EVALUATION REPORT

SBA's FY 2018 Compliance With the Improper Payments Elimination and Recovery Act of 2010

MAY 23, 2019

REPORT NUMBER 19-13

EXECUTIVE SUMMARY

SBA'S FY 2018 COMPLIANCE WITH THE IMPROPER PAYMENTS ELIMINATION AND RECOVERY ACT

Report Number 19-13

May 23, 2019

What OIG Reviewed

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

Our objectives were to (1) determine whether SBA is compliant with IPERA using guidelines outlined in the Office of Management and Budget (OMB) Memorandum M-18-20, Appendix C to OMB Circular No. A-123, Requirements for Payment Integrity Improvement, and (2) assess progress SBA made in remediating improper payment–related recommendations. We performed limited procedures and consulted with a statistician to evaluate the accuracy and completeness of the program-specific improper payment rates.

What OIG Found

Our overall qualitative review of Agency efforts to prevent and reduce improper payments showed that SBA continued to maintain controls to prevent and reduce improper payments, as summarized in the following table.

OIG IPERA Qualitative Assessment for FY 2018 by Program or Activity

SBA Program or Activity	Status
Section 7(a) Loan Guaranty Approvals	Substantial Progress
Section 504 CDC Loan Guaranty Approvals	Substantial Progress
Section 7(a) Loan Guaranty Purchases	Implemented
Disaster Direct Loan Disbursements	Progress
Disbursements for Goods and Services	Implemented

Further, SBA was generally compliant in meeting the minimum requirements in accordance with OMB guidance. In accordance with IPERA, SBA published and posted an agency financial report (AFR) on its website, conducted program-specific risk assessments, and published improper payment estimates for all programs and activities identified as susceptible to significant improper payments.

We noted that for the disbursements for goods and services area, this was the second consecutive year that SBA reduced its rate of improper payments and had improper payment amounts that were less than the statutory threshold of $10 million. As a result, on February 19, 2019, SBA submitted a memo to OMB requesting relief from reporting improper payments for disbursements for goods and services.

SBA also published extracts from the applicable programmatic corrective action plans in the AFR for three of five areas tested for fiscal year (FY) 2018 reporting and published and met the annual reduction target for three of the applicable five areas tested, including the disaster loan program. However, we noted that SBA eased controls for the disaster program regarding the requirement for justifications to exceed the maximum acceptable fixed debt, which was the primary cause for improper payments in FY 2018.

We concluded that SBA was not compliant with IPERA because the actual improper payment rate for 7(a) and 504 CDC loan guaranty approvals exceeded the annual reduction target for FY 2018.

OIG Recommendations

We made two recommendations to address 7(a) and 504 CDC loan guaranty approvals not meeting their annual reduction targets.

Agency Response

SBA management agreed with the findings and recommendations of this report. Within 90 days of this report, the Agency plans to take action to address the recommendations. For recommendations 1 and 2, SBA intends to submit a plan to the Senate Committee on Homeland Security and Governmental Affairs, the House Committee on Oversight and Reform, and OMB describing the actions that the Agency will take to address its noncompliance with IPERA regarding the 7(a) and 504 CDC loan guaranty approvals programs.

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

Final Report Transmittal
Report Number 19-13

DATE: May 23, 2019

TO: Christopher Pilkerton
Acting Administrator and General Counsel

FROM: Hannibal "Mike" Ware
Inspector General

SUBJECT: SBA's FY 2018 Compliance With the Improper Payments Elimination and Recovery Act of 2010

Attached for your review is the evaluation report on the Small Business Administration's (SBA's) fiscal year (FY) 2018 compliance with the Improper Payments Elimination and Recovery Act of 2010 (IPERA). Our objectives were to (1) determine whether SBA is compliant with IPERA using guidelines outlined in the Office of Management and Budget (OMB) Memorandum M-18-20, Appendix C to OMB Circular No. A-123, Requirements for Payment Integrity Improvement, and (2) assess progress SBA made in remediating improper payment–related recommendations.

