

U.S. SMALL BUSINESS ADMINISTRATION

OFFICE OF INSPECTOR GENERAL

SBA's Screening of 7(a) Loan Applications Under its Risk Mitigation Framework



Evaluation Report

Report 26-07

March 11, 2026



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NOTICE:

Pursuant to the James M. Inhofe National Defense Authorization Act for Fiscal Year 2023, Public Law 117-263, Section 5274, any nongovernmental organizations and business entities identified in this report have the opportunity to submit a written response for the purpose of clarifying or providing additional context as it relates to any specific reference contained herein. Comments must be submitted to AIGA@sba.gov within 30 days of the final report issuance date. We request that any comments be no longer than two pages, Section 508 compliant, and free from any proprietary or otherwise sensitive information. The comments may be appended to this report and posted on our public website.



U.S. Small Business Administration Office of Inspector General

EXECUTIVE SUMMARY

SBA's Screening of 7(a) Loan Applications Under its Risk Mitigation Framework (Report 26-07)

What OIG Reviewed

This report presents the results of our evaluation of the Small Business Administration's (SBA) screening of 7(a) loan applications under its Risk Mitigation Framework. On August 1, 2023, SBA assumed responsibility for determining applicants' eligibility via a framework that involved using technology for real time validation of applicant data. Prior to this, lenders were responsible for certifying applicant eligibility for 7(a) loans.

Using the framework, SBA screened applicants and alerted lenders to potential eligibility issues using compliance check error codes. The lender was then required to work with SBA to clear the code. If SBA verified an applicant to be eligible who was later discovered to be ineligible, SBA could not use that discovery to repair or deny the lender's guaranty purchase request.

From August 1, 2023, to December 31, 2024, SBA approved and disbursed 73,302 7(a) loans totaling about \$32 billion, using the framework to determine applicants' eligibility. Of the 73,302 loans, 9,650, totaling about \$5.9 billion, had at least one resolved error code.

Effective June 1, 2025, SBA is no longer responsible for determining applicants' eligibility and, instead, has restored this responsibility back to the lenders.

Our objective was to assess SBA's screening of 7(a) loan applications under its Risk Mitigation Framework.

What OIG Found

SBA's Risk Mitigation Framework was not sufficient to determine borrowers' eligibility

because it did not screen or fully screen for three of the six eligibility requirements. Specifically, the framework did not screen to determine whether a small business (1) was organized for profit, (2) met SBA's size requirements, or (3) was an ineligible business type.

Additionally, we reviewed 188 of the 9,650 loans that had at least one error code. We found SBA did not maintain sufficient documentation to support the reviewer's decision to clear error codes for 71 (or 38 percent) of the loans we reviewed, totaling about \$60.7 million.

As a result of SBA's incomplete screenings, there is limited assurance that borrowers met eligibility requirements for the 73,302 loans, totaling about \$32 billion in questioned costs. This includes the subset of 71 loans we identified, totaling about \$60.7 million, for which SBA did not maintain sufficient documentation to support its decision to clear the error codes, further limiting this assurance.

What OIG Recommended

We made a recommendation for SBA to flag the 73,302 loans for review at guaranty purchase to assess whether borrowers met all eligibility requirements and seek remedy for all loans deemed ineligible.

Agency Response

SBA management agreed with the recommendation, stating they will flag the 73,302 loans for review at guaranty purchase and seek recovery where appropriate and legally justified. Management's planned actions satisfy the intent of the recommendation.

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Introduction

This report presents the results of our evaluation of the Small Business Administration's (SBA) screening of 7(a) loan applications under its Risk Mitigation Framework.

Background

SBA is authorized under Section 7(a) of the Small Business Act to provide financial assistance to small businesses in the form of government-guaranteed loans. Participating lenders enter into an agreement with SBA to make loans to small businesses in accordance with SBA rules, regulations, policies, and procedures. When a 7(a) loan goes into default and the lender requests guaranty payment, SBA reviews loan documentation to determine whether the lender made, closed, serviced, and liquidated the loan in accordance with SBA program requirements and prudent lending standards.

