

# TOP MANAGEMENT AND PERFORMANCE CHALLENGES FACING THE SMALL BUSINESS ADMINISTRATION IN FISCAL YEAR 2021

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## MESSAGE FROM THE INSPECTOR GENERAL

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I am pleased to present the Office of Inspector General Report on the *Top Management and Performance Challenges Facing the Small Business Administration* for fiscal year (FY) 2021, as required by the Reports Consolidation Act of 2000.

This year has presented tremendous challenges to SBA, the likes of which the agency has never encountered in its history. The devastating impact of Coronavirus Disease 2019 (COVID 19) on our nation and small businesses catapulted SBA into the spotlight as the primary agency responsible for providing nationwide assistance to small businesses.



This report discusses several challenges and issues, many of which we have discussed in previous reports. Managing COVID 19 stimulus is the greatest overall challenge facing SBA currently. This crucial new challenge is exacerbated by persisting management and performance challenges best described as systemic. Pandemic response has, in many instances, magnified the challenging systemic issues in SBA's mission-related work.

Overall, the agency has made progress addressing this year's list of management challenges. We believe that progress is in large part attributable to the agency's concerted effort to address outstanding internal control recommendations that are reflected in many component challenge corrective action areas.

However, our audits and investigations continue to find the agency facing significant risks in

- loan program oversight and controls,
- oversight of statutory programs to promote small business development and government contracting, and
- deploying information technology and related cybersecurity controls.

### Challenges Not Failings

Identification of an issue as a top challenge does not necessarily denote significant deficiencies or lack of attention on SBA's part. All but one of these challenges are longstanding, inherently difficult, and may likely continue to be challenges in the coming years. Resolving the challenges will require consistent, focused attention from agency management and ongoing engagement with Congress, the public, and other stakeholders.

**It is also important to note that the top challenges are not listed in order of importance or magnitude, except for the COVID 19 challenge,** which we address first in this report. We view all eight challenges as critically important to SBA operations in the upcoming year.

## Changes to This Year's Report

We have made some significant changes in this year's report, as follows:

- **We added a new challenge (Challenge 1)** related to the impact of the COVID 19 pandemic on SBA programs and operations.
- **We present challenges in a new format** to include a discussion of each challenge and underlying issues, agency progress in meeting the challenge, and work remaining for the agency to reduce or eliminate the challenge.
- **We eliminated recommendations for each challenge.** In previous reports, each management challenge was followed by a series of recommended actions to enhance the effectiveness of agency programs and operations. Each recommended action was assigned a color score to indicate its status. Instead, in this year's report, we color-code issues underlying each challenge, shown in Table B.
- **We removed the human capital management challenge (formerly Challenge 3).** SBA has made substantial improvements to its human capital strategies to address the challenges we identified. SBA developed and implemented plans that aligned talent needs and capability with its strategic plan. It also implemented strategic workforce and succession plans to identify competency gaps, strengthen leadership capacity, and address the challenges of its aging workforce.

SBA continues to make progress in addressing our recommendation to update its human capital management policies. In FY 2020, SBA updated and implemented 11 human capital management policies. SBA also improved communication of the new policies through outreach efforts.

- **We removed the challenge on SBA's exclusions for determining governmentwide federal contracting goal-setting guidelines, referred to as "goaling" (previously included in Challenge 2).** Over the last several years, SBA has amended its goaling guidelines and since FY 2013, the agency has been adding previously excluded contracts back to the goaling equation.

SBA has also improved transparency of the exclusions on its website by adding a link to the FY 2018 guidelines. OIG maintains the Small Business Act requires SBA to use the value of all prime contracts to determine governmentwide small business procurement goals and achievements; excluding prime contracts for governmentwide goals and reports does not meet the law. However, because of SBA's new transparency in disclosing how it calculates goal percentages, we no longer believe this issue is a serious management challenge.

- **We removed the challenge on SBA's portfolio risk management system (previously included in Challenge 4).** From FY 2016 to FY 2020, SBA made significant improvements to ensure the portfolio risk management program supported risk-based decisions and implemented additional controls to reduce risks in SBA loan programs. Specifically, SBA established performance measures and risk mitigation goals for each loan program and the entire lending portfolio.
- **We removed the challenge on SBA's quality control program to reduce improper payments (previously included in Challenge 6).** Over the last several years, SBA developed enhanced improper payment reporting to monitor root causes, identify operational risk, and create corrective action plans.

From FY2018 to FY2020, SBA provided a comprehensive metric report documenting the effectiveness of corrective actions to mitigate improper payments and an assessment of the improper payment process. The agency also required additional controls to ensure proper scrutiny is applied in testing plans and checklists. SBA has confirmed that the quality control function continues to make policy recommendations to the Office of Financial Assistance and lender referrals to the Office of Credit Risk Management on matters that could potentially cause improper payments.





Table 2 lists the management challenges and issues associated with each that we discuss in this report.

## Color Coding to Indicate Progress

As in previous years, this report uses a color scheme as a visual indicator of the agency’s progress in confronting the issues that make a particular function a top management challenge. We include a color meter indicator with the issues we describe for each challenge to show whether SBA has made progress (see Table 1). The exception in this year’s report is Challenge 1.

We have not color-coded the issues the agency is confronting with the COVID-19 loan programs because the situation creates a new reporting element. In this report, we describe the issues and problems we have found so far. But it would be unfair to judge progress when the agency is diligently working to fulfill the economic goals of the laws passed in March.

**Table 1. Color-Code Definitions**

Color	Definition	Color indicator
Green	Issue Resolved or Appropriately Reduced	
Yellow	Substantial Progress	
Orange	Moderate or Limited Progress	
Red	No Progress	

The management challenges report is an important tool to help the agency prioritize its work to improve program performance and enhance operations. These challenges will guide OIG work in the coming year. We look forward to continuing to work with SBA’s leadership team to address the agency’s top management and performance challenges.

**Table 2. Top Management and Performance Challenges Facing SBA in FY 2021.**

Challenge	Issues
<b>Challenge 1</b> SBA's Economic Relief Programs Are Susceptible to Significant Fraud Risks and Vulnerabilities	Paycheck Protection Program Susceptible to Abuse and Fraud
	Paycheck Protection Program Eligibility
	Paycheck Protection Program Data Reliability
	Potentially Fraudulent COVID-19 Economic Injury Disaster Loans
<b>Challenge 2</b> Inaccurate Procurement Data and Eligibility Concerns in the Small Business Contracting Programs Undermine the Reliability of Contracting Goal Achievements	Agencies Receive Credit for Ineligible Firms or Firms No Longer in the 8(a) or HUBZone Programs
	Women-Owned Small Business Federal Contracting Program Susceptible to Abuse
<b>Challenge 3</b> SBA Needs to Improve Oversight of IT Investment and Reduce IT Security Risks	SBA's New IT Investment Controls Need Improvement
	Additional Progress Needed on Security Controls
<b>Challenge 4</b> SBA Risk Management and Oversight Practices Need Improvement to Ensure the Integrity of Loan Programs	SBA's Oversight of High-Risk Lending Participants
	Increased Risk Introduced by Loan Agents
	Increased Risk Introduced by Lender Service Providers
<b>Challenge 5</b> SBA Needs to Administer the Section 8(a) Business Development Program Effectively	SBA Continues to Address Its Ability to Develop Firms in the 8(a) Program and Measure Results
	Streamlined Application Process May Expose the 8(a) Program to Higher Fraud Risk
	Deficiencies in Continuing Eligibility Processes Expose the 8(a) Program to Higher Fraud Risk
	SBA Dollar Threshold for Economic Disadvantage Should Be Based on Verifiable Data
<b>Challenge 6</b> Identification of Improper Payments in SBA's Loan Programs Remains a Challenge	Improvements Needed to Ensure High Risk 7(a) Loan Reviews Reduce the Risk of Losses
<b>Challenge 7</b> SBA's Disaster Assistance Program Must Balance Competing Priorities to Deliver Prompt Assistance but Prevent Potential Fraud	Reserve Staff Need Training to Sustain Productivity During Mobilization
	Improper Payment Quality Assurance Process Needs Strengthening
	Inadequate Verification of Cause and Extent of Damages
<b>Challenge 8</b> SBA Needs Robust Grants Management Oversight	SBA's Grants Management System Needs Improvement