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

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

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

cc: Dorrice Roth, Acting Chief Financial Officer and Associate Administrator for Performance Management
William Manger, Associate Administrator for Capital Access
James Rivera, Associate Administrator for Disaster Assistance
Martin Conrey, Attorney Advisor, Legislation and Appropriations
LaNae Twite, Director, Office of Internal Control
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Introduction

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

Background

In accordance with the Office of Management and Budget (OMB) guidance, each Office of Inspector General (OIG) should review its agency's improper payment reporting in the annual performance and accountability report (PAR) or agency financial report (AFR), and accompanying materials. OIG should complete its review and determination and submit its final report by May 15 of the following year.[2] OMB requested each OIG to assess the following:

- the accuracy and completeness of agency reporting
- agency's performance in reducing and recapturing improper payments
- whether agency corrective action plans are focused on the true root cause, are actually reducing improper payments, and are implemented effectively
- agency efforts to prevent and reduce improper payments

To perform our qualitative assessment of the areas listed above, the Small Business Administration (SBA) OIG categorically developed the following ratings:

- implemented because no further improvements were noted for this reporting period
- substantial progress due to a change in the improper payments rate, implementation of improved controls, and closed recommendations
- progress because SBA either reduced the improper payments rate since last year, improved its controls, or closed recommendations
- improvement needed because controls were not fully implemented

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

- published a PAR or AFR for the most recent fiscal year and posted that report and any accompanying materials required by OMB on the agency website

[1] IPIA was amended by IPERA and the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA).
[2] OMB issued Memorandum M-18-20, Appendix C to OMB Circular No. A-123, Requirements for Payment Integrity Improvement, to create a more unified, comprehensive, and less cumbersome set of requirements (June 26, 2018).

- conducted a program-specific risk assessment for each applicable program or activity that conforms with Section 3321 Note of Title 31 U.S.C. (if required)
- published improper payment estimates for all programs and activities identified as susceptible to significant improper payments under its risk assessment (if required)
- published programmatic corrective action plans in the PAR or AFR (if required)
- published and met the annual reduction targets for each program assessed to be at risk and measured for improper payments (if required and applicable)
- reported a gross improper payment rate of less than 10 percent for each program and activity for which an improper payment estimate was obtained and published in the PAR or AFR

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

Prior Work

Prior OIG audits have identified 7(a) loans that were ineligible, lacked repayment ability, or were not properly closed, resulting in improper payments. Also, disaster loans were vulnerable to improper payments, fraud, and default because loan transactions were often expedited to provide quick relief to disaster survivors.

OIG's fiscal year (FY) 2017 IPERA review found that SBA continued to maintain adequate controls to prevent and reduce improper payments. Further, SBA was generally compliant in meeting the minimum requirements in accordance with OMB guidance. In accordance with IPERA, SBA published and posted an AFR on its website, conducted program-specific risk assessments, and published improper payment estimates for all programs and activities identified as susceptible to significant improper payments. SBA also published extracts from the applicable programmatic corrective action plans in the AFR for three of five areas tested for FY 2017 reporting, and it met the annual reduction target for three of the applicable five areas tested. However, SBA was not compliant with IPERA reporting requirements because disbursements for disaster direct loans had an improper payment rate that exceeded the 10 percent threshold. SBA's improper payment rate for disaster direct loan disbursements more than doubled, from 5.32 percent in FY 2016 to 13.65 percent in FY 2017. SBA management attributed the increase in the disaster improper payment rate to SBA loan officers not providing justifications when they approved loans exceeding SBA's guidelines for repayment ability, documenting insurance coverage, or properly determining eligible loan amounts as a result of insurance or other payments received by the borrower related to the disaster. Also, 7(a) loan guaranty purchases and disbursements for disaster direct loans did not meet their annual reduction target.

Objectives

Our objectives were to (1) determine whether SBA is compliant with IPERA using guidelines outlined in the Office of Management and Budget (OMB) Memorandum M-18-20, Appendix C to

OMB Circular No. A-123, Requirements for Payment Integrity Improvement, and (2) assess progress SBA made in remediating improper payment–related recommendations. More specifically, we assessed the status of OIG's open prior year audit recommendations, which focused on the accuracy and completeness of SBA's reporting, and performance in reducing and recapturing improper payments.

Results

We have divided our review into five sections: one for each program or activity that has been identified as susceptible to improper payments. While SBA continued to strengthen its controls over preventing and reducing improper payments for FY 2018, we determined that two of five areas did not meet the minimum reporting requirements for IPERA compliance. Specifically, 7(a) and 504 CDC loan guaranty approvals were not compliant because the actual improper payment rate exceeded the planned reduction target for FY 2018 (see table 1).