On August 1, 2023, SBA assumed responsibility for determining whether applicants were eligible for 7(a) loans via its Risk Mitigation Framework, which included using technology to validate applicant data in real time. Prior to implementing the framework, lenders were responsible for certifying applicants' eligibility for loans and maintaining documentation to support eligibility determinations. From August 1, 2023, to December 31, 2024, SBA approved and disbursed 73,302 7(a) loans, totaling about \$32 billion, using the framework to determine applicants' eligibility. Of the 73,302 7(a) loans, 9,650, totaling about \$5.9 billion, had at least one resolved compliance error check code.

Risk Mitigation Framework

SBA's Risk Mitigation Framework for determining eligibility used a network of third-party databases and solutions to validate applicant data. The framework was intended to check whether applicants met the following six eligibility requirements according to SBA's policy:

- An operating business,
- Organized for profit,
- Located in the U.S.,
- Small under SBA size standards,
- Not an ineligible business type, and
- Met ownership requirements for non-U.S. citizens who are lawful permanent residents.

Applicants certified that they met all eligibility requirements by signing an application form. Lenders then digitally submitted loan application requests to SBA via its electronic loan application system (E-Tran), which used the framework to validate applicants' eligibility. Applicants' unique identifiers combined with the Application Program Interface was intended to enable SBA to validate identification information, financial data, and eligibility criteria. The framework relied on multiple sources of information, including Treasury's Do Not Pay list, an online data compilation and analytics provider's evaluation of businesses and principals, and the business' credit.

Additionally, the framework included compliance checks, which alerted lenders to other issues such as bankruptcy, affiliation, deceased applicants, inactive businesses, and citizenship status. If a potential issue was identified for an applicant, the framework returned a compliance check error code and lenders were able to review the code in E-Tran, which included additional details. The lender was then required to work with SBA to clear the code.

SBA's guidance to lenders established instructions and acceptable support documentation that could resolve error codes. Lenders were responsible for uploading the supporting documentation into E-Tran and notifying SBA via email that the documents required review. After SBA reviewed and cleared the error code, the agency issued a loan number signaling to the lender that it could continue processing the application. In accordance with SBA's policy,¹ if SBA verified an applicant's eligibility using the framework and later discovered the applicant to be ineligible, it could not use that discovery to deny or repair the guaranty purchase requested by the lender.

Effective June 1, 2025, SBA was no longer responsible for determining applicant eligibility and, instead, restored this responsibility back to the lenders.²

¹ Standard Operating Procedure 50 10 7.1, *Lender and Development Company Loan Programs*, Section A, Chapter 1, November 15, 2023.

² SBA Information Notice 5000-866746, *Issuance of SOP 50 10 8*, April 22, 2025.

Objective

Our objective was to assess SBA's screening of 7(a) loan applications under its Risk Mitigation Framework.

Results

SBA used its Risk Mitigation Framework to validate borrower eligibility for 73,302 7(a) loans approved and disbursed from August 1, 2023, to December 31, 2024. However, the framework was not sufficient to determine whether borrowers met all eligibility requirements because it did not screen or fully screen for three of the six eligibility requirements. Additionally, SBA did not always maintain sufficient information in the loan files to support the reviewer's decision to clear the compliance check error code.

As a result of the framework's incomplete screenings, SBA had limited assurance that borrowers met eligibility requirements for the 73,302 loans, totaling about \$32 billion. This includes the subset of 71 loans we identified, totaling about \$60.7 million, for which SBA did not maintain sufficient documentation to support its decision to clear the error codes.

Finding 1: SBA's Risk Mitigation Framework was not Sufficient to Validate Whether Borrowers met all 7(a) Loan Eligibility Requirements

According to SBA's policy,³ determining applicant eligibility for an SBA guaranteed loan was one of the most critical steps in the lending process. Due to the importance of this step, lessons learned from the Paycheck Protection Program, and SBA's need to control both speed and certainty, SBA made the final decision regarding applicants' eligibility using its Risk Mitigation Framework (see the Background section).

