBA implemented recommendation 1 and needs to continue to demonstrate in FY 2018 that it monitors and verifies implementation of corrective actions.

## **SBA Improved Portfolio Risk Management Program**

A July 2013 OIG report ([Report 13-17](#)) found that SBA traditionally focused on loan approval volume and loss rates to evaluate overall program performance with risk being assessed at the lender level. As a result, SBA had not developed an effective portfolio risk management program that monitored portfolio segments to identify risk based on default statistics. Our limited analysis showed that SBA continued to guarantee loans to high-risk franchises and industries without monitoring risks, and where necessary, implementing controls to mitigate those risks. OIG reports have also found that SBA did not establish measures to evaluate the performance of pilot loan programs or evaluate performance when performance measures were established. For example, SBA's Community Express loan program was maintained as a pilot program for over 10 years without SBA performing an evaluation of the program. The pilot had been dominated by two lenders employing questionable credit practices and charging higher interest rates that ultimately led to SBA ending the program.

Since that time, SBA has made substantial progress in demonstrating that information from the portfolio risk management program is used to support risk-based decisions and implementing additional controls to mitigate risks in SBA loan programs. In 2016 SBA established performance measures and risk mitigation goals applicable to each loan program and the entire lending portfolio. OCRM also conducted portfolio analyses of problem lenders with heavy concentrations in SBA 7(a) lending and sales on the secondary market. In response, OCRM proposed actions to mitigate SBA exposure on the secondary market. In FY 2017, SBA began an ongoing study of lender compliance with SBA Form 1502 reporting. SBA identified deficiencies with certain types of reporting and subsequently issued Information Notice 5000-1945, reminding lenders of the reporting requirements.

SBA maintains that the current program tracks performance to support risk-based decisions at the portfolio, sub-program, and lender level, and that identified risk issues are presented to SBA executive leadership at Lender Oversight Committee meetings. SBA will need to continue to demonstrate during FY 2018 that information from this program is used to support risk-based decisions and implement additional controls to mitigate risks.

## **Increased Risk Introduced by Loan Agents**

Prior OIG audits and investigations identified that SBA did not have a way to effectively identify and track loan agent involvement in its 7(a) and 504 loan portfolios and had outdated enforcement regulations. Additionally, OIG investigations have revealed a pattern of fraud by loan packagers and other for-fee agents in the 7(a) Loan Program, involving hundreds of millions of dollars. Since 2005, OIG has investigated at least 22 cases with confirmed loan agent fraud, totaling at least \$335 million. Further, OIG has determined that loan agents were involved in approximately 15 percent of all 7(a) loans and resulted in increased risk of default. Despite the prevalence of fraud in its loan portfolios, SBA's oversight of loan agents has been limited.

In response to this challenge, SBA has made limited progress. To track loan agent activity on 7(a) program loans, SBA decided to have lenders fax a loan agent disclosure form (Form 159) to SBA's fiscal and transfer agent (FTA) and require the FTA to enter the data into a database accessible to SBA. SBA also began linking 7(a) loan Form 159 information with its loan data. However, a September 2015 OIG report on SBA's loan agent oversight ([Report 15-16](#)) identified significant issues in the data quality on the Form 159. While SBA has implemented an automated Form 159 within the SBA One system, an automated lending platform that assists lenders with everything from determining loan eligibility through closing their loan, SBA will likely need to make further

modifications to this process. In 2016, SBA issued a notice to lenders reiterating its requirements for loan agent disclosures and submission of the Form 159 to its FTA.

Additionally, in response to OIG concerns that SBA loan agent enforcement regulations are outdated, SBA prepared the Final Rule for Agent Revocation and Suspension Procedures, which was submitted to and approved by the SBA Administrator. However, due to the Presidential Executive Order on Reducing Regulation and Controlling Regulatory Costs, SBA has not submitted the final regulation to the Office of Management and Budget (OMB).

OIG maintains that SBA also needs to develop a system to assign a unique identifier to loan agents that participate in the 7(a) Loan Program. The lack of a unique identifier limits SBA's ability to perform effective oversight. In response to our loan agent's report, SBA stated that it will explore the feasibility of implementing a registration system. To date, no solutions have been implemented.

