

THE SMALL BUSINESS ADMINISTRATION'S
IMPLEMENTATION OF RECOMMENDED CONTROLS AND
THE ECONOMIC AID ACT

REPORT NUMBER 21-19 | August 12, 2021





EXECUTIVE SUMMARY

THE SMALL BUSINESS ADMINISTRATION'S IMPLEMENTATION OF RECOMMENDED CONTROLS AND THE ECONOMIC AID ACT

Report
21-19

August 12,
2021

What OIG Reviewed

The Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (Economic Aid Act) was enacted on December 27, 2020 to continue assistance under the Paycheck Protection Program (PPP) for small businesses financially impacted by the ongoing coronavirus pandemic. Under the Economic Aid Act, the PPP was extended to provide over \$284 billion in guaranteed SBA loans. The additional funds under the Economic Aid Act were available until March 31, 2021. The PPP Extension Act of 2021 later extended the program to June 30, 2021. The PPP ended on May 31, 2021 and lenders approved over \$277 billion in PPP funds under the Economic Aid Act.

On December 23, 2020, the Office of Inspector General (OIG) issued a memorandum on key PPP-related recommendations at the request of the Small Business Administration (SBA) and in anticipation of the Economic Aid Act. Based on previous and ongoing reviews, OIG offered key recommendations to strengthen internal controls to prevent fraud and ensure only eligible businesses receive PPP funds.

Our objectives were to determine if SBA 1) considered prior OIG key recommendations to strengthen controls for ensuring eligibility and mitigating fraud and 2) implemented the PPP in accordance with the Economic Aid Act. To accomplish our objective, we reviewed the Economic Aid Act, SBA's Interim Final Rules and Frequently Asked Questions. We also assessed SBA Procedural Notices, a letter from the SBA Administrator, and PPP applications.

What OIG Found

SBA implemented or initiated action on all of the OIG recommendations to strengthen internal controls related to the PPP, as outlined in the OIG Key Recommendations memorandum. Overall, we found SBA implemented the PPP in accordance with the Economic Aid Act with two exceptions relative to the assessment of faith-based organizations and the issuance of guidance for farm credit system institution requirements. SBA did not 1) require an assessment of affiliation for faith-based organizations which contