



STATEMENT OF
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BEFORE THE
SUBCOMMITTEE ON CONTRACTING AND WORKFORCE
COMMITTEE ON SMALL BUSINESS
U.S. HOUSE OF REPRESENTATIVES

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INTRODUCTION

Chairman Knight, Ranking Member Murphy, and distinguished members of the subcommittee, thank you for the opportunity to discuss our oversight of the U.S. Small Business Administration's (SBA's) Historically Underutilized Business Zones (HUBZone) program. The HUBZone program encourages economic development in historically underutilized business zones through the establishment of preferences in Federal contracting opportunities.

The Office of Inspector General (OIG) was established within SBA by statute to promote economy, efficiency, and effectiveness and to deter and detect waste, fraud, abuse, and mismanagement in the Agency's programs and operations. During fiscal year (FY) 2016, OIG achieved nearly \$145 million in monetary recoveries and savings—an almost seven-fold return on investment relative to our FY 2016 operating budget—and made 81 recommendations for improving SBA's operations and reducing fraud and unnecessary losses in the Agency's programs.

OIG'S ROLE

The stated purpose of the Inspector General Act of 1978, as amended (IG Act) is to create an independent and objective unit within specified agencies to combat fraud and abuse in the programs. To this end, my office is responsible for conducting audits and investigations of the programs and operations and undertaking other activities, such as inspections and evaluations, to promote economy, efficiency, and effectiveness in Agency programs. Importantly, as Acting Inspector General (IG), I am charged with keeping the Administrator and Congress fully and currently informed about problems and deficiencies in the Agency. The IG Act contains a variety of statutory guarantees of OIG independence, designed to ensure the objectivity of OIG work and to safeguard against efforts to compromise that objectivity or hinder OIG operations. It is these guarantees of independence that make statutory IGs unique.

The IG Act affords my office the authority to mount a multidisciplinary approach to Agency oversight. We have a broad statutory mandate to conduct audits and investigations relating to the programs and operations of the Agency and to conduct other activities for the purpose of promoting economy and efficiency in the administration of the Agency. Within this broad mandate, I am given full discretion to undertake those audits and investigations that are “necessary or desirable.”

OIG audits are conducted in accordance with Federal audit standards established by the Comptroller General, and other reviews generally are conducted in accordance with standards established by the Council of the Inspectors General for Integrity and Efficiency (CIGIE). In addition, we coordinate with the Government Accountability Office (GAO) to avoid duplicating Federal audits. We also establish criteria to ensure that the non-Federal auditors (typically, certified public accountant firms) that OIG uses comply with Federal audit standards.

OIG investigations are conducted in accordance with the CIGIE Quality Standards for Investigations and Federal law. In conducting investigations, whenever the IG has reason to

believe that Federal criminal law has been violated, the IG must promptly report that evidence directly to the Department of Justice, without prior clearance by Agency officials outside OIG.

TOP MANAGEMENT CHALLENGES FACING SBA

We have aligned our resources to focus on the areas of highest risk within SBA, especially those programs with identified, systemic concerns. In accordance with the Reports Consolidation Act of 2000, OIG released its *Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration in FY 2017* in October 2016 and has prepared similar reports since FY 2000. This report represents our current assessment of Agency programs and activities that pose significant risks, including those that are particularly vulnerable to fraud, waste, error, mismanagement, or inefficiencies. Its overall goal is to focus attention on significant issues in order to work with SBA managers to enhance the effectiveness of programs and operations under their purview. The report highlights the following top management challenges facing SBA:

- Challenge 1. Weaknesses in Small Business Contracting Programs and Inaccurate Procurement Data Undermine the Reliability of Contracting Goals Achievements
- Challenge 2. SBA's IT Leadership Capabilities Need Strengthening to Address Operational Risks and Challenges
- Challenge 3. SBA Needs Effective Human Capital Strategies to Carry Out its Mission Successfully and Become a High-Performing Organization
- Challenge 4. SBA Needs to Improve its Risk Management and Oversight Practices to Ensure Its Loan Programs Operate Effectively and Continue to Benefit Small Businesses
- Challenge 5. SBA Needs to Ensure that the Section 8(a) Business Development Program Identifies and Addresses the Needs of Program Participants, Only Eligible Firms Are Admitted in the Program, and Standards for Determining Economic Disadvantage Are Justifiable
- Challenge 6. SBA Can Improve Its Loan Programs by Ensuring Quality Deliverables and Reducing Improper Payments at SBA Loan Operation Centers
- Challenge 7. Disaster Assistance Must Balance Competing Priorities to Deliver Timely Assistance and Reduce Improper Payments
- Challenge 8. SBA Needs to Effectively Manage Its Acquisition Program

The management challenges are driven by SBA's current needs and are based not only on our understanding of SBA's programs and operations, but also on recent reports from other government agencies, including GAO. Accordingly, the challenges we present each year may change based on the SBA's risks, as well as the actions that it has—or has not—taken to remedy past weaknesses.

The management challenge report is an important tool that we believe assists SBA in prioritizing its efforts to improve program performance and enhance its operations. For our FY 2018 report, we will strive to achieve a shared understanding of the most pressing risks facing SBA leaders, with the goal of better informing Congress and other stakeholders. The chart below summarized the status of SBA’s top management challenges:

		Color Scores					
		Status at End of FY 2016				Change from Prior Year	
	Challenge	Green	Yellow	Orange	Red	Up ↑	Down ↓
1	Small Business Contracting	1	1	2		1	
2	IT Leadership			3			
3	Human Capital		2				
4	SBA Loan Program Risk Management and Oversight		5	1			
5	8(a) Business Development Program		2		1	2	
6	Ensuring Quality Deliverables and Reducing Improper Payments at SBA Loan Operation Centers		3				
7	Disaster Loan Program		2	1			
8	Acquisition Management		4			4	
	TOTAL	1	19	7	1	7	0

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

OIG OVERSIGHT ACTIVITIES INVOLVING HUBZONE PROGRAM

Through audits and other reviews, OIG provides independent oversight of critical aspects of SBA’s programs and operations to improve the Agency’s efficiency and effectiveness. OIG works closely with GAO to provide oversight of SBA’s programs and operations and to promote integrity and efficiency. An important aspect of this work is identifying and following up on SBA’s major management and performance challenges. OIG also supports SBA’s mission by detecting, investigating, and deterring fraud and other wrongdoing in the Agency’s programs and operations. OIG serves as a Government-wide training resource for small business fraud and enforcement issues. These activities help to ensure that SBA employees, loan applicants, and program participants possess a high level of integrity. This is critical to properly administering SBA programs because it helps ensure that the Agency’s resources are used by those who deserve and need them most.

OIG has identified weaknesses in small business contracting programs and inaccurate procurement data as a top management challenge. These weaknesses and inaccuracies undermine the reliability of contracting goal achievement reporting to Congress. The Small Business Act established a Government-wide goal that 23 percent of all prime contracts be

awarded to small businesses each FY. SBA has reported since FY 2013 that the Federal Government met or exceeded its goal of awarding 23 percent of Federal contracting dollars to small businesses. As the advocate for small business, SBA should strive to ensure that only eligible small firms obtain and perform small business awards. Further, SBA should ensure that procuring agencies accurately report contracts awarded to small businesses when representing their progress in meeting small business contracting goals. However, over the years, Congress has expressed concerns about the accuracy of the Small Business Goaling Report. These concerns have been substantiated by OIG audits and other Government studies that have shown widespread misreporting by procuring agencies, since many contract awards that were reported as having gone to small firms have actually been substantially performed by larger companies. Awards made to ineligible firms affect procurement opportunities for small businesses and damage SBA's credibility in reporting accurate small business contracting goals achievements. While some contractors may misrepresent or erroneously calculate their size, the incorrect reporting also results from errors made by Government contracting personnel, including the misapplication of small business contracting rules. Without reliable data, SBA cannot accurately measure the Federal Government's small business contracting goal achievements, which in turn weakens the ability of Congress and other Federal policy makers to determine whether the Government is maximizing contracting opportunities for small businesses.

Opportunities Exist to Further Improve Quality and Timeliness of HUBZone Certifications

In November 2013, OIG issued Audit Report 14-03, *Opportunities Exist to Further Improve Quality and Timeliness of HUBZone Certifications*. This report presents the results of the OIG's audit to determine whether SBA's HUBZone program certification process provides assurance to limit program certification to eligible firms.