In addition, a March 2015 audit ([Report 15-06](#)) noted that the outsourcing of traditional lender functions to Lender Service Providers (LSPs), a type of loan agent, has significantly increased in recent years. Specifically, in 2014, over 770 lenders—or approximately 28 percent of the active 7(a) lenders—had an approved agreement with at least one LSP. Additionally, SBA loan portfolios associated with the three largest LSPs exceeded that of many of the top 100 active SBA 7(a) program lenders.

Since our 2015 report, the number of SBA-approved LSP agreements has reached over 2,200, due in part to SBA's effort to better control access by LSPs to its systems. Specifically, SBA assigns an identifying number for all LSPs that access SBA systems and records all SBA-approved LSP agreements. This trend has enabled OCRM to develop initial performance metrics on LSP performance, but oversight is still limited. This audit also noted that a number of referrals regarding improper loan agent activities had not been acted upon by OCRM. In response, OCRM developed and now maintains a tracking system on referrals.

As loan agent involvement in the 7(a) program continues to increase, it will become especially important for SBA to have oversight tools in place to identify and track loan agent involvement in this sizeable program.

Number of Actions Accomplished (Green Status) During Past Four Fiscal Years (Challenge first reported in FY 2001)	2013 7(a) loans: 2 504 loans: 2	2014 7(a) loans: 0 504 loans: 0	2015 7(a) loans: 1 504 loans: 1	2016 7(a) loans: 0 504 loans: 0
Recommended Actions for FY 2018	Status at end of FY 2017		7(a)	504
1. Monitor and verify implementation of corrective actions to ensure effective resolution prior to closeout.	<b>Green ↑</b>	<b>Green ↑</b>		
2. Demonstrate that information from the portfolio risk management program is used to support risk-based decisions and implement additional controls to mitigate risks in SBA loan programs.	<b>Yellow</b>	<b>Yellow</b>		
3. Develop an effective method of disclosing and tracking loan agent involvement in SBA business loan programs.	<b>Yellow</b>	<b>Orange</b>		
4. Update regulations (13 CFR Part 103) regarding loan agents to provide effective enforcement procedures.	<b>Yellow</b>	<b>Yellow</b>		
5. Implement a loan agent registration system, including the issuance of a unique identifying number for each agent.	<b>Orange</b>	<b>Orange</b>		

**Green**-Implemented    **Yellow**-Substantial progress    **Orange**-Limited Progress    **Red**-No progress



## **Challenge 5: SBA Needs to Ensure That the Section 8(a) Business Development Program Identifies and Addresses the Needs of Program Participants, Only Eligible Firms Are Admitted Into the Program, and Standards for Determining Economic Disadvantage Are Justifiable**

---

SBA's 8(a) Business Development Program was created to provide business development assistance to eligible small disadvantaged businesses seeking to compete in the American economy. A major benefit of the 8(a) program is that 8(a) firms can receive sole source, as well as set-aside, competitive Federal contracts so that small businesses do not need to compete with large businesses that may have an industry advantage. SBA's challenge has been to ensure that it is providing effective business development assistance to 8(a) firms and that only eligible firms are admitted into and remain in the program. Additionally, SBA faces the challenge of developing objective and reasonable criteria for determining at which point socially disadvantaged individuals are deemed economically disadvantaged.

### **SBA Continues to Address Its Ability to Deliver an Effective 8(a) Program**

SBA has made its assistance more readily available to program participants by using resource partners, such as small business development centers, SCORE, and procurement technical assistance centers. SBA also has taken steps to ensure business opportunity specialists assess program participants' business development needs during site visits. Additionally, in September 2016, SBA issued its 8(a) program SOP to reflect the March 2011 regulatory changes.

While SBA took a positive step by issuing the 8(a) program SOP, SBA has made limited progress in its monitoring efforts to track participants' progress. For example, although SBA awarded a \$1.9 million contract in December 2011 to develop and deploy a new IT system to assist in monitoring 8(a) program participants, in 2014, SBA decided not to deploy this new system. Instead, SBA is now developing and implementing another IT system, Certify.sba.gov, that is broader in scope than just the 8(a) program to include the WOSB, HUBZone, and Mentor-Protégé programs. SBA plans to implement the 8(a) program functions later in 2017. As of August 2017, SBA has spent \$6.8 million on this system.