## Challenge 1

# SBA's Economic Relief Programs Are Susceptible to Significant Fraud Risks and Vulnerabilities

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## Paycheck Protection Program

### Why This Is a Challenge

**M**ore than 30 million small businesses in the United States have been negatively affected by COVID-19. The President signed the Coronavirus Aid, Relief, and Economic Security (CARES) Act into law on March 27, 2020, to provide economic relief to our nation.

Under the CARES Act, the Small Business Administration (SBA) fully guarantees relief loans for eligible small businesses, individuals and nonprofit organizations that can be forgiven if loan proceeds were used as the Act requires. Eligible expenses include payroll, rent, utility payments, and other limited uses. The CARES Act appropriated \$349 billion for the SBA Paycheck Protection Program (PPP) under the 7(a) small business lending program.

In early April 2020, SBA launched the \$349 billion PPP in collaboration with the U.S. Department of the Treasury. On April 24, 2020, Congress appropriated an additional \$321 billion for PPP through the Paycheck Protection Program and Health Care Enhancement Act, bringing the total for the program to \$670 billion. The deadline for PPP borrowers to apply for a loan was originally June 30, 2020, however Congress passed legislation that extended the expiration of the program until August 8, 2020.

As of August 8, 2020, SBA had processed 5.2 million guaranteed loans, totaling \$525 billion through 5,460 private lenders, far more than all of SBA's combined lending under the 7(a) program from 1990 to 2019. From fiscal years (FYs) 2000-2019, SBA made about 1.2 million 7(a) loans totaling \$333 billion. On average, SBA made about 62,000 loans a year totaling about \$16.7 billion.

SBA moved quickly to establish the new nationwide program but eased controls required in its lending programs to do so, increasing the risk of rampant fraud.

### Issue: Paycheck Protection Program Susceptible to Abuse and Fraud



Our preliminary investigative oversight revealed strong indicators of widespread potential abuse and fraud in the PPP. Since the PPP began, OIG has had a major increase in reports of suspected fraud. These reports of suspected fraud have come from various sources, including OIG Hotline complaints, contacts from financial institutions, and other

law enforcement agencies, and we have launched numerous investigations based on these reports.

Examples of suspicious activities and suspected PPP fraud include:

- False statements on applications
- Fraudulent supporting documents (such as payroll and tax forms)
- Accounts established using stolen identities
- Corporate identity theft
- Inflation of payroll
- Misuse of proceeds
- Unqualified borrowers
- Businesses created after PPP was in effect
- Lender fraud

OIG received more than 77,000 Hotline complaints of potential fraud by the end of September and the numbers continue to rise. Complaints of potential fraud or scams include the following:

- Loan applicants fraudulently have stated they own a business but do not
- Business owners have received funds but did not use it for their business
- Business owners have laid off employees to reduce their employment numbers and qualify for a PPP loan
- Business owners have refused to allow employees to return to work, telling them to continue unemployment assistance
- People on the web have offered to prepare fraudulent applications for a fee

OIG has identified trends that indicate widespread fraudulent activity in the program in the high volume of complaints. These trends match the arrests and ongoing investigations our agents and other government agencies are pursuing. As of August 28, 2020, the Justice Department had filed 39 PPP fraud cases, charging 56 defendants. Defendants are charged with bilking taxpayers out of tens of millions of dollars.

SBA's engagement with financial institutions to immediately identify disbursements that may have been obtained fraudulently could reduce or prevent additional losses because associated loan forgiveness will still be in process, and the loan forgiveness process could trigger another round of suspected fraud activity. Strong controls will help reduce or eliminate fraud risk and enhance program integrity for the PPP and similar programs enacted in the future.

### **Agency Progress**

As of October 1, 2020, SBA had not initiated loan reviews other than the automated loan reviews conducted by the application system or forgiven any loans because agency management had not finalized loan review and forgiveness processes. Agency management told us they could not share details until the processes were finalized. Without details of the loan review and loan forgiveness processes, we could not adequately assess the agency's ongoing progress.

SBA's plans and actions to reduce fraud risks and prevent further losses will determine how this challenge will be rated in the future. Our investigations into suspected fraud and suspicious activities continue. We have an ongoing review of duplicate loans made under the PPP. We anticipate future audit work on PPP loan eligibility, loan forgiveness, and lender activities, and we will continue to monitor agency actions to assess and reduce fraud risk and address vulnerabilities in the PPP.

## Issue: Paycheck Protection Program Eligibility



OIG's ongoing inspection of SBA's implementation of the PPP and coordination with the Treasury Department have revealed systemic issues. Our preliminary results found indications of deficiencies with internal controls related to eligibility of borrowers. Our ongoing review of SBA's implementation of PPP has identified thousands of loans

erroneously provided to potentially ineligible borrowers.

For example, SBA inappropriately approved loans for businesses that

- exceeded maximum loan amounts for the number of employees,
- were in the government's Do Not Pay database,
- exceeded the maximum size allowed, and
- obtained a Taxpayer Identification Number (TIN) after the program began in February 2020.

Approving loans for ineligible borrowers reduces the amount of critical program capital available to eligible borrowers. We expect to issue final reports addressing PPP eligibility in early FY 2021.

### Businesses Exceeding Maximum Loan Amounts

We found tens of thousands of approved and disbursed loans were made to borrowers for amounts that exceeded the maximum allowed based on the number of employees and compensation rates as defined in the CARES Act.

### Borrowers on Do Not Pay Database

We coordinated with the Treasury Department to compare TIN and name data provided in SBA data files against Do Not Pay debt, exclusions, and death data sources. We found tens of thousands of loans that matched a Do Not Pay data source record indicating potential loan ineligibility.

The Treasury Department Do Not Pay system helps agencies fulfill the obligation to deny federal loans, loan insurance, and loan guarantees to businesses delinquent on federal debts and obligations. To be eligible to receive PPP funds, a business must not have any current federal debarments or suspensions, and the applicant must not have delinquent federal loans or have defaulted on any federal loans in the last 7 years. The OIG will issue a report early in FY 2021 providing the final results of this analysis.