Table 1. Summary of SBA's IPERA Compliance

	Section 7(a) Loan Guaranty Approvals	Section 504 CDC Loan Guaranty Approvals	Section 7(a) Loan Guaranty Purchases	Disaster Direct Loan Program	Disbursements for Goods and Services
Posted materials	Compliant	Compliant	Compliant	Compliant	Compliant
Assessed risk*	Compliant	Compliant	Compliant	Compliant	Compliant
Published estimates for susceptible programs	Compliant	Compliant	Compliant	Compliant	Compliant
Published programmatic corrective action plans	Compliant	Compliant	Compliant	Compliant	Compliant
Published and met annual reduction target	**Not compliant**	**Not compliant**	Compliant	Compliant	Compliant
Reported rate of less than 10 percent	Compliant	Compliant	Compliant	Compliant	Compliant
Overall FY 2018 results	**Not compliant**	**Not compliant**	Compliant	Compliant	Compliant

* All reporting segments have been deemed as susceptible to significant improper payments and are already reporting an estimate. Therefore, no risk assessment is required in accordance with OMB Memorandum M-18-20.

Section 1: Section 7(a) Loan Guaranty Approvals

The Agency's largest lending program, the 7(a) Loan Program, is SBA's principal vehicle for providing small businesses with access to credit that cannot be obtained elsewhere. This program relies on numerous outside parties (e.g., borrowers, loan agents, and lenders) to complete loan transactions, with about 80 percent of the loans being made by lenders to whom SBA has delegated loan-making authority. In FY 2018, SBA guaranteed approximately $25.4 billion in 7(a) loan approvals.

OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate for 7(a) loan guaranty approvals increased from 1.29 percent ($233.9 million) in FY 2017 to 2.77 percent ($519.4 million) in FY 2018. SBA determined that the most prevalent root cause for 7(a) loan approval improper payments stemmed from delegated lenders' failure to authenticate borrowers' eligibility at origination. As a means to reduce the occurrence of future improper payments, SBA formalized a corrective action plan that includes collaboration between SBA offices to monitor lender deficiencies and training to both SBA personnel and lenders.

OIG's assessment included reviewing three 7(a) loan guaranty approvals from SBA's sample, analyzing SBA's internal process, and interviewing SBA officials involved in the 7(a) loan guaranty approval IPERA process. Based on our limited assessment, we determined that SBA's internal process includes key areas for review to identify improper payments. We also found that SBA followed its internal process and took corrective actions to resolve identified improper payments.

For FY 2017, we rated the Agency as "Substantial Progress" for accuracy and completeness of Agency reporting. For FY 2018, we upgraded the rating to "Implemented" because we did not identify any discrepancies in SBA's reporting. Additionally, we determined SBA properly followed its internal controls. Also, the Agency appropriately disclosed that it does not perform payment recapture audits because such audits are not cost effective.

We reduced our rating for the quality of corrective action plans from "Implemented" to "Substantial Progress" because the improper payment rate increased from 1.29 percent in FY 2017 to 2.77 percent in FY 2018. However, we noted that SBA had a corrective action plan in place and took corrective actions, such as obtaining additional documentation and reducing the guaranty, training, and collaborating with the Office of Credit Risk Management to address root causes of improper payments. Based on our overall assessment of Agency efforts, we maintained the overall rating of "Substantial Progress" for FY 2018. Table 2 summarizes OIG's evaluation of Agency efforts.

Table 2. OIG's Evaluation of Agency Efforts

OMB Criteria	Status at End of 2018
Overall assessment of Agency efforts	Substantial Progress
Accuracy & completeness of Agency reporting	Implemented
Performance in reducing/recapturing improper payments	N/A*
Quality of corrective action plans	Substantial Progress

* SBA determined that 7(a) loan guaranty approvals are not subject to recapture audits because no payment is made at the time of approval.

AFR Review

Our review of the AFR found that SBA was compliant with five of six IPERA reporting requirements. The improper payment rate was below the statutory threshold of 10 percent; however, SBA did not meet its planned reduction target of 1.19 percent. The actual improper payment rate was 2.77 percent. SBA is required to establish and meet an annual reduction target for each program assessed to be at risk and estimated for improper payments. OMB also requires agencies that are not compliant for 1 fiscal year to submit a plan to Congress describing the actions it will take to become compliant. Table 3 summarizes OIG's review of the AFR.