We found SBA's Risk Mitigation Framework did not screen to determine whether a small business was organized for profit or whether the business met SBA's size requirements for the business's primary industry. Additionally, the framework did not fully screen to determine whether an applicant was an ineligible business as it only screened for five of the 19 ineligible business types — namely, businesses with marijuana sales, loan packagers, entities with

³ SOP 50 10 7.1, *Lender and Development Company Loan Programs*, Section A, Chapter 1, November 15, 2023.

associates that have a criminal history, entities with a prior loss to the government, and entities with certain Small Business Investment Company financing.⁴

SBA management stated the framework did not screen or fully screen for three of the six eligibility requirements because the agency did not have all the data available electronically to determine whether an applicant was organized for profit and an eligible business type or conduct a size standard analysis. Further, they relied on oversight activities that occur after the loan is made, such as random improper payment reviews, guaranty purchase reviews, or Office of Credit Risk Management reviews to validate eligibility. Management also stated they relied on the requirement that lenders must not knowingly submit an ineligible application.

During our review, SBA updated its eligibility verification policy and effective June 1, 2025, the agency is no longer responsible for determining applicant eligibility. Instead, this responsibility has been restored back to the lenders. Based on the deficiencies we identified regarding SBA's use of the Risk Mitigation Framework to determine applicant eligibility, we believe SBA's action to restore this responsibility back to the lenders could mitigate the risk of ineligible applicants being approved for 7(a) loans and potential financial losses. Further, SBA's action aligns with lenders' responsibility to comply with customer identification program regulations to verify the identities of individuals associated with loan applications. As a result, we are not making any recommendations regarding SBA's Risk Mitigation Framework.

However, because the Risk Mitigation Framework did not screen for all eligibility requirements, SBA had limited assurance that borrowers met eligibility requirements for the 73,302 7(a) loans, totaling about \$32 billion in questioned costs, exposing the program to potential improper payments and financial loss (see Appendix 2).

Finding 2: SBA's Reviews to Resolve Compliance Check Error Codes Were not Always Adequate to Ensure Borrowers met Eligibility Requirements

SBA did not always maintain sufficient documentation to support its decision to clear compliance check error codes and deem borrowers eligible for 7(a) loans. From August 1, 2023, to December 31, 2024, there were 9,650 7(a) loans, totaling about \$5.9 billion, with resolved compliance check error codes. We reviewed 188 of these loan files and found that SBA appropriately resolved error codes for 117 loans but inappropriately cleared codes for 71 (or 38 percent),

⁴ Standard Operating Procedure 50 10 7.1, *Lender and Development Company Loan Programs*, Section A, Chapter 1, November 15, 2023, list all of the ineligible business types.

totaling about \$60.7 million, as it did not maintain sufficient documentation in the loan file to support the reviewer’s decision to clear the code.

Of the 71 loans, 62 (or 87 percent) had an 803 compliance check error code (Additional Business Affiliation), which was the most common error code assigned during our scope period. The remaining nine loans had varied codes. See Table 1 for the list of error codes for the 71 loans.

Table 1: Compliance Check Error Code for Sample Loans

Compliance Check Error Code	Error Code Description	No. of Error Codes*
803	Additional Business Affiliation	62
807	Mismatch of TIN	4
808	Entity Mismatch	2
809	Marijuana Business	3
813	Citizenship	1
819	TOP Debt Check	2
820	TOP CAIVRS	2
825	Potential Active Indictment	1
Total		77

* There are more than 71 compliance check error codes because some loans had multiple error codes.
Source: SBA OIG analysis of 7(a) loan files.