## Businesses that Exceeded Maximum Size Standards

Under the CARES Act, an eligible business cannot exceed the greater of 500 employees or the SBA size standard for number of employees in the industry, if applicable. We found hundreds of businesses obtained PPP loans that may have been erroneously approved. These businesses exceeded both 500 employees and the applicable employee-based size standard for the business industry

## Taxpayer Identification Number Registered after February 15, 2020

The CARES Act requires that businesses must have been in operation before February 15, 2020, to be eligible for a PPP loan. We found thousands of businesses obtained PPP loans with TINs that were not registered until after that date. The businesses would have been ineligible for PPP loans because they likely did not meet the CARES Act eligibility requirement of being in operation before February 15.

## Agency Progress

To confront this new challenge, agency management is reassessing existing controls and developing additional controls to ensure only eligible recipients receive loans. According to agency management, these additional controls will address various processes, including loan reviews and loan forgiveness.

SBA has established a PPP loan forgiveness platform and began accepting loan forgiveness applications on August 10, 2020. SBA also hired new staff and contractors to assist with loan reviews and loan forgiveness. However, as noted earlier, as of October 1, 2020, SBA had not finalized loan review and loan forgiveness processes, forgiven any loans, or initiated loan reviews other than the automated reviews conducted by the application system.

Swift management action to identify and review potentially ineligible loans could prevent improper payments to lenders because the associated loan forgiveness may still be in process. As we complete current reviews and do future audit work, SBA's plans and actions to reduce and prevent improper payments will determine how we will rate this challenge in the future.

## Issue: Paycheck Protection Program Data Reliability



OIG's ongoing inspection of SBA's implementation of the PPP has found that the data SBA publicly reported as well as the loan-level PPP data was inaccurate and incomplete. Job statistics were inaccurate and incomplete, industry classification codes were incomplete, loan disbursement dates were inaccurate, and underserved market data was

incomplete. Without accurate and complete data, SBA cannot reliably and accurately inform SBA management and Congress about program effectiveness and measures needed to inform program decisions. We plan to issue final reports addressing PPP data reliability in early FY 2021.

## Underserved Market Data Was Incomplete

In our flash report of May 8, 2020, we found that SBA’s demographic information for underserved markets for PPP borrowers was incomplete. SBA’s borrower application for PPP did not include standard SBA fields to request demographic information.

### Agency Progress

On May 15, 2020, SBA issued the initial PPP loan forgiveness application, which included an optional page to submit borrower demographic information. We have an ongoing audit of duplicate loans made under the PPP and anticipate future audit work to review PPP loan eligibility, loan forgiveness, and lender activities, and we will continue to monitor agency actions to enhance data reliability.

## Economic Injury COVID 19 Disaster Loan Program

### Why This Is a Challenge

In FY 2020, the CARES Act and the Paycheck Protection Program and Healthcare Enhancement Act provided \$366 billion for disaster assistance and \$20 billion for emergency advance grants for eligible entities.

SBA’s initial response to implement the COVID-19 EIDL program made billions of dollars of capital available to provide prompt economic relief to businesses affected by COVID-19. To expedite the process, SBA “lowered the guardrails” or relaxed internal controls, which significantly increased the risk of program fraud. The unprecedented demand for COVID-19 EIDLs and the equally unprecedented challenges SBA had in responding to this pandemic combined with lowered controls put significant stress on existing controls.

SBA had approved 2.2 million disaster loans for \$66.7 billion in its entire history since 1953. By contrast, between March and the end of July this year, SBA had received more than 14 million COVID-19 Economic Injury Disaster Loan (EIDL) applications and approved 3.2 million loans totaling \$169.3 billion.

During large-scale disasters such as COVID-19, SBA must bring on new loan officers to match the volume of loan applications and prevent processing backlogs that delay the delivery of disaster assistance. In its COVID-19 response, SBA increased its permanent and temporary trained staff size to more than 9,000, which was more than any other previous disaster. SBA also outsourced loan processing to a subcontractor.

## Issue: Potentially Fraudulent COVID-19 Economic Injury Disaster Loans



From the beginning of the COVID-19 EIDL program until September 30, 2020, OIG received more than 77,000 Hotline complaints, most of them alleging fraudulent activity, and thousands of complaints from banks about potentially fraudulent activity. OIG has steadily received hundreds of additional complaints per day. OIG has launched numerous investigations into this fraudulent activity. In addition, our ongoing inspection of SBA’s

initial disaster assistance response to COVID-19 has identified suspicious activity.

We found several serious problems, including significant evidence that SBA approved billions in potentially fraudulent loans to

- applicants who changed the bank account number to pay out the loan to a different number than that listed on the original loan application;
- applicants using the same Internet Protocol (IP) address, the same email address, the same bank accounts, or businesses listed at the same addresses; and
- ineligible businesses that registered an Employer Identification Number after the cutoff date of January 31, 2020.

**Potentially Fraudulent Loans to Accounts that Differed from the Original Bank Accounts Listed on Applications.** SBA had approved billions in COVID-19 EIDLs to applicants who later changed the bank account number to pay out the loan to a different number. For these applications, additional funds were disbursed in advance grants. Although there are reasons an applicant might need to change a bank account number during the loan process, the number of applicants who changed their bank account numbers or accounts to an entirely different bank before loan disbursements is concerning.

**Potentially Fraudulent Loans Made to Applicants Using Duplicate Information.** We found SBA had approved more than one loan to applicants who used the same IP addresses, email addresses, business addresses, or bank accounts. There are some legitimate reasons for individual occurrences of applicants using the same addresses or accounts to apply for loans. Multiple occurrences, however, are a strong indication of fraud.

**Potentially Fraudulent Loans Made to Ineligible Entities.** We found that SBA approved millions in COVID-19 EIDLs and advance grants to potentially ineligible entities. In our July 2020 Management Alert, we warned SBA that we had found approximately \$250 million in approved loans to ineligible entities.

## Challenge 2

# Inaccurate Procurement Data and Eligibility Concerns in Small Business Contracting Programs Undermine the Reliability of Contracting Goal Achievements

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## Why This Is a Challenge

The Small Business Act has established a governmentwide goal that 23 percent of all prime contracts be awarded to small businesses each fiscal year. Since FY 2013, the Small Business Administration (SBA) has reported that the federal government met or exceeded its goal of awarding 23 percent of federal contracting dollars to small businesses in its annual *Small Business Goaling Report*.

However, over the years, Congress has expressed concerns about the accuracy of the report. These concerns have been substantiated by OIG and Government Accountability Office (GAO) audits, which identified widespread misreporting by agencies, because contract awards reported as having gone to small firms have been substantially performed by larger companies.

As the advocate for small business, SBA must strive to ensure that only eligible small firms obtain and perform small business awards. Because SBA's goal setting, or "goaling" achievement reports do not portray federal contract dollars awarded only to small businesses, SBA reduces the ability of Congress and other federal policymakers to determine whether the government is maximizing contracting opportunities for small businesses.

## Issue: Agencies Receive Credit for Ineligible Firms or Firms No Longer in the 8(a) or HUBZone Programs



OIG audits continue to identify federal agencies that may have erroneously received credit towards their small business goals for small, disadvantaged businesses because of inaccurate reporting of the award data.