### **Streamlined Application Process May Expose the 8(a) Program to a Higher Risk of Fraud**

Since 2010, there had been a steady decline in the number of firms participating in the 8(a) program from about 7,000 in 2010 to about 4,900 as of August 2016. Consequently, in FY 2016, SBA leadership developed an aggressive growth plan to increase the number of participants in the 8(a) program by 5 percent over the previous year through a streamlined application process. As of March 2017, SBA reported the 8(a) program includes 5,260 firms.

According to SBA officials, the streamlined application process is less burdensome for firms applying to the 8(a) program. As part of this modified process, various documents previously used to determine an applicant's eligibility to participate in the 8(a) program would no longer be requested or would be required in a modified version. However, shortening the review process by eliminating documents may erode core safeguards that prevented questionable firms from entering the 8(a) program. Furthermore, in FY 2016, we initially reported that SBA did not fully document that 30 of 48 firms were eligible for the 8(a) program. As a result, it was not clear whether these 30 firms should have been approved into the 8(a) program ([Report 16-13](#)). At the request of SBA's former Deputy Administrator, we conducted a follow-on audit to determine whether SBA resolved eligibility concerns for the 30 firms. We determined that SBA resolved eligibility concerns for 20 of

the 30 firms that we reviewed. However, we continued to question the eligibility of 10 of the 30 firms ([Report 17-15](#)). Based on the audit, SBA agreed to add additional controls to the process.

Although SBA’s efforts to increase the participation in the 8(a) program is consistent with its mission, SBA still needs to ensure that only eligible firms are admitted into and remain in the program, and that the documentation supporting 8(a) program application approvals is maintained in a method ensuring clear eligibility of the applicant. A lack of documentation clearly demonstrating eligibility of applicants or a lack of due diligence by SBA program managers can present evidentiary challenges when pursuing fraud against SBA and its program participants.

### **SBA Dollar Threshold for Economic Disadvantage Not Justified**

In March 2011, SBA revised its regulations and established additional standards to address the definition of “economic disadvantage.” Although the March 2011 regulations establish the threshold for “economic disadvantage,” we have concerns that SBA’s standards for determining economic disadvantage are not justified or objective because they are not based on economic analysis.

Agency officials stated that the comments they received to the revised regulations served as an adequate proxy to objectively and reasonably determine effective measures for economic disadvantage, and they were not aware of any reliable sources of data to determine economic disadvantage. OIG contends that public comment, while valuable, cannot replace the expert and independent analysis that Congress entrusted SBA to provide when implementing this program. The Agency should develop objective and reasonable criteria for determining the threshold where socially disadvantaged individuals face economic disadvantage due to diminished credit and capital opportunities. In September 2017, SBA awarded a contract to conduct a study to assist them in defining or establishing criteria for determining what constitutes “economic disadvantage.”

Number of Actions Accomplished (Green Status) During Past Four Fiscal Years (Challenge first reported in FY 2003)	2013: 0	2014: 0	2015: 0	2016: 0
Recommended Actions for FY 2018				Status at end of FY 2017
1. Develop and implement a plan, including SOP provisions, which ensures that the 8(a) Business Development Program identifies and addresses program participants’ business development needs on an individualized basis.				Green ↑
2. Update and issue the 8(a) Business Development SOP to reflect the March 2011 regulatory changes.				Green ↑
3. Establish objective and reasonable criteria that effectively measure “economic disadvantage” and implement the new criteria.				Orange ↑
4. Augment and Implement controls that ensure only eligible firms are admitted into the 8(a) program.				New
5. Develop and implement a system to assist program officials in monitoring participants’ progress in the 8(a) Business Development Program and providing business development needs on an individualized basis.				New

**Green**-Implemented    **Yellow**-Substantial Progress    **Orange**-Limited Progress    **Red**-No Progress

## **Challenge 6: SBA Can Improve Its Loan Programs by Ensuring Quality Deliverables and Reducing Improper Payments at SBA Loan Operation Centers**

---

In FY 2016, the dollar amount of SBA's 7(a) loans approvals reached record highs of \$24.1 billion. The majority of these loans are made by lenders with delegated approval authority. When a loan goes into default, SBA will conduct a review of 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." For loans sold on the secondary market, SBA is obligated to purchase the guarantee from the investor and performs a review of the lenders actions after payment is made. Pursuing recovery from a lender on sold loans is generally a more difficult task for SBA. In FY 2016, the amount of loans sold on the secondary market reached record highs of \$9.4 billion.