To resolve the additional business affiliation code, loan applicants and their affiliates must be small under SBA size standards to qualify for a 7(a) loan. For affiliation, SBA must validate a lender’s analysis based on applicant ownership, ownership percentage, and primary industry. In determining size, applicants can meet the standard using annual receipts or number of employees, or tangible net worth and average net income. We reviewed the 62 loans that had a cleared 803 compliance check error code, but the files did not include source documentation to support the affiliation or size analysis. Specifically:

- Twenty-two loan files with matters related to ownership percentage did not have sufficient supporting documentation that validated the percentage. This is important because, for example, if the applicant owns more than 50 percent of another business, that other entity is considered an affiliate and must be included in the lender's analysis.
- Sixteen loan files did not have supporting documentation that could validate size standard calculations for the applicant. For example, if annual receipts were identified in a lender's analysis, there was no documentation such as tax returns to validate the analysis.
- Thirteen loan files did not have sufficient supporting documentation pertaining to sold or inactive businesses. For example, if an applicant sold a potential affiliate, the loan file did not have documentation such as a sales contract to support the lender's analysis.
- Eleven loan files related to other matters, such as verifying business industry and name, also did not have sufficient supporting documentation necessary for SBA to validate the lender's analysis.

The Standards for Internal Controls in the Federal Government require management to provide supporting documentation for their decisions — including how decisions are made — and underscore the importance of documentation and records being properly managed, maintained, and available.⁵ SBA was required to obtain sufficient documentation to clear compliance check error codes based on instructions specific for each code. For example, instructions for compliance check error code 803 required the lender to provide a copy of their credit memorandum or other documentation demonstrating their affiliate analysis of the applicant and impact on loan eligibility.

However, while SBA guidance referenced documentation that could be used to resolve compliance check error codes and required reviewers to support their decisions, it did not require the reviewer to obtain the underlying supporting documentation. For example, SBA relied solely on the lender credit memorandum and did not always obtain source documentation to support the lender's analysis. Loan specialist reviewers only questioned the credit memorandum and requested additional information when an issue was identified, such as details about an affiliation document in the loan file that did not align with the lender's credit memorandum. Although the credit memorandum is listed as acceptable support, on its own it is not sufficient to validate an applicant's information because it does not include underlying source documentation used to develop the credit memorandum.

⁵ GAO-14-704G, *Standards for Internal Controls in the Federal Government*, September 2014.

Because SBA also did not obtain sufficient supporting documentation to clear the error codes for the subset of 71 of 188 loans reviewed (or 38 percent), totaling about \$60.7 million, the agency's assurance that applicants met eligibility requirements was further limited.

During discussions, SBA officials indicated it was not feasible for SBA to review all 73,302 loans awarded using the Risk Mitigation Framework. Rather, they stated they would flag all the loans and seek remedy on all defaulted loans deemed ineligible, in which the lender knew of the ineligibility.

Recommendation

To ensure 7(a) loan eligibility requirements were met, we recommend the Administrator direct the Associate Administrator for the Office of Capital Access to:

Recommendation 1: Flag the 73,302 7(a) loans for review at guaranty purchase to assess whether borrowers met all eligibility requirements and seek remedy for all loans deemed ineligible.

Evaluation of Agency Response

SBA management provided formal comments on the draft report, which we considered when preparing this final report. Management agreed with the recommendation and their planned actions satisfy the intent. See Appendix 3 for management's comments in their entirety.

Summary of Actions Necessary to Close the Recommendation

The following section summarizes the status of our recommendation and the actions necessary to close it.

Recommendation 1

To ensure 7(a) loan eligibility requirements were met, we recommend the Administrator direct the Associate Administrator for the Office of Capital Access to flag the 73,302 7(a) loans for review at guaranty purchase to assess whether borrowers met all eligibility requirements and seek remedy for all loans deemed ineligible.

Status: Resolved

SBA management agreed with this recommendation, stating they will flag 73,302 loans in the Centralized Loan Chron System for review at the time of guaranty purchase and seek recovery where appropriate and legally justified. In subsequent correspondence, management stated they plan to implement the corrective action by February 17, 2027.

This recommendation will be closed when management provides (1) evidence that they flagged the 73,302 7(a) loans for review at guaranty purchase to seek recovery where appropriate and legally justified; and (2) a summary of results for all reviews completed as of the date they request recommendation closure.