OIG found that the HUBZone certification process was reengineered from self-certification to a full document review, and we found that SBA properly certified 9 of 12 firms reviewed. However, OIG identified three firms the SBA certified even when the firms did not meet all of the eligibility criteria. Ineligible firms that obtained certification distorted the small business HUBZone goaling numbers by at least \$1.3 million and possibly took contracting opportunities away from eligible firms. Additionally, certifying ineligible firms detracted from the economic benefits the program intends to promote in the disadvantaged HUBZone areas. The SBA also did not meet the required 30-calendar-day timeline for any of the 12 firms we reviewed, nor did it meet the proposed deadline of 90 days for 5 firms. For firms that are certified, the amount of time SBA takes to review the application directly inhibits opportunities to obtain Federal contracts. OIG recommended three actions directed to the Office of Government Contracting and Business Development to improve the HUBZone certification process and decrease the likelihood of ineligible firms receiving HUBZone certification. SBA officials have since implemented corrective action to close these recommendations.

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

In September 2014, OIG issued Evaluation Report 14-18, *Agencies are Overstating Small Disadvantaged Business and HUBZone Goaling Credit by Including Contracts Performed by*

Ineligible Firms. This report presents the results of our evaluation of select Section 8(a) Business Development Program and HUBZone contract awards.

OIG identified over \$400 million in contract actions that were awarded to ineligible firms, which may have contributed to the overstatement of goaling dollars for the HUBZone and small disadvantaged preference programs in FY 2013. Besides reporting inaccurate information in Federal Procurement Data System-Next Generation (FPDS-NG), procuring agencies may have limited contracting opportunities for firms currently participating in the 8(a) or HUBZone programs.

Further, OIG found that HUBZone and 8(a) certification information is not consistently transmitted to the Dynamic Small Business Search and the System for Award Management. As a result, the affected small businesses are not getting the visibility in the Dynamic Small Business Search, especially the HUBZone firms, which may affect Federal agencies' ability to meet their HUBZone procurement goals.

Additionally, OIG also identified over \$1.5 billion dollars in contract actions for firms that were in the 8(a) or HUBZone programs at the time of contract award but were no longer in the programs in FY 2013. Specifically, SBA regulations permit procuring agencies to claim small disadvantaged business and HUBZone goaling credit on certain contract actions even after firms have left the program. In our opinion, the amount of dollars the SBA reports to Congress and the public as being performed by 8(a) and HUBZone firms in the Small Business Goaling Report is significantly influenced by the inclusion of contract actions performed by former program participants.

OIG made two recommendations to the Associate Administrator for Government Contracting and Business Development intended to strengthen controls between SBA databases on certification data of 8(a) and HUBZone firms and information reported in FPDS-NG. SBA officials have since implemented corrective action to close these recommendations.

HOTLINE, INVESTIGATIONS, SUSPENSION AND DEBARMENT REFERRALS, AND TRAINING AND OUTREACH ACTIVITIES

Hotline

OIG's Hotline receives and reviews allegations of waste, fraud, abuse, or serious mismanagement within SBA or its programs from employees, contractors, and the public. In FY 2016, the Hotline received 1,041 complaints, 18 of which pertained to the HUBZone program. For context, the Hotline received 28 HUBZone-related complaints in FY 2014 and 13 HUBZone-related complaints in FY 2015. Hotline analysts conduct a preliminary review of each allegation and may consult with OIG's Investigations Division, Audits Division, and Office of Counsel to determine the appropriate course of action. Referrals within OIG may result in corrective actions, audits, or administrative, civil, or criminal investigations. Referrals made to SBA program offices are done so for any appropriate tracking or action. Of the 18 HUBZone complaints received in FY 2016, 12 were referred to SBA program officials, 3 were referred to

outside agencies, 2 were referred to OIG's Investigations Division, and 1 was resolved by the Hotline.

Investigations

OIG aggressively investigates allegations of fraud, waste, and abuse involving SBA's programs and operations, to include the HUBZone program. In FY 2016, the SBA OIG's investigations resulted in 45 indictments or informations and 41 convictions. Since FY 2014, OIG opened 13 investigations involving the HUBZone program, resulting in 13 indictments or informations, 12 convictions or guilty pleas, \$11,891,589 in dollar accomplishments (potential investigative recoveries, fines, and asset forfeitures attributed to OIG investigations), and \$35,000,000 of cost avoidances (loans/contracts not approved or canceled as a result of OIG investigations).