Previous OIG audits noted that quality control activities were not being performed at the Centers in accordance with SBA's overall Quality Control and Center specific guidance, and SBA management emphasized quantity over quality for 7(a) loan origination reviews and loan specialists were not provided adequate guidance or training. In addition, OIG identified 7(a) loans that were ineligible, lacked repayment ability, or were not properly closed, resulting in improper payments. These improper payments occurred in part because SBA did not adequately review loans.

Since the audits, the Office of Capital Access (OCA) improved the quality control program for its loan centers and took actions to accurately report and reduce improper payments. Also, OCA modified the structure of a key loan center to allow for appropriate supervision and revised production standards for loan specialists. Further, OCA is also in the process of hiring additional staff.

While OCA made substantial improvements, it needs to continue to demonstrate in FY 2018 that its process over disputed cases ensures adequate and timely resolution. In addition, OCA needs to provide evidence that the developed corrective action plans are effective in reducing improper payments. OCA will also need to demonstrate that its loan centers are staffed with qualified resources that are appropriately trained and supervised.

### **SBA Improved Its Quality Control Program to Ensure Timely Implementation of Corrective Actions**

OCA has made significant progress in developing and implementing a quality control program for all of its loan centers to verify and document compliance with the loan process, from origination to closeout. Additionally, OCA has taken actions to accurately report and reduce improper payments in SBA's 7(a) Loan Program. OCA has formalized its improper payment sampling, demonstrated that its improper payments review process is effective for 7(a) loan approvals, formalized its process to review disputed cases, formalized the recovery process and time standards for 7(a) purchases, developed corrective action plans for 7(a) loans, established repayment ability review requirements that are effective at identifying improper payments, revised improper payment review checklists, and demonstrated recovery from lenders in a timely manner during FY 2016.

To improve effectiveness, OCA revised its dispute resolution process and established a committee of senior leaders that meets regularly to discuss disputed cases and reach consensus. This committee includes directors from key OCA offices, including the Office of Credit Risk Management. In FY 2017, OCA created a specialized team to triage loans in inventory, dedicated a staff member to work on denial cases involving origination issues, and resolved 125 denial cases. In addition, SBA noted that there were no disputed loans in the last 3 years between the National Guaranty Purchase Center and Office of Portfolio Management. To further improve reviews of loans, OCA is working on

assigning analysts based on the primary denial issues and age of the loans. OCA is also completing its “triage project,” which it believes will help resolve issues by obtaining additional information from lenders.

In FY 2017, OCA developed enhanced improper payments reporting to monitor root causes and identify operational risk. These reports inform management on training opportunities and improvements needed in policies and procedures. Further, the quality control team recommended policy changes in the SOP 50 10 rewrite to reduce improper payments.

OCA needs to continue to demonstrate in FY 2018 that its process over disputed cases ensures adequate and timely resolution. Further, OCA needs to provide evidence that the developed corrective action plans are effective in reducing improper payments.

### **Inadequate Staffing, Training, and Supervision Have Resulted in Material Underwriting Deficiencies**

The need to deliver timely SBA loan approval, servicing, and purchase decisions while ensuring they meet reasonable standards for quality and accuracy is often a difficult balance for program management. In addition, SBA processing centers often have to meet high demands for production with limited resources, resulting in inventory backlogs and a focus on production activities. For example, a 2014 report ([Report 14-13](#)) noted that SBA management emphasized quantity over quality for 7(a) loan origination reviews at the Loan Guaranty Processing Center (LGPC) and that loan specialists were not provided adequate guidance or training to conduct their 7(a) loan review activities. SBA addressed our recommendations to revise production standards, improve internal guidance, develop a training plan, and allocate resources to ensure risk is mitigated and quality is emphasized. In doing so, SBA modified the structure of the LGPC to allow for appropriate supervision. Additionally, the center revised production standards for loan specialists related to screen outs. SBA will need to continue to demonstrate that the LGPC is appropriately staffed with qualified resources that are appropriately trained and supervised.