Agency contracting officers have incorrectly reported ineligible firms as certified either in the 8(a) or HUBZone programs in the Federal Procurement Data System – Next

Generation. The Office of Inspector General of the General Services Administration recently found \$89 million in procurements erroneously recorded as small business in the Federal Procurement Data System–Next Generation.<sup>1</sup>

OIG audits continue to find that SBA did not consistently detect ineligible firms in its

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<sup>1</sup> General Services Administration OIG Report Number A170121/Q/6/P20006, *The Federal Acquisition Service's Reporting of Small Business Procurements Contained Significant Inaccuracies* (September 14, 2020).

preference contract programs. In a September 2018 audit report (Report 18-22), we found SBA did not consistently detect ineligible firms in the 8(a) program and did not always act to remove firms it determined were no longer eligible for the program. We found that 20 of the 25 firms we reviewed should have been removed from the 8(a) program. These firms received \$126.8 million in new 8(a) set-aside contract obligations in FY 2017 at the expense of eligible disadvantaged firms.

In a March 2019 report (Report 19-08), we also found that SBA did not ensure that only eligible firms entered the HUBZone program; 3 of the 15 firms reviewed did not meet eligibility requirements. These firms received \$589,000 in HUBZone contract obligations at the expense of eligible firms.

In 2020, SBA changed the requirements for HUBZone employee residency eligibility. An employee no longer needs to be a current HUBZone resident to count toward the residency requirement. Instead, an employee counts as a HUBZone resident throughout that employee's unbroken tenure with the company, as long as that employee lived in a HUBZone when first used for certification purposes and remained in the residence for 180 days afterward.

HUBZone businesses could theoretically have no employees (zero) currently residing in the HUBZone but continue to be qualified under this rule. Consequently, the government's ability to argue the employee residency requirements for enforcement purposes is significantly weakened. Allowing continued certification of concerns without current HUBZone residents and no requirement that the company hire such residents in the future, appears inconsistent with the agency's legislative authorization for this program.

In FY 2020, SBA removed regulations allowing for protests of a firm's Small Disadvantaged Business status. Protest and review processes protect program integrity. This process is important because of the volume of transactions SBA reports each year as part of the governmentwide goal achievements that are *not* 8(a) Small Disadvantaged Business. As of September 2020, SBA's Dynamic Small Business Search database included 152,986 firms self-certifying as small, disadvantaged businesses.

The amount of dollars SBA reports to Congress and the public as being performed by 8(a) and HUBZone firms in the *Small Business Goaling Report* is inflated by the inclusion of contract actions performed by ineligible program participants. SBA needs to strengthen its oversight to ensure only eligible firms participate in these preference contract programs.

### **Agency Progress**

SBA has made substantial progress in implementing controls to detect ineligible firms in the 8(a) and HUBZone programs. In FY 2020, SBA updated its HUBZone policy directives for the current certification process to standardize analysis and oversight and trained staff on the guidance. SBA also implemented procedures to ensure program officials justified recommendations to admit firms applying to the 8(a) program and that tracked complaints about firms' eligibility to participate in the 8(a) program.

More transparent reporting of awards to firms that grow beyond the definition of "small" after award is necessary to show a true picture of the small business goal achievements.



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



SBA's Women-Owned Small Business (WOSB) program is intended to give those companies that meet the program's requirements greater access to federal contracting opportunities. Both OIG and GAO have reported weaknesses in SBA's controls that are supposed to ensure only eligible firms receive WOSB program set-aside contracts.

SBA officials have said the agency examines a sample of firms for eligibility and has conducted a compliance review of all four SBA-approved third-party certifiers. However, these processes and procedures have not yet been formalized.

The National Defense Authorization Act in FY 2015 granted contracting officers the authority to award sole-source awards to firms in the WOSB program and required firms to be certified by a federal agency, a state government, SBA's Administrator, or a national certifying entity approved by the Administrator. However, SBA implemented the sole-source authority provision first without a certification program.

OIG considers allowing sole-source contracting authority in the WOSB program without implementing the contemporaneously required certification program to be inconsistent with the statutory authorization. In a June 2018 audit report (Report 18-18), OIG found contracting officers at various federal agencies made sole-source awards without having the necessary documentation to determine eligibility because of SBA's implemented sole-source authority without a certification program. The change resulted in approximately \$52.2 million awarded to potentially ineligible firms.

### Agency Progress

SBA has made substantial progress toward addressing this challenge by establishing a certification process for the WOSB program and issuing a final rule. In May 2020, SBA published the WOSB certification final rule outlining new WOSB certification requirements and roles and responsibilities of SBA and third-party certifiers. SBA added language in its third-party certifier agreement to increase oversight of the certifiers, require additional reporting metrics, and include a review of the third-party certifier determination methodologies.

SBA incorporated a prescreening process to ensure that firms submit complete applications and initiated a phased approach to certifying firms in Beta.Certify.SBA.gov. The first phase began July 2020 when WOSB firms (including economically disadvantaged WOSBs) began submitting application documentation self-certifying that the firm meets program requirements. The second phase was planned to begin in October 2020 and involves SBA analysts making eligibility determinations.

Because SBA still has not implemented a certification process for the WOSB program as required, firms continue to self-certify, exposing the WOSB program to potential fraud and abuse, as well as overstating SBA WOSB contracting goals.

SBA's plans to begin making decisions on firm eligibility to participate in the program should result in agency compliance with the statutory authorization that required firms to be certified by the SBA's Administrator, among others.

### Challenge 3

## SBA Needs to Improve Oversight of IT Investments and Security Risks

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### Why This Is a Challenge

**T**he agency must continually improve its capabilities to provide program assistance to small businesses. IT security and systems oversight represent growing challenges to provide this assistance. New IT investments are needed to improve the portal interfaces for small businesses.

New portal systems must address concurrent issues such as significant transaction growth and IT security controls. SBA's systems are meeting these needs by placing a growing reliance on cloud and other third-party providers. At the same time, SBA must develop internal applications to meet changing program requirements and growing program demand.

Our previous audit work indicates SBA needs to continuously monitor internal and third-party computer systems to protect information and preserve data integrity. Application software must be properly maintained to prevent security vulnerabilities, and contingency planning to handle multiple types of threats is needed. Effective IT investment controls must be established to ensure IT investments meet identified functional requirements, projected schedules, and estimated costs.

Our current audit work seeks to gain an understanding of security incidents such as the data exposure that occurred during the EIDL loan program.

### Issue: SBA's New IT Investment Controls Need Improvement



Growth in program requirements and increasing transaction volumes requires SBA make significant investments in its IT systems. SBA's most significant IT investment during the past 5 years has been development of its Certify system, which was intended to improve small business access to SBA's contracting and assistance programs.

During our recent review, we identified a need for improved planning and performance oversight throughout this project. As a result, Certify.gov did not meet its original goal of improving SBA's small business certification process, and the \$30 million investment has not yielded the intended results.

In the future, SBA plans to migrate to another platform to address Certify's limitations. However, until SBA addresses these oversight weaknesses, identified through several investment control recommendations, there is a continued risk of repeating past project shortcomings.