In pursuing investigations involving fraud, waste, or abuse in the HUBZone program, OIG has a strong record of collaborating with GAO. Two notable examples of such efforts were initiated in 2008 and 2009, respectively:

- In testimony on July 17, 2008, GAO identified 10 firms in the Washington, DC, area participating in the HUBZone program even though they clearly did not meet the eligibility requirements. These 10 firms were investigated by OIG. All 10 cases were declined criminally by the United States Attorney's Office; however, the Department of Justice's Civil Fraud Division opened investigations on 6 firms that were alleged to be in non-compliance with the HUBZone principal office requirement, resulting in \$1.3 million in civil settlements from 4 of these companies.
- On March 25, 2009, GAO released report GAO-09-440: *HUBZONE PROGRAM - Fraud and Abuse Identified in Four Metropolitan Areas*. The four metropolitan areas identified were Dallas, TX; Huntsville, AL; San Antonio, TX; and San Diego, CA. OIG opened investigations in Texas and California in response to the findings of this report. One of the investigations resulted in a \$200,000 civil settlement.

Suspension and Debarment Referrals

OIG promotes suspensions, debarments, and similar administrative enforcement actions. These actions protect taxpayer funds from parties who are not a good risk for the Government. A typical OIG referral contains a summary of allegations, suggested administrative record (evidence supporting the case), and a draft notice of suspension or proposed debarment. Most OIG administrative referrals involve SBA's loan and contract programs. OIG ensures a suspension and debarment official reviews all appropriate allegations arising in other contexts, such as the investigation of False Claims Act qui tam cases.

In FY 2016, OIG sent 75 suspension and debarment referrals to the SBA. Included among these 75 referrals were 7 involving the HUBZone program. For context, OIG referred 74 matters to the SBA in FY 2015, with 6 of these involving the HUBZone program, and in FY 2014, OIG referred 50 matters to SBA, with 2 of these involving the HUBZone program. With the exception of the lending programs, SBA has not acted on suspension and debarment referrals

from OIG in a timely manner. As such, OIG has planned a review of SBA's suspension and debarment processes to increase transparency in this area and inform the Administrator and Congress of our findings.

Training and Outreach Activities

OIG also conducts, supervises, and participates in various training activities to counter fraud in SBA programs. Annually, OIG's training and outreach efforts include over a thousand attendees, including Government employees, lending officials, and law enforcement representatives, on topics related to fraud in Government lending and contracting programs. In FY 2016, OIG partnered with the National Science Foundation OIG to present the second annual Small Business Procurement Integrity Seminar. This seminar, which OIG offered in two locations, equipped Federal oversight personnel with the knowledge to identify, develop, and pursue small business contracting fraud cases. The course covered the major small business contracting programs and included a discussion of typical fraud schemes, program rules, and key procurement databases accentuated by multiple case studies. At the end of the session, participants took part in a hypothetical case, which allowed the application of principles taught during the day. OIG personnel also participated in the training of criminal investigators from several Federal agencies and the District of Columbia OIG. This training included information on subpoenas, civil remedies, administrative remedies, and small business procurement cases. OIG will continue to pursue these training opportunities as part of its outreach efforts.

CONCLUSION

OIG continues to focus on the most critical risks facing SBA, and weaknesses in small business contracting programs and inaccurate procurement data is among these risks. Though the Federal Government has a goal of only 3 percent of all dollars for Federal prime contracts to HUBZone-certified small business concerns, OIG will continue to focus its oversight efforts on this program to maintain its integrity and inform the Administrator and Congress of findings related to the program's operations. We are planning a review involving the HUBZone program for inclusion on our 2018 Audit Oversight Plan. As always, we will coordinate with our GAO colleagues with a view toward avoiding duplication and ensuring effective coordination and cooperation on oversight of the HUBZone program. We value our relationship with this subcommittee, and with the Committee on Small Business and Congress at large, and we look forward to working together to address identified risks and the most pressing issues facing the HUBZone program.