### **Improvements Are Needed in the Identification of Improper Payments**

As noted above, OCA has taken actions to accurately report and reduce improper payments in SBA’s 7(a) Loan Program. However, OIG audits have identified 7(a) loans that were ineligible, lacked repayment ability, or were not properly closed, resulting in improper payments. These improper payments occurred in part because SBA did not adequately review loans.

OIG reviews high-risk loans purchased by SBA to determine whether lenders materially complied with SBA requirements or identify suspicious activity. Results to date ([Report 16-22](#)) have found that both SBA purchase and quality control operations continue to miss material lender underwriting deficiencies, resulting in improper payments. Specifically, we have recommended recoveries of nearly \$5 million on six loans. In addition, we identified suspicious activity on two loans totaling \$1.4 million, resulting in formal referrals to our Investigations Division. While previous audits have noted that the application of increased scrutiny was necessary on high-dollar loans that default early, further improvements are needed for SBA to ensure that the risk of improper payments on these loans is sufficiently mitigated. For example, the 7(a) loans we review are often complex and require additional time and research to validate the appropriateness of lender actions. We observed that in some cases, SBA loan specialists questioned lenders on material compliance issues; however, these loan specialists ultimately accepted explanations and documentation from lenders that did not cure the deficiencies. We noted that loan specialists are generally required to complete loan file reviews within 6 hours. We recommended that SBA

evaluate the time National Guaranty Purchase Center loan specialists have to review complex early-defaulted loans.

In FY 2017, OCA modified the production standards to allow loan specialists more time to review complex early-defaulted loans. In addition, OCA made the decision to increase the staffing level at the NGPC and is in the process of hiring staff. OCA needs to demonstrate in FY 2018 that the additional time allotted to loan specialists on complex early-defaulted loans, is sufficient to identify complex improper payments. Further, OCA needs to provide comprehensive training plans.

Actions Accomplished (Green Status) During Past Four Fiscal Years (Challenge first reported FY 2010)	2013 7(a) Approvals:1 7(a) Purchases: 0	2014 7(a) Approvals:1 7(a) Purchases:1	2015 7(a) Approvals:0 7(a) Purchases:1	2016 7(a) Approvals:0 7(a) Purchases:0
Recommended Actions for FY 2018	Status at end of FY 2017			
	7(a) Approvals		7(a) Purchases	
1. Reassign responsibility for final approval of disputed denial, repair, and improper payment decisions to the Office of Credit Risk Management (OCRM) to ensure an adequate and timely resolution.	N/A		Green ↑	
2. Demonstrate that corrective action plans are effective in reducing improper payments in the 7(a) Loan Program.	Yellow		Yellow	
3. Ensure that centers are appropriately staffed with qualified resources that are appropriately trained and supervised and that the quality of Center resource deliverables is appropriately balanced against their production requirements.	Yellow		Yellow	
<b>Green</b> -Implemented <b>Yellow</b> -Substantial Progress <b>Orange</b> -Limited Progress <b>Red</b> -No Progress				

## **Challenge 7: Disaster Assistance Must Balance Competing Priorities to Deliver Timely Assistance and Reduce Improper Payments**

---

The disaster loan programs play a vital role in the aftermath of disasters by providing long-term, low-interest loans to affected homeowners, renters, businesses of all sizes, and non-profit organizations. SBA's FY 2016 year-end disaster assistance loan portfolio balance was \$6 billion. SBA must balance the priority of delivering timely assistance to disaster survivors in the immediate aftermath of a devastating life event against the need to ensure program integrity.

Following Hurricane Katrina, in 2008, new private sector disaster loan programs were statutorily authorized and were intended to assist in disbursing funds quickly and effectively. SBA has not fully implemented all of these programs. The authorizing legislation required SBA to implement guaranteed disaster loan programs in partnership with private lenders. SBA only has promulgated regulations to implement two of the three new private sector disaster loan programs, which were intended to facilitate more timely assistance to disaster survivors by leveraging private sector resources. The Recovery Improvements for Small Entities (RISE) After Disaster Act of 2015 also authorized another private lender disaster loan program, which SBA has not implemented. The ability to provide low-interest disaster loans in a timely manner is necessary to help small businesses and homeowners recover from a declared disaster, which is a key tenet of SBA's mission—to assist in the economic recovery of communities after disasters.