Table 3. OIG's Review of the AFR

OMB Reporting Requirement	Status at End of 2018
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Not Compliant
Reported rate of less than 10 percent	Compliant

Recommendation

We recommend that the Administrator require the Director for the Office of Financial Program Operations to

1. Submit to the Senate Committee on Homeland Security and Governmental Affairs, the House Committee on Oversight and Reform, and OMB, within 90 days of this report, a plan for the 7(a) loan guaranty approvals program that includes the following:

   (a) measurable milestones for becoming compliant with IPERA,
   (b) designation of an accountable senior Agency official, and
   (c) the establishment of an accountability mechanism, describing the actions the Agency will take to become compliant.

Analysis of Agency Response

SBA management provided formal comments that are included in their entirety in Appendix III. SBA management agreed with our recommendations, and its planned actions resolve both of our recommendations. SBA management asserted that they are committed to reducing the dollar amount of improper payments, ensuring program integrity, and continuing to implement effective risk management procedures.

Summary of Action Necessary to Close the Recommendation

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

Section 2: Section 504 CDC Loan Guaranty Approvals

SBA's 504 Loan Program provides small businesses with long-term, fixed-rate financing to purchase land, buildings, machinery, and other fixed assets. Economic development organizations, approved by SBA, are known as certified development companies (CDCs). CDCs package, close, and service these loans, which are funded through a variety of private sector lenders, proceeds from selling SBA-guaranteed debentures, and borrower equity investment. Of the total project costs, a third-party lender provides at least 50 percent of the financing, the CDC provides up to 40 percent of the financing through a 100 percent SBA-guaranteed debenture, and the applicant provides at least 10 percent of the financing. In FY 2018, SBA guaranteed approximately $5 billion in 504 loan approvals.

OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate for 504 CDC loan guaranty approvals increased from 1.20 percent ($59.2 million) in FY 2017 to 2.58 percent ($118.1 million) in FY 2018. SBA determined that the most prevalent root cause for improper payments in FY 2018 was due to the CDC's failure to authenticate borrowers' eligibility at origination. As a means to reduce the occurrence of future improper payments, SBA formalized a corrective action plan that includes collaboration between SBA offices to monitor lender deficiencies and training to both SBA personnel and lenders to ensure appropriate documentation is obtained.

Our assessment included reviewing three 504 CDC loan guaranty approvals from SBA's sample, analyzing SBA's internal process, and interviewing SBA officials involved in the 504 CDC loan guaranty approval process. Based on our limited assessment, we determined that SBA's internal process includes key areas to identify improper payments. We also found SBA followed its internal process and took corrective actions to resolve identified improper payments.

For FY 2018, we maintained the rating of "Implemented" for accuracy and completeness of Agency reporting because we did not identify any discrepancies in SBA's reporting. Additionally, we determined that SBA properly followed its internal controls related to improper payments. Also, the Agency appropriately disclosed that it does not perform payment recapture audits because such audits are not cost effective.

We rated the quality of corrective action plans as "Substantial Progress." Although SBA had a corrective action plan in place and took adequate corrective actions to address the root causes of improper payments, the rate increased from 1.20 percent in FY 2017 to 2.58 percent in FY 2018.[3] Based on our overall assessment of Agency efforts, we reduced the overall rating to "Substantial Progress" for FY 2018. Table 4 summarizes OIG's evaluation of Agency efforts.

Table 4. OIG's Evaluation of Agency Efforts

OMB Criteria	Status at End of 2018
Overall assessment of Agency efforts	Substantial Progress
Accuracy & completeness of Agency reporting	Implemented
Performance in reducing/recapturing improper payments	N/A*
Quality of corrective action plans	Substantial Progress

* SBA has determined that the 504 Loan Program is not subject to recapture audits because no payment is made at the time of approval.

[3] We did not rate this element in FY 2017 because SBA's improper payments did not meet the reporting threshold. Therefore, it was not required to implement a corrective action plan.