SBA has begun moving to a new application platform to address Certify's weaknesses. Certify was envisioned to be the single gateway to all of SBA's contracting programs and a

vehicle to improve small business participation in federal contracts.

Certification program changes such as those mandated for the Women-Owned Small Business Program requires Certify's functionality to be expanded to address new program requirements, streamline the certification process and improve productivity.

The system was also supposed to provide management views of in-progress applications, automate repetitive tasks, and make document review straightforward to help the agency identify fraud, waste, and abuse. We plan to monitor the Certify investment to ensure necessary functionality is added and federal guidance followed for major future IT investments.

## Issue: Additional Progress Needed on Security Controls



Inspectors General are required by the Federal Information Security Modernization Act's (FISMA) to assess the effectiveness of information security programs on a maturity model spectrum and assess security capability in eight domains. The current benchmark for an effective program within the context of the maturity model is Level 4, *Managed and Measurable*.

Our most recent evaluation indicated SBA has achieved Level 4 for incident response but is at level 2 "Defined" or level 3 "Consistently Implemented" in the remaining seven areas. Consequently, SBA is at an overall level of "not effective." At the same time, however, significant progress is being made towards an "effective" level as outlined in the FISMA metrics.

### Agency Progress

SBA has made significant progress on policies to implement information security continuous monitoring activities and ensure controls are tested on a regular basis by internal and external testers. In addition, the agency has implemented encryption for data at rest and in transit and has established a policy for responding to data breaches.

However, we continue to find problems with information security continuous monitoring and data protection. These areas include establishing security baselines for systems, ensuring vulnerabilities identified are corrected promptly, and establishing metrics to document the effectiveness of data protection efforts.

SBA officials also have made significant progress in risk management by communicating agency risks to appropriate personnel and maintaining processes to identify risks that may affect the agency in the future. SBA is also working to ensure backups are completed and contingency plans are up to date.

We continue to find challenges in risk management and contingency, however. These areas include improving oversight of plans of actions and milestones, maintaining up-to-date software and hardware inventories, and ensuring security controls for agency systems and third-party systems are assessed for effectiveness. In addition, SBA has made significant improvement in access control, implementing an agency-wide policy for user access, proper

approvals for new users, and using two-factor authentication. In configuration management, SBA is using automation to ensure systems are properly configured and secured.

Challenges remain in the areas of user access configurations, applying patches in a timely manner, documenting departures from system baselines, and documenting proper permissions for new users.

## Challenge 4

# SBA Risk Management and Oversight Practices Need Improvement to Ensure the Integrity of Loan Programs

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## Why This Is a Challenge

**S**BA's Office of Credit Risk Management (OCRM) manages credit risk for a loan portfolio of more than \$744 billion. However, those loans are originated by lenders and certified development companies that have various degrees of expertise in SBA loan program requirements.

Most traditional 7(a) and 504 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 fee-based and other third-party agents to help originate, close, service, and liquidate SBA loans.

Previous OIG audits have shown that SBA did not recognize significant lender weaknesses. In response, SBA initiated actions to address identified issues with its oversight of lenders, and implemented all our audit recommendations before FY 2019. However, although SBA took action to address previous concerns about lender oversight, an OIG FY 2020 audit of SBA's oversight of high-risk lenders identified additional internal control weaknesses in lender oversight.

Consequently, we have added a new issue related to SBA's oversight of high-risk lenders. SBA has planned several actions to address recommendations made in the 2020 audit that should continue to improve SBA's oversight of lenders in the 7(a) program.

Additionally, many lenders rely on the services of fee-based and other third-party agents to help originate, close, service, and liquidate SBA loans. Previous OIG audits have shown that SBA did not effectively identify and track third-party agent involvement in its 7(a) and 504 loan portfolios. SBA has made substantial progress in identifying and tracking third-party agents.

## Issue: SBA's Oversight of High-Risk Lending Participants



The risks inherent in delegated lending require effective oversight to monitor compliance with SBA policies and procedures and take corrective actions when material noncompliance is detected. However, OIG's audit of SBA's oversight of high-risk lenders found that OCRM did not always effectively oversee high-risk lenders to identify and mitigate risks (Report 20-03, November 12, 2019).

SBA did not always conduct planned high-risk lender reviews, recommend appropriate and consistent risk mitigation actions for the deficiencies identified during the oversight reviews of high-risk lenders, or communicate loan deficiencies noted during high-risk lender reviews to SBA approval and purchase loan centers.

## Agency Progress

In FY 2020, SBA issued a final rule to implement the Small Business 7(a) Lending Oversight Reform Act of 2018. The regulations include SBA's informal enforcement actions for 7(a) lenders, authority to impose civil monetary penalties on all 7(a) lenders, and an updated definition of "credit elsewhere."

SBA also realigned the OCRM organizational structure to provide greater management depth and consistency for its review teams and added additional resources to the review teams for effective oversight.

OCRM also implemented quarterly meetings to assess high-risk lender review results and developed a communications protocol that documents deficiencies identified during loan file reviews. OCRM plans to issue updated standard operating procedures in FY 2021. The agency is also developing a database to manage the oversight of high-risk lenders that will be implemented during FY 2021.

## Issue: Increased Risk Introduced by Loan Agents



Previous OIG audits and investigations have shown SBA could not effectively identify and track loan agent involvement in its 7(a) and 504 loan portfolios and had outdated enforcement regulations. OIG investigations have also revealed a pattern of fraud by loan packagers and other fee-based agents in the 7(a) loan program, involving hundreds of millions of dollars.

Over the course of a decade, OIG investigated at least 22 cases with confirmed loan agent fraud, totaling approximately \$335 million (Report 15-16, September 25, 2015). The audit determined that loan agents were involved in approximately 15 percent of all 7(a) loans increasing the risk of default. SBA has indicated the percentage decreased to approximately 7 percent in FY 2020. Despite the prevalence of fraud in its loan portfolios, SBA's oversight of loan agents was limited.

SBA implemented a process that requires lenders to provide a loan agent disclosure form (Form 159) to SBA's fiscal-and-transfer agent for 7(a) loans. The fiscal-and-transfer agent must enter the data into a database accessible to SBA. SBA also began linking 7(a) loan Form 159 information with its loan data. In the report on SBA's loan agent oversight (Report 15-16), we identified significant issues in the data quality of Form 159. Additionally, the report found that SBA had not implemented tracking Form 159 in the 504-loan program.

## Agency Progress

In response to our report on SBA's oversight of loan agents, SBA stated that it would explore the feasibility of implementing a registration system for the 7(a) loan program (Report 15-16). SBA determined the best way to gather information on loan agents was by improving Form 159. The enhanced Form 159 was approved by the Office of Management and Budget and rolled out with official notification and lender training.

In FY 2019, SBA also implemented an effective method of disclosing and tracking loan agent involvement in the 504-loan program. SBA requires 504 lenders to electronically submit Form 159 directly into SBA's electronic lending system.

In addition, SBA has awarded a new Fiscal Transfer Agent contract. The contract requires the Fiscal Transfer Agent to develop application and follow-up controls over 7(a) lender submissions to ensure critical fields on each form are completed. The migration phase is in process, and SBA expects the enhanced controls to be fully implemented in FY 2021.