We also are concerned that SBA does not limit the proportion of a borrower's gross income that may be relied on to service debt, potentially leaving borrowers with insufficient income to cover living expenses, taxes, and loan payments. Loans to borrowers with high debt burdens are more likely to default. Additionally, prior audits performed by OIG and GAO have found that because SBA had not taken sufficient steps to prepare for large-scale disasters, such as properly preparing and training a new workforce for high application volumes, the program has often been unable to provide timely assistance in the aftermath of major disasters.

Finally, disaster loans are vulnerable to improper payments, fraud and default because loan transactions are often expedited in order to provide quick relief to disaster survivors, lending personnel hired in connection with a disaster declaration may lack sufficient training or experience, and the volume of loan applications may overwhelm SBA's resources and its ability to exercise careful oversight of lending transactions. SBA has greatly reduced its reported improper payment rate from prior years, but because of the need to mobilize a new workforce to respond to large-scale disasters such as Hurricane Harvey, SBA is continually challenged to maintain a low improper payment rate in this program.

### **Private Lender Programs Intended to Quickly Disburse Disaster Funds Not Implemented**

In the wake of disasters like Hurricane Sandy, congressional representatives expressed concern that SBA did not effectively develop and utilize programmatic innovations intended to assist in disbursing funds quickly and effectively. In particular, SBA has not implemented two of the three private lender disaster loan programs mandated by the Small Business Disaster Response and Loan Improvements Act of 2008. Through these mandates, Congress sought to expand steps taken by SBA after Hurricane Katrina and require new measures to help ensure that SBA would be prepared for future disasters. The act included three provisions requiring SBA to issue regulations to establish new guaranteed disaster programs using private sector lenders—the Economic Injury Disaster Assistance Program (EDAP), the Private Disaster Assistance Programs (PDAP), and the Immediate Disaster Assistance Program (IDAP). Together, these programs are collectively known as the “Guaranteed Disaster Assistance Programs.”

SBA established regulations and procedures to deliver IDAP, but has not done so for the EDAP and PDAP. In July 2016, SBA notified Congress that it had sought advance public comment on proposed rulemaking for EDAP and PDAP and received limited public responses, the majority of which were opposed their implementation. SBA also reports that its partner lenders have chosen not to participate in IDAP. That aside, SBA indicates that it has improved its disaster assistance delivery channel and is now better equipped to provide more timely disaster assistance. SBA asserts that larger unsecured disaster loan limits, now \$25,000, allow more funds to be disbursed quickly following a disaster.

In FY 2017, SBA continued to refine internal procedures to account for IDAP loans. However, SBA also has requested Congress to rescind the program in its FY 2018 Budget Justification. Correspondingly, the House Appropriations markup includes permanent cancellation of \$2.6 million in unobligated funding for IDAP and EDAP in FY 2018. OIG notes GAO has closed all audit recommendations related to these programs. Without congressional action to rescind the Guaranteed Disaster Assistance Programs, SBA should seek lender participation in IDAP and conclude the rulemaking process to establish regulations implementing EDAP and PDAP in compliance with the law.

### **Express Recovery Opportunity Loan Program Not Implemented**

The RISE After Disaster Act, enacted November 25, 2015, introduced the Express Recovery Opportunity Loan Program that was intended to leverage private sector resources to quickly provide up to \$150,000 loans to disaster survivors. The Act required SBA to promulgate regulations for the loan program within 270 days, which SBA has not yet accomplished.