AFR Review

Our review of the AFR found that SBA was compliant with five of six IPERA reporting requirements. The rate was below the statutory threshold of 10 percent; however, SBA did not meet its annual reduction target of 1.10 percent. The actual improper payment rate was 2.58 percent. SBA is required to establish and meet an annual reduction target for each program assessed to be at risk and estimated for improper payments. OMB also requires agencies that are not compliant for 1 fiscal year to submit a plan to Congress describing the actions it will take to become compliant. Table 5 summarizes OIG's review of the AFR.

Table 5. OIG's Review of the AFR

OMB Reporting Requirement	Status at End of 2018
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Not Compliant
Reported rate of less than 10 percent	Compliant

Recommendation

We recommend that the Administrator require the Director for the Office of Financial Program Operations to

2. Submit to the Senate Committee on Homeland Security and Governmental Affairs, the House Committee on Oversight and Reform, and OMB, within 90 days of this report, a plan for the 504 CDC loan guaranty approvals program that includes the following:

    (a) measurable milestones for becoming compliant with IPERA,
    (b) designation of an accountable senior Agency official, and
    (c) the establishment of an accountability mechanism, describing the actions the Agency will take to become compliant.

Summary of Action Necessary to Close the Recommendation

Recommendation 2: Resolved. SBA concurred that its 504 CDC guaranty loan approvals program failed to meet its annual reduction target for 1 year and is subject to the requirements outlined in the recommendation. The Office of Financial Program Operations management stated it will comply within 90 days of the date this report is published. This recommendation can be closed upon SBA providing evidence supporting that it submitted to congressional committees and OMB a plan outlining how it will become compliant with IPERA.

Section 3: Section 7(a) Loan Guaranty Purchases

Under the 7(a) Loan Program, SBA guarantees up to 90 percent of the principal amount of loans made by banks and other lending institutions to small businesses not able to obtain credit elsewhere. When a loan goes into default, SBA reviews the lender's actions on the loan to determine whether it is appropriate to pay the lender the guaranty, which SBA refers to as a "guaranty purchase." Under its regulations, SBA is released from liability on the guaranty, in whole or in part, within SBA's exclusive discretion, if the lender fails to comply materially with any SBA loan program requirement or does not prudently make, close, service, or liquidate the loan. The guaranty purchase review is SBA's primary control for ensuring lender compliance and preventing improper payments. In FY 2018, SBA purchased approximately $771 million in 7(a) loan guaranties.

OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate for 7(a) loan guaranty purchases decreased from 4.32 percent ($28.4 million) in FY 2017 to 3.22 percent ($22.2 million) in FY 2018. In its FY 2018 AFR, SBA stated that the root cause for the identified improper payments was new center staff making administrative and process errors. As a means to reduce the occurrence of future improper payments, SBA formalized a corrective action plan that includes internal training and recovering unjustified expenses.

In FY 2017, based on a prior OIG audit report, we determined that opportunities existed for SBA to improve its improper payment review process to ensure they accurately identified improper payments. The recommendations from the prior report were to (1) conduct an assessment of the improper payment process to improve improper payment identification, (2) revise internal center guidance to ensure that critical lender calculations were verified and/or recalculated, and (3) revise internal center guidance to ensure the guides were consistent with the appropriate standard operating procedures. As of December 2018, SBA implemented, and we approved, the corrective actions for these three recommendations.

OIG's assessment of the Agency's FY 2018 efforts included reviewing four 7(a) loan guaranty purchases from SBA's improper payment sample, analyzing SBA's internal process, and interviewing SBA officials involved in the 7(a) loan guaranty purchase IPERA process. Based on our limited assessment, we determined that SBA's internal process included key areas to identify improper payments. We also found that SBA followed its internal process and took corrective actions to resolve identified improper payments.

For FY 2017, we rated the Agency as "Progress" for accuracy and completeness of Agency reporting due to the three open recommendations to improve the improper payment review process. However, SBA took, and OIG approved, corrective actions to address the related recommendations. For FY 2018, we upgraded the rating to "Implemented" because we did not identify any discrepancies in SBA's reporting. Also, the Agency appropriately disclosed that it does not perform payment recapture audits because the audits are not cost effective.