Because loan agent involvement in the 7(a) program is significant, it is important for SBA to have oversight tools in place to identify and track loan agent involvement in this sizeable program. SBA also needs to effectively mitigate the risk introduced by high-risk loan agents. OIG will continue to monitor SBA's oversight of loan agents and conduct audits and reviews as necessary.

### **Issue: Increased Risk Introduced by Lender Service Providers**



In 2019, five former officers and employees at one of the largest lender service providers were charged for their alleged roles in a 13-year conspiracy to defraud SBA in connection with programs to guarantee loans made to small businesses.

The officers allegedly fraudulently obtained guarantees for loans SBA deemed ineligible. The officers hid signs of ineligibility from the SBA by misrepresenting the use of SBA loan proceeds and unlawfully diverting previously denied loan applications into expedited approval channels. The officers originated dozens of loans, totaling more than \$10 million in disbursements, that were not eligible for SBA guarantees.

SBA has had to contend with the issue of risks introduced by lender service providers for some time. In a March 2015 audit (Report 15-06), we noted that the outsourcing of traditional lender functions to lender service providers, a type of loan agent, had significantly increased. Since then, the number of SBA-approved lender-service-provider agreements has grown significantly, reaching almost 2,900, in part because of SBA's effort to better control access to its systems by lender service providers.

SBA assigns an identifying number for all lender service providers that access SBA systems and records all SBA-approved agreements. Use of the identification number has made it possible for OCRM to develop initial metrics on provider participation in SBA's 7(a) program, but oversight is still limited. SBA's loan agent performance analysis does not combine lender service provider loan-level information to identify high-risk lender service providers.

#### **Agency Progress**

In response to our report on SBA's oversight of lender service providers, SBA implemented a method to track lender service provider involvement at the loan level. However, this information was not aggregated to evaluate performance.

In FY 2020, SBA worked with a contractor to develop performance analysis for lender



service provider portfolios to identify any high-risk lender service providers. SBA plans to complete and implement the enhancement in FY 2021.

As lender service provider involvement in the 7(a) program continues to increase, it will be especially important for SBA to evaluate lender service provider performance and effectively mitigate the risk introduced by high-risk lender service providers. OIG will continue to monitor SBA's oversight of lender service providers and conduct audits and reviews as necessary.

## Challenge 5

# SBA's Management and Monitoring of Section 8(a) Business Development Program Needs Improvement

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## Why This Is a Challenge

**S**BA'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, which means small businesses do not have to compete against 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.

## Issue: SBA Continues to Address Its Ability to Develop Firms in the 8(a) Program and Measure Results



In the past, SBA has adequately emphasized business development to enhance the ability of 8(a) firms to compete for federal contracts. SBA has made assistance more readily available to program participants by using resource partners, such as small business development centers, the SCORE Association (formerly known as the Service Corps of Retired Executives), and procurement technical assistance centers to

offer individualized development assistance.

SBA also has taken steps to ensure business opportunity specialists assess program participants' business development needs during site visits. During FY 2018, SBA implemented additional measures for business opportunity specialists to use to assess development of firms in the 8(a) mentor-protégé program.

However, despite these improvements, SBA has not fully established an IT system to perform regular performance monitoring and reporting for 8(a) participants to assure compliance with their business plans. Without an effective IT system to monitor 8(a) participant progress in meeting individualized business development goals, SBA may not be able to consistently determine whether 8(a) participants have demonstrated the ability to compete in the marketplace without 8(a) assistance.

SBA has unsuccessfully attempted to revamp its IT systems for monitoring 8(a) firms. SBA has partially implemented an IT system, Certify.SBA.gov, that was intended to be a comprehensive approach to service delivery for all of SBA's contracting programs.

However, the system in place only handles certification management and does not offer many of the key essential search, analytical, and reporting tools it was supposed to have. SBA already plans to develop a new IT system to replace Certify.SBA.gov.

### Agency Progress

SBA has decided to stop development on the current Certify.gov platform and redevelop it as an exclusive certification management system. After spending more than \$30 million, SBA's initial attempt to implement Certify faced serious developmental challenges and was scheduled to be decommissioned at the end of FY 2020.

SBA plans to develop a separate system to monitor 8(a) participants' business development outside of Certify.gov, SBA created a manual workaround for business opportunity specialists to assess the 8(a) participant's individual business development during the annual review and input results in a Microsoft Excel spreadsheet. This file is retained in the firm's Certify.gov case file, which lacks reporting functionality. Currently, SBA has no system to assist program officials in monitoring 8(a) participants' business development to assess the effectiveness of the program.

In 2019, SBA formed a team to develop a solution to help program officials monitor 8(a) participants' business development and assess the program effectiveness. The team has defined business development activities and identified performance measures to assess outcomes. The team continues to explore technology solutions to capture the business development and performance outcomes. Currently, SBA's system for monitoring 8(a) participants development on an individualized basis is limited to Excel files in the case files for the individual firm.

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



For 6 years, there was a steady decline in the number of firms participating in the 8(a) program, from about 7,000 in 2010 to about 4,900 in August 2016. 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. However, as of August 2020, SBA reports the 8(a)

program now includes only 4,486 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. At the request of SBA's former Deputy Administrator, we conducted a follow-on audit to a report issued in FY 2016 (Report 16-13) to determine whether SBA resolved eligibility concerns for the 30 sample firms in our audit. We determined that SBA resolved eligibility concerns for

20 of the 30 firms that we reviewed. We questioned the eligibility of 10 firms (Report 17-15).

### **Agency Progress**

We verified that SBA added controls to the application review process and has implemented corrective actions during FY 2019. SBA updated its 8(a) program policies and procedures to include a statement of difference in the review notes of each application when a final application decision differed from a lower level reviewer recommendation. SBA also updated its policies and procedures to require Business Opportunity Specialists to submit a request to the Internal Revenue Service for the tax transcripts to verify the 8(a) applicant's financial information.

Although SBA updated its internal policies and procedures, these are guidelines and not mandatory. SBA should finalize the corresponding regulations to require the use of tax transcripts to verify applicant financial information as a program requirement.

### **Issue: Continuing Eligibility Processes Expose the 8(a) Program to Higher Fraud Risk**



In FY 2018, we reported that SBA's oversight was insufficient to ensure that 8(a) Business Development Program participants met continuing eligibility requirements (Report 18-22). We found SBA did not consistently identify ineligible firms in the 8(a) program and did not always act to remove firms it determined were no longer eligible for the program.

In addition, SBA did not perform required continuing eligibility reviews when it received specific and credible complaints regarding firms' eligibility and did not log all complaints.

### **Agency Progress**

SBA has updated its 8(a) program policies and procedures governing the 8(a) continuing eligibility review process and evaluation standards, as well as the process for removing firms deemed ineligible for program assistance and submitted its draft revised policies and procedures for review.

SBA implemented the BD Hotline Complaints Tracker as the official system to track complaints about firms' continuing eligibility for the 8(a) program and the actions taken to address them. Since beginning to use the tracker in FY 2019, SBA has identified two firms as high risk, determined ineligible, and terminated from the program.