Appendix 1: Scope and Methodology

This report presents the results of our evaluation of the Small Business Administration's (SBA) screening of 7(a) loan applications under its Risk Mitigation Framework. Our objective was to assess SBA's screening of 7(a) loan applications under this framework. Our scope covered 7(a) loans approved and disbursed from August 1, 2023, to December 31, 2024, for which SBA used the framework to determine applicants' eligibility.

To answer our objective, we reviewed regulations, procedures, and guidance related to 7(a) loan eligibility and the Risk Mitigation Framework. We interviewed SBA officials from various offices in the Office of Capital Access, including the Office of Performance Systems Management, and the Office of Financial Program Operations to gain an understanding of the framework. In addition, we analyzed data from SBA's electronic loan application system (E-Tran) to identify approved and disbursed 7(a) loans with compliance check error codes.

We randomly selected 385 of 9,650 7(a) loans with resolved compliance check error codes for review to assess whether SBA resolved the codes appropriately. However, due to our findings that (1) the framework did not screen or fully screen for three of the six eligibility requirements and (2) 38 percent (71 of 188) of the loan files reviewed did not have sufficient documentation to support SBA's decision to clear the error codes, we stopped our loan file review at 188 of 385. Further, during our evaluation, SBA updated its policy and restored the responsibility of determining applicant eligibility back to the lender.

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

Use of Computer-Processed Data

We relied on data from E-Tran to analyze loans from the scope period. We performed limited testing on data extracts by comparing information in the data extracts to SBA's Loan Program Performance website. In addition, we performed data reliability testing on the data extracts for completeness. Further, we reviewed data reliability assessments from a prior SBA Office of

Inspector General (OIG) inspection that used E-Tran data. As a result, we believe the data used in this report is sufficiently reliable to support our report conclusions.

Prior Audit Coverage

The OIG did not identify any prior audits or reviews related to the objective of this evaluation.

Appendix 2: Monetary Impact

Monetary Impact identified in this report is categorized as questioned costs. Questioned costs are expenses not supported by adequate documentation at the time of the audit, or which otherwise do not comply with legal, regulatory, or contractual requirements.

Table 3: Schedule of Monetary Impact (Questioned Costs)

Description	Amount (Dollars)	Explanation
Unsupported Costs	\$32,014,783,042	SBA determined applicant eligibility for 73,302 7(a) loans using the Risk Mitigation Framework. However, the framework was not sufficient to determine whether borrowers met all eligibility requirements because it did not screen or fully screen for three of the six eligibility requirements in accordance with SBA's Standard Operating Procedure 50 10 7.1.
Total	\$32,014,783,042	

Source: SBA OIG analysis.

Appendix 3: Agency Response

Small Business Administration
Response to the Evaluation Report



U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, DC 20416

To: William Kirk
Inspector General
U.S. Small Business Administration

From: Jihoon Kim, Director, Office of Financial Program Operations, OCA

JI KIM
Digitally signed by
JI KIM
Date: 2026.02.19
10:30:29 -05'00'

Date: February 12, 2026

Subject: Response to OIG Draft Report – SBA’s Screening of 7(a) Loan Applications
Under its Risk Mitigation Framework (Project 25002)

Background: On August 1, 2023, SBA assumed responsibility for determining whether applicants were eligible for 7(a) loans via its Risk Mitigation Framework, which included using technology to validate applicant data in real time. Prior to implementing the framework, lenders were responsible for certifying applicants’ eligibility for loans and maintaining documentation to support eligibility determinations.

SBA used its Risk Mitigation Framework to validate borrower eligibility for 73,302 7(a) loans approved and disbursed from August 1, 2023, to December 31, 2024.

Recommendation 1: Flag the 73,302 7(a) loans for review at guaranty purchase to assess whether borrowers met all eligibility requirements and seek remedy for all loans deemed ineligible.

SBA Response: SBA agrees with Recommendation 1. SBA will flag 73,302 loans in the Centralized Loan Chron System (CLSC) for review at the time of guaranty purchase and will seek recovery where appropriate and legally justified.