We maintained our rating as "Implemented" for the quality of corrective action plans. We found that SBA took appropriate action, such as collecting funds for overpayments and reimbursements to the lender and providing training to address the root cause for the improper payments. Based on our overall assessment of Agency efforts, we upgraded the overall rating from "Substantial Progress" for FY 2017 to "Implemented" for FY 2018. Table 6 summarizes OIG's evaluation of Agency efforts.

Table 6. OIG's Evaluation of Agency Efforts

OMB Criteria	Status at End of 2018
Overall assessment of Agency efforts	Implemented
Accuracy & completeness of Agency reporting	Implemented
Performance in reducing/recapturing improper payments	N/A*
Quality of corrective action plans	Implemented

* SBA has determined that payment recapture audits for 7(a) loan guaranty purchases would not be cost effective.

AFR Review

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

Table 7. OIG's Review of the AFR

OMB Reporting Requirement	Status at End of 2018
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Compliant
Reported rate of less than 10 percent	Compliant

Section 4: Disaster Direct Loan Program

The Disaster Direct Loan Program plays a vital role in the aftermath of disasters by providing long-term, low-interest loans to affected homeowners, renters, businesses, and nonprofit organizations. SBA offers home and business loans to compensate for physical damages and also offers loans to businesses to compensate for economic damages. This program is particularly vulnerable to fraud and unnecessary losses because loan transactions are expedited to provide quick relief to disaster survivors. In FY 2018, SBA disbursed $3.08 billion in disaster assistance.

OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate for the Disaster Direct Loan Program disbursements decreased from 13.65 percent ($123.38 million) in FY 2017 to 8.91 percent ($274.4 million) in FY 2018. SBA stated in its FY 2018 AFR that the decrease from the FY 2017 rate is attributed to SBA's focusing on what makes a payment improper and improving controls over the underwriting and disbursement process. The lack of insurance documentation was the primary root cause for the improper payments. To reduce the improper payments, the Office of Disaster Assistance initiated its ongoing insurance review training in collaboration with the Office of Disaster Strategic Engagement and Effectiveness in October 2018.

OIG's assessment included reviewing three disbursements from SBA's sample, analyzing SBA's sample selection, and interviewing SBA officials involved in the disaster assistance loan IPERA process. Based on our limited assessment, we determined that SBA's improper payment review process was adequate to identify improper payments and met OMB guidelines. Additionally, we did not identify any significant discrepancies with SBA's sampling and testing methodology for improper payments.

Although we did not identify any significant discrepancies, we noted that the Office of Disaster Assistance eased controls for one of SBA's primary root causes for improper payments in FY 2017. Specifically, SBA stated in its 2017 AFR that one cause of the improper payments included lack of appropriate justification for borrowers who may not have had a repayment ability, based on their having a maximum acceptable fixed debt (MAFD) percentage that exceeded SBA's recommended limit. However, in September 2017, SBA increased the threshold for required justification for MAFD from the standard 40 percent to 75 percent.[4] In our 2017 IPERA report, we recommended management establish and implement corrective action plans to address the quality of justifications for exceeding the standard MAFD. Management disagreed with the recommendation, reiterating they would only require justifications for MAFDs exceeding 75 percent. We closed the recommendation as not implemented because loans approved subsequent to this policy change have not had sufficient time to perform. Therefore, we could not fully assess the impact of the policy change on the default rate. OIG will continue to monitor this matter.

We believe lessening internal controls could increase the risk of default in the program. Therefore, we maintain our rating as "Progress" for accuracy and completeness of agency reporting. For FY 2017, we rated the Agency as "Improvement Needed" for quality of corrective actions plans. We upgraded the rating to "Progress" for FY 2018 because SBA implemented insurance review training in collaboration with the Office of Disaster Strategic Engagement and Effectiveness to address the primary root cause of the improper payments for FY 2018. We also upgraded our overall assessment of the Agency's efforts from "Improvement Needed" in 2017 to "Progress" in 2018. Table 8 summarizes OIG's evaluation of Agency efforts.

[4] Office of Disaster Assistance Memorandum No. 17-22, New Credit Model Pilot (September 6, 2017).

Table 8. OIG's Evaluation of Agency Efforts

OMB Criteria	Status at End of 2018
Overall assessment of Agency efforts	Progress
Accuracy & completeness of Agency reporting	Progress
Performance in reducing/recapturing improper payments	N/A*
Quality of corrective action plans	Progress

* SBA has determined that payment recapture audits for this program would not be cost effective.