In FY 2017, SBA studied this proposed program and concluded that it duplicates the existing SBA Express Loan Program, cannot be delivered as designed without subsidy costs, and puts the entire SBA Express Loan Program at risk due to an extended eligibility period. SBA determined that this program could not be delivered at zero subsidy with the fee structure that was enacted. The Act provides for loans with an 85 percent guarantee with a fee equivalent to 50 percent guarantee; we note, however, that the Act provides an exception to this fee structure in years where the program cost is greater than zero and this cost can be attributed to Express Recovery Opportunity Loans. SBA also believes that the 5-year disaster eligibility period will cause lenders to shift ordinary Express loans to Recovery Express loans due to the higher guarantee rate, exposing SBA to greater risk and endangering the program. SBA stated that it plans to request rescission of this program in its FY 2019 Budget Justification and for this reason, it has deferred creation of program regulations. Without congressional action on its request to rescind the Express Recovery Opportunity Loan Program, SBA must promulgate regulations in compliance with the law.

### **Maximum Allowable Fixed Debt May Be Exceeded, Limiting Borrower's Ability to Repay Disaster Loans**

SBA's disaster assistance loan officers work diligently to provide eligible disaster survivors with the maximum available financial assistance on attractive terms. On occasion, in order to facilitate widespread program delivery of disaster home loan benefits, SBA exceeds its normal home loan debt-to-income lending parameters, potentially straining and/or limiting the borrowers' ability to repay the disaster loans. SBA's disaster assistance home loan rules do not specify an upper limit to the proportion of a borrower's gross income that may be relied upon to service debt. Allocating too much of the borrower's income for debt servicing could result in the borrower having insufficient income to cover unavoidable living expenses, such as health insurance, utility bills, and taxes. This practice also results in more defaulted loans and additional financial distress to disaster survivors.

The revised disaster assistance SOP, issued in 2015, permits approval of home loans with greater than normal debt-to-income ratios; however, the SOP did not establish an upper threshold to income allocated for home loan debt service under this provision. While SBA's disaster assistance SOP does provide a formula for determining the minimal amount of income reserved for living expenses and taxes when evaluating disaster business loan guarantors' repayment ability, the disaster home loan program rules do not include a similar required reserve of income to meet necessary living expenses.

An August 2016 report ([Report 16-18](#)) on early-defaulted Hurricane Sandy loans found that loans to borrowers who did not otherwise have repayment ability were approved by allocating high proportions of borrower income to service debt. Home loans with higher than normal debt service ratios given to borrowers with low incomes and poor credit histories appeared especially vulnerable to default. SBA should determine when the borrower's proposed debt service ratio creates an unacceptable financial burden to the disaster survivor and train its loan officers to safeguard loan affordability.

In FY 2017, SBA continued to train loan processing personnel on repayment ability and provide guidance to make appropriate credit decisions. In FY 2018, SBA should establish policy that limits the percentage of income that may be relied upon to service debt and provide a reasonable percentage of income remaining to meet essential needs.

### **Reserve Staff Require Training to Sustain Productivity During Mobilization**

During large-scale disasters such as Hurricanes Sandy and Harvey, SBA must bring on new loan officers and loss verifiers in order to match the volume of loan applications and prevent processing backlogs that delay the delivery of disaster assistance. A prior Hurricane Sandy GAO audit found that new loan officers were not adequately trained to quickly respond to the backlog of loan applications and took longer than expected to learn how to correctly process loans. SBA has since adjusted its training approach, but Hurricane Harvey is the first large-scale mobilization since Hurricane Sandy in 2012.

In FY 2017, SBA conducted loan officer and loss verification training and developed just-in-time training for new staff. This training imparts required knowledge and skills for immediate application at the time staff are mobilized. SBA believes that because staff will immediately use the material taught, they will be motivated and focused to learn it. SBA has trained 100 loan officers and 100 loss verifiers who can be quickly mobilized in the event of a disaster. In FY 2018, SBA should monitor its results and refine its training approach, if needed, depending on the results of the Hurricanes Harvey and Irma disaster cycles.