## Issue: SBA Dollar Threshold for Economic Disadvantage Should Be Based on Verifiable Data



The Small Business Act requires that participants be socially and economically disadvantaged. The Act defines economic disadvantage as diminished capital and credit opportunities compared to owners of similar businesses that are not disadvantaged. SBA, however, has not adequately determined what constitutes diminished capital and credit opportunities.

Section 8(a)(6)(A) of the Small Business Act states, "In determining the degree of diminished credit and capital opportunities, the Administration shall consider, but not be limited to, the assets and net worth of such socially disadvantaged individual[s]." According to SBA regulations, when considering diminished capital and credit opportunities, SBA is to review such factors as personal income, personal net worth, and the fair market value of all assets. SBA is also to compare the financial condition of the company with other small businesses in the same primary industry classification.

Although SBA does review several factors when determining economic disadvantage, it relies primarily on the net worth of the individual. Net worth by itself, however, does not show whether an individual has diminished capital and credit opportunities.

In 2020, SBA published a rule to establish economic disadvantage net worth of \$750,000 program. Before this year, SBA regulations allowed individuals with a net worth of up to \$250,000 for initial eligibility and \$750,000 to remain in the program and be classified as economically disadvantaged.

### Agency Progress

In March 2011, SBA revised its regulations and established additional standards to address the definition of "economic disadvantage" to be a net worth of less than \$250,000. In FY 2018, SBA hired a contractor to do a study to help the agency establish criteria defining economic disadvantage and set individual net worth thresholds.

The study developed three potential methodologies to set the threshold for economic disadvantage. Depending on the methodology chosen, the financial threshold ranged between \$400,000 and \$1.2 million, without adjustments for home and business equity.

The contractor's study recommended SBA use the methodology that concluded that individuals with an adjusted net worth of \$375,000 (\$1.1 million without adjustments) should be considered economically disadvantaged. However, SBA did not adopt the \$375,000 net worth standard because the agency did not consider economic disadvantage to be the deciding factor of continuing eligibility for the program.

In May 2019, SBA published a proposed rule to address increasing the economic disadvantage to adopt the \$750,000 net worth continuing eligibility standard for all economically disadvantaged determinations. SBA requested comments to the proposed rule on whether the \$375,000 or \$750,000 net worth standard should be used for the 8(a)

program. SBA also requested comments on whether SBA should decrease the economically disadvantaged Women-Owned Small Business net worth standard from \$750,000 to the lower \$375,000 net worth standard supported by the study.

SBA considered the 146 comments that supported the \$750,000 adjusted net worth standard to be a diverse set of perspectives, which represented a balance in the public's review of the final rule. However, most of the comments opposed SBA decreasing the economically disadvantaged WOSB \$750,000 adjusted net worth standard to the lower \$375,000.

SBA concluded that the \$375,000 net worth standard related to entry into the 8(a) program as opposed to participation in the free enterprise system as an economically disadvantaged business owner. In 2020, SBA published its final rule for economic disadvantage to adopt a \$750,000 net worth threshold for initial and continuing eligibility in the 8(a) program, which aligned the 8(a) net worth threshold with other SBA preference contracting programs with economic disadvantaged considerations.

Instead of adopting the \$375,000 net worth standard for establishing economic disadvantage as the study had found through empirical research, SBA relied on the \$750,000 adjusted net worth that it had established for its other preference contracting programs.

## Challenge 6

# Identification of Improper Payments in SBA's Loan Programs Remains a Challenge

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## Why This Is a Challenge

In FY 2019, the dollar amount of SBA's 7(a) loan approvals totaled \$23.6 billion. Most of these loans were made by lenders with delegated approval authority. When a loan goes into default, SBA conducts 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 review the lender's actions after payment is made. Pursuing recovery from a lender on sold loans is generally a more difficult task for SBA.

In FY 2014, OIG established a High-Risk 7(a) Loan Review Program to evaluate lender compliance with SBA requirements for high-dollar, early defaulted 7(a) loans. High-dollar, early defaulted loans are loans of \$500,000 or more that default within the first 18 months of initial disbursement. During FY 2019, OIG identified material lender noncompliance in five of the eight loans reviewed, totaling approximately \$8.7 million in questioned costs.

This year, because of OIG's priority focus on the Paycheck Protection Program, we only completed one assessment of a high-dollar, early defaulted 7 (a) loan for FY 2020. That review identified material lender noncompliance, resulting in more than \$2 million in questioned costs (Report 20-18, August 25, 2020).

Although SBA completed purchase and quality control reviews on all the loans, the agency did not identify or fully address the material deficiencies noted in the subsequent OIG review.

## Issue: Improvements Needed to Ensure High-Risk 7(a) Loan Reviews Reduce the Risk of Losses



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 the related loans.

The OIG High-Risk 7(a) Loan Review Program uses an internal scoring system to prioritize loans for review based on known risk attributes. This evaluation includes a review of high-risk loans purchased by SBA to determine whether lenders materially complied with SBA requirements and to identify suspicious activity.

Since FY 2014, we have recommended recoveries on 17 loans totaling more than \$19.3

million under this program. In addition, we identified suspicious activity on 5 loans totaling nearly \$4 million, resulting in formal referrals to our Investigations Division.

Our reviews have consistently identified issues regarding eligibility, repayment ability, size standards, franchise agreements, business valuations, appraisals, equity injection, and debt refinance. The program also identified concerns with change of ownership transactions and SBA's identification of improper payments.

### **Agency Progress**

SBA modified production standards to allow loan specialists more time to review complex early defaulted loans. In addition, the agency improved its review of loans by providing training to loan specialists and updating the loan review checklist.

In FY 2020, SBA evaluated its purchase process and quality control reviews for 7(a) guaranteed loans to determine why the loan center reviews did not identify or correct lenders' noncompliance with SBA requirements, as noted in OIG reports.



## Challenge 7

# SBA's Disaster Assistance Program Must Balance Competing Priorities to Deliver Prompt Assistance but Prevent Potential Fraud

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## Why This Is a Challenge

**T**he disaster loan program plays a vital role in the aftermath of disasters by providing long-term, low-interest loans to affected homeowners, renters, businesses of all sizes, and nonprofit organizations. SBA must continually balance the priority of quickly assisting disaster survivors in the immediate aftermath of a devastating life event against the need to ensure program integrity.

During large-scale disasters such as COVID-19, SBA must bring on new loan officers to match the volume of loan applications and prevent processing backlogs that delay the delivery of disaster assistance. To respond to the COVID-19 pandemic, SBA increased its permanent and temporary trained staff size to more than 9,000, which was more than any other previous disaster. It has been a challenge for SBA to bring on significant numbers of staff and provide them with the proper level of training.

In our September 2019 report (Report 19-23), *SBA's Audit of Desktop Loss Verification*, we found the desktop loss verification process helped SBA meet its timeliness goals for disaster applications, but controls needed strengthening to reduce the risk of fraud and ensure program integrity. SBA did not always validate the cause and extent of damages and repair and replacement costs before disbursing loan funds and relied on reports from the Federal Emergency Management Agency that did not contain pertinent information needed to validate the reported damages and losses in the initial loss verification.

Loan files also did not contain sufficient documentation to support loan-making decisions. Without adequate loss verification, loans could be made to individuals who do not qualify for the loan or do not have damages that justify the amount of the loan.