AFR Review

Based on our review of the AFR and our limited testing, we found that SBA was fully compliant with IPERA reporting requirements. Table 9 summarizes OIG's review of the AFR.

Table 9. OIG's Review of the AFR

OMB Reporting Requirement	Status at End of 2018
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Compliant
Reported rate of less than 10 percent	Compliant

Section 5: Disbursements for Goods and Services

SBA awards contracts for goods and services to assist in carrying out its mission. For FY 2018, SBA made 3,387 disbursements for goods and services totaling approximately $120.3 million.

OIG's Qualitative Assessment of Agency Efforts

SBA's improper payment rate decreased from 4.99 percent ($5.4 million) in FY 2017 to 1.88 percent ($2.2 million) in FY 2018. SBA attributed the reduction of improper payments to implementation of an internal control program in 2017, including an Internal Control Plan and Internal Control Process Plan. The Internal Control Plan established common document templates, checklists, and guides to enhance the quality of contract documentation and invoice reviews prior to payment. Since SBA's improper payment amount totaled less than $10 million, SBA was not required to implement a corrective action plan.

This is the second consecutive year that SBA reduced its rate of improper payments and had improper payment amounts that were less than the statutory threshold of $10 million. As a result, on February 19, 2019, SBA submitted a memo to OMB that requested relief from reporting improper payments for disbursements for goods and services.

Because SBA's improper payment rate has continued to decrease, we maintained the rating of "Implemented" for FY 2018. Table 10 summarizes OIG's evaluation of agency efforts.

Table 10. OIG's Evaluation of Agency Efforts

OMB Criteria	Status at End of 2018
Overall assessment of agency efforts	Implemented
Accuracy & completeness of agency reporting	Implemented
Performance in reducing/recapturing improper payments	N/A*
Quality of corrective action plans	N/A**

* SBA has determined that payment recapture audits for this program were not cost effective.
** Improper payments did not exceed the 1.5 percent and $10 million threshold for reporting a corrective action plan.

AFR Review

Our review of the AFR found that SBA was compliant with IPERA reporting requirements. Table 11 summarizes OIG's review of the AFR.

Table 11. OIG's Review of the AFR

OMB Reporting Requirement	Status at End of 2018
Posted materials	Compliant
Assessed risk	Compliant
Published estimates for susceptible programs	Compliant
Published programmatic corrective action plans	Compliant
Met annual reduction target	Compliant
Reported rate of less than 10 percent	Compliant

Appendix I: Objectives, Scope, and Methodology

This report presents the results of our evaluation of SBA's FY 2018 compliance with IPERA. Our objectives were to (1) determine whether SBA is compliant with IPERA using guidelines outlined in OMB Memorandum M-18-20, Appendix C to OMB Circular No. A-123, Requirements for Payment Integrity Improvement, and (2) assess progress SBA made in remediating improper payment–related recommendations. To perform the evaluation, our scope included an assessment of improper payments that SBA reported for 7(a) loan guaranty purchases, 7(a) loan guaranty approvals, 504 CDC loan guaranty approvals, disbursements for Disaster direct loans, and disbursements for goods and services.

To answer our objectives, we assessed the controls SBA implemented to address prior-year OIG recommendations and evaluated whether SBA addressed required provisions, and we reviewed SBA documentation and plans to assess compliance with identified controls and IPERA provisions. We also assessed the Agency's efforts to prevent and reduce improper payments and reviewed the accuracy and completeness of improper payment reporting in the AFR, as specified in OMB guidance. We performed limited procedures and consulted with a statistician to evaluate the accuracy and completeness of the program-specific improper payment rates. Moreover, we assessed progress the Agency had made since our 2017 review.

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

Use of Computer-Processed Data

We relied on information provided by SBA officials that was extracted from SBA's Disaster Credit Management System, Oracle Federal Financial System, Guaranty Purchase Tracking System, and E-Tran. OIG audits have verified that the financial information maintained in those systems is reasonably reliable. Further, certain data elements associated with loans, procurements, and grants were verified against source documentation maintained in SBA files. We believe this information is reliable for the purposes of this evaluation.

Prior Coverage

Between March 2012 and September 2018, OIG issued the following reports related to the Agency's controls over improper payments.