### **Improper Payment Rate Remains Above IPERA Significance Threshold**

In FY 2016, the Disaster Assistance Program's improper payment rate decreased to 5.32 percent from the 8.13 percent reported in FY 2015.<sup>2</sup> However, it remains above the threshold for significant improper payments defined by IPERA (\$10 million and 1.5 percent of program outlays)—improper payments were \$18.35 million of the \$345 million in program outlays in FY 2016. To reduce disaster loan improper payments, SBA's Office of Disaster Assistance (ODA) should strengthen controls related to verification and documentation of loan eligibility, insurance coverage, and other program requirements that have been identified as the most prevalent errors in the program. If properly addressed, SBA can effectively reduce the improper payment rate in

---

<sup>2</sup> The most current improper payment data available at this time are for FY 2016.



future years. While SBA has made progress in reducing improper payments in the disaster loan programs, our ongoing audit work indicates that further improvements are needed. In FY 2018, SBA needs to continue to meet its improper payment reduction targets.

Actions Accomplished (Green Status) During Past 4 Fiscal Years (Challenge first reported FY 2015)	2013: N/A	2014: N/A	2015: N/A	2016: N/A
Recommended Actions for FY 2018				Status at end of FY 2018
1. Promulgate regulations for the new guaranteed disaster loan programs mandated by Congress in 2008.				<b>OCA</b> <b>Yellow ↑</b>
2. Promulgate regulations for the Express Recovery Opportunity loan program provided by the RISE After Disaster Act.				<b>OCA</b> <b>Yellow</b>
3. Demonstrate that the Agency has adequately trained loan processing resources that can be quickly mobilized in the event of a disaster.				<b>ODA</b> <b>Yellow</b>
4. Establish policies that limit borrower debt burdens to affordable levels and train loan processing personnel in the application of those policies.				<b>ODA</b> <b>Yellow</b>
5. Reduce the improper payment rate to 4.78 percent or lower in FY 2018, in accordance with the reduction targets established in the FY 2016 Agency Financial Report.				<b>ODA</b> <b>Yellow</b>

**Green** Implemented   **Yellow**-Substantial Progress   **Orange**-Limited Progress   **Red**-No Progress

## Challenge 8: SBA Needs to Effectively Manage Its Acquisition Program

Annually, SBA spends over \$100 million on contracts for goods and services required to meet its mission. With decreasing budgets, it is essential that SBA manages its acquisition program in an efficient, effective, and accountable manner to ensure the Agency obtains quality goods and services on time and at a fair price. However, prior OIG audits have identified instances where this was not the case. For example, SBA did not always comply with Federal regulations when determining whether using interagency acquisitions was the best procurement approach, and it inadequately planned its requirements for procuring IT products and services.

During FY 2017, SBA took appropriate actions to address challenges in its acquisition program. SBA hired a Senior Procurement Executive, responsible for managing and directing the Agency's acquisition system, including implementing unique acquisition policies, regulations, and standards. SBA also implemented actions to address the deficiencies identified in its assessment of the acquisition program's internal controls by, among other things, revising and issuing the Government Acquisition Program SOP, streamlining the hiring process for contracting officers, and making significant improvements to its information systems. Though OMB recently suspended its requirement for agencies to conduct such reviews, SBA plans to continue to conduct internal control reviews of its acquisition program. As a result, these implemented improvements fully address the concerns in this challenge.

Actions Accomplished (Green Status) During Past 4 Fiscal Years ( <i>Challenge first reported FY 2013</i> )	2013: 0	2014: 0	2015: 1	2016: 0
Recommended Actions for FY 2018				Status at end of FY 2017
1. Create and implement a comprehensive improvement plan—based on the results of the acquisition function assessment—that has measurable goals, objectives, prioritized actions, and timeframes to address deficiencies identified in the organizational alignment and leadership assessment area.				Green ↑
2. Create and implement a comprehensive improvement plan—based on the results of the acquisition function assessment—that has measurable goals, objectives, prioritized actions, and timeframes to address deficiencies identified in the acquisition policies and processes assessment area (i.e., acquisition management SOP).				Green ↑
3. Create and implement a comprehensive improvement plan—based on the results of the acquisition function assessment—that has measurable goals, objectives, prioritized actions, and timeframes to address deficiencies identified in the acquisition workforce assessment area.				Green ↑
4. Create and implement a comprehensive improvement plan—based on the results of the acquisition function assessment—that has measurable goals, objectives, prioritized actions, and timeframes to address deficiencies identified in the knowledge management and information systems assessment area.				Green ↑

**Green**-Implemented    **Yellow**-Substantial progress    **Orange**-Limited Progress    **Red**-No progress