## Issue: Reserve Staff Need Training to Sustain Productivity During Mobilization



SBA has had this challenge for several years but has made progress in reducing risks. However, the magnitude of the COVID-19 pandemic required SBA to rapidly increase trained staff to historic levels. The number of personnel needed to address this pandemic was almost twice the previous historic high in numbers of total staff. And the agency had to develop the needed training to address the new criteria for COVID-19 disaster loans.

In response to Hurricanes Harvey, Irma, and Maria, SBA's Office of Disaster Assistance increased its trained staff from 800 to more than 5,000 employees in December 2017. By contrast, in response to the COVID-19 pandemic, SBA increased its permanent and

temporary staff size to more than 9,000 employees to handle the unprecedented volume of applications and prevent processing backlogs that delay the delivery of disaster assistance.

SBA outsourced EIDL processing to a subcontractor. However, the process to approve or decline COVID-19 EIDLs was left to SBA staff. Suddenly, SBA had to train both the existing staff and all the newly hired employees the new system to approve or decline loan applications.

### **Agency Progress**

Although SBA is continuing to face this challenge, it is slightly different requiring the training of staff to the new COVID-19 EIDL criteria. SBA had previously addressed OIGs recommendations and based on their progress the recommendations were closed. However, the staff training issue was still included in last year's Management Challenges report. In FY 2020, the COVID-19 pandemic reignited the need to train and mobilize the largest number of new employees ever.

In 2018, SBA published an "after action" report reviewing its successes, challenges, and action items from the response to hurricanes Harvey, Irma, and Maria. SBA then launched a cross-functional training plan development team to develop core training modules, as well as online and automated tutorials. A similar after-action report for the response to COVID-19 will help SBA to determine if employees were sufficiently trained to accurately process loans and make appropriate loan decisions.

### **Issue: Improper Payment Quality Assurance Process Needs Strengthening**



SBA received a historic number of loan applications in FY 2020. In our ongoing work, we have found a significant number of potentially fraudulent loans, which will increase the improper payment testing and put pressure on the current improper payment process.

The deadline to apply for COVID-19 EIDLs is December 31, 2020. SBA will continue to process loan applications submitted before the deadline after that date, as well as continuing to provide other disaster relief, situations that could easily result in improper payments.

In February 2020, we reported on weaknesses we found in the improper payment quality assurance process. We found that the improper payments appeal process effectively assessed improper payments, but the initial review process was inefficient.

### **Agency Progress**

SBA has acted on this new issue to reduce or eliminate the number of improper payments being made on COVID-19 loans. We will continue to monitor agency actions to ensure policies are clear and comprehensive and staff is adequately trained to effectively identify improper payments.

## Issue: Inadequate Verification of Cause and Extent of Damages



A critical part of the disaster lending process is evaluating the cause and extent of property damages, which provides SBA the information necessary to establish eligibility for disaster loan funds. In 2019, we reported on the desktop loss verification process (Report 19-23).

In the past, loss verifiers conducted on-site inspections to assess damages. But in January 2017 in response to the increased number of digital applications, SBA implemented the desktop loss verification process to expedite assistance to disaster survivors.

The desktop loss verification process uses a two-pronged approach: an initial desktop loss verification and a post desktop review. The initial desktop loss verification is used to estimate the cost of repairs. After the initial desktop loss verification, SBA requires a post-desktop review to validate the total damage estimates obtained from the initial desktop loss verification.

However, SBA did not always validate the cause and extent of damages and repair and replacement costs before disbursing loan funds. SBA relied on Federal Emergency Management Agency reports that did not contain information needed to validate damages and losses reported in the initial loss verification, and loan files did not contain sufficient documentation to support loan-making decisions.

As a result, SBA disbursed 36,869, or 50 percent, of the 73,313 loans included in our scope, totaling \$594,286,878 without validating damages and losses. We recommended SBA strengthen controls to reduce the risk of fraud and ensure program integrity for the loss verification process.

### Agency Progress

The agency has made substantial progress to strengthen controls to reduce the risk of fraud and ensure program integrity. In FY 2020, the agency updated its policies and controls to prevent loan disbursement before a post-desktop review. The agency also stopped using Federal Emergency Management Agency reports to conduct post-desktop review and confirmed all post-desktop reviews will be performed onsite.

The agency also updated its policy and now requires loss verifiers to provide sufficient documentation to support conclusions of post-desktop review. We will continue to monitor agency actions to strengthen controls to reduce the risk of fraud and ensure program integrity.

## Challenge 8

# SBA Needs Robust Grants Management Oversight

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## Why This Is a Challenge

**I**n FY 2020, SBA had \$261 million to administer grants and cooperative agreements to resource partners and other nonfederal entities for technical assistance and training programs to develop small businesses. This amount doubled in March 2020 when Congress increased the funds available to provide additional technical assistance to small businesses affected by the COVID-19 pandemic.

With recent governmentwide emphasis on grants management reform, and a priority initiative to modernize the government in the President's Management Agenda of 2018, it is SBA's responsibility to maximize the value of its grant funding to ensure its grant programs effectively and efficiently accomplish program objectives. In OIG's review of past audit findings (Report 19-02), we identified systemic issues with SBA's accuracy of grant data for both financial and performance reporting and ineffective oversight. We have continued to find grant management deficiencies in recent reviews of SBA grant programs.

## Issue: SBA's Grants Management System Needs Improvement



During FY 2020, most of SBA's technical assistance programs used the federal Procurement Request Information System Management, or PRISM, to award and report on grants. The PRISM system requires substantial manual data entry, which is prone to human errors.

In March 2018, we issued a Management Advisory memorandum (Report 18-15) on material weaknesses identified by an independent accounting firm in SBA's controls over the accuracy of data reported in USASpending.gov.

In SBA's internal A-123 review on the grant management process, SBA's internal auditors found that 100 percent of the sampled transactions included inaccuracies. These data inaccuracies inhibit policymakers' and the public's ability to effectively track federal spending. Such errors also affect the agency's ability to report complete and accurate information on time, as required by the Digital Accountability and Transparency Act of 2014.

## Agency Progress

SBA has made substantial progress to modernize its grants management system. In FY 2019, SBA approved funding totaling \$2.5 million over 5 years to implement Grantsolutions.gov.

SBA management believes the investment will help the agency

- improve funding management, awarding of grants, processing payments, and close-outs;

- enhance ability to develop accurate performance metrics reporting;
- reduce compliance violations; and
- increase auditability, accountability, and transparency.

In 2019, SBA entered into an interagency agreement with the U.S. Department of Health and Human Services to provide transition analysis, infrastructure setup, and training services to launch Grantsolutions.gov.

SBA has incrementally transitioned its grant programs to the new Grantsolution.gov system. In FY 2020, several of SBA's program offices have adopted SBA's new grants management system. For each program, officials must ensure the system is customized to meet the program's needs.

SBA has also worked to integrate the financial system with Grantsolution.gov. SBA continues to make progress implementing the system despite competing priorities in managing the CARES Act programs. SBA plans to fully implement the system for all grant programs in 2021. The full implementation of Grantsolution.gov will improve SBA's compliance, oversight, and management of its grant programs.