The OIG High Risk 7(a) Loan Review Program (Report 18-23, September 13, 2018)

The OIG High Risk 7(a) Loan Review Program (Report 18-21, August 15, 2018)

Accuracy of the FY 2015 Disaster Loan Program Improper Payments Rate (Report 18-12, February 13, 2018)

Accuracy of the FY 2015 7(a) Loan Guaranty Purchase Improper Payment Rate (Report 18-07, December 11, 2017)

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Appendix II: Status of Open Recommendations

Since our FY 2018 evaluation, the 7(a) loan guaranty approvals program closed one recommendation, disaster assistance closed four, and 7(a) loan guaranty purchases program closed eight improper payment–related recommendations. The following improper payment–related recommendations remain open.

OIG Report	Recommendation	Management Decision Date	Final Action Date
18-07, Accuracy of the FY 2015 7(a) Loan Guaranty Purchase Improper Payment Rate (December 11, 2017)	7. Require bank to bring the loan into compliance and, if not possible, seek recovery of $69,730, plus interest, on the guaranty paid by SBA for the loan to (see report for bank and borrower names).	01/03/2018	06/28/2019
	9. Require bank to bring the loan into compliance and, if not possible, seek recovery of $1,903,213, plus interest, on the guaranty paid by SBA for the loan to (see report for bank and borrower names).	01/03/2018	07/31/2019
18-21, OIG High Risk 7(a) Loan Review Program (August 21, 2018)	1. Require the lender to bring the loan into compliance, or, if not possible, seek recovery of $799,159 on the guaranty paid by SBA.	08/07/2018	08/01/2019
	2. Require the lender to bring the loan into compliance, or, if not possible, seek recovery of $552,406 on the guaranty paid by SBA.	08/07/2018	08/01/2019
18-23, OIG High Risk 7(a) Loan Review Program (September 13, 2018)	1. Require the lender to bring the loan into compliance, or, if not possible, seek recovery of $448,287 plus interest on the guaranty paid by SBA.	09/20/2018	09/14/2019
	2. Require the lender to bring the loan into compliance, or, if not, seek recovery of $855,116 plus interest on the guaranty paid by the SBA.	09/20/2018	09/14/2019

SBA's Response to Evaluation Report

U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, DC 20416

DATE: May 20, 2019

TO: Hannibal "Mike" Ware
Inspector General

FROM: William Manger
Associate Administrator for Capital Access

SUBJECT: Response to Audit: SBA's FY2018 Compliance with the Improper Payments Elimination and Recovery Act

The Small Business Administration (SBA) appreciates the opportunity to review and respond to the draft Evaluation Report: SBA's FY2018 Compliance with the Improper Payments Elimination and Recovery Act.

SBA is committed to reducing the dollar amount of improper payments, ensuring program integrity, and continuing to implement effective risk management procedures.

SBA concurs with the Recommendations made in this Evaluation Report and is providing the following comments in response to those recommendations.

Recommendation 1. Submit to the Senate Committee on Homeland Security and Governmental Affairs, the House Committee on Oversight and Reform, and OMB, within 90 days of this report, a plan for the 7(a) loan guaranty approvals program that includes the following:

(a) measurable milestones for becoming compliant with IPERA,
(b) designation of an accountable senior Agency official, and
(c) the establishment of an accountability mechanism, describing the actions the Agency will take to become compliant.

Agency Response. SBA will draft and provide a letter to the Senate and House Committees, as required. Within that letter, SBA will include measurable milestones for becoming compliance; will designate an accountable senior Agency official; and, will establish an accountability mechanism, describing Agency actions to become complaint.

Recommendation 2. Submit to the Senate Committee on Homeland Security and Governmental Affairs, the House Committee on Oversight and Reform, and OMB, within 90 days of this report, a plan for the 504 CDC loan guaranty approvals program that includes the following:

(a) measurable milestones for becoming compliant with IPERA,
(b) designation of an accountable senior Agency official, and
(c) the establishment of an accountability mechanism, describing the actions the Agency will take to become compliant.

Agency Response. SBA will draft and provide a letter to the Senate and House Committees, as required. Within that letter, SBA will include measurable milestones for becoming compliance; will designate an accountable senior Agency official; and, will establish an accountability mechanism, describing Agency actions to become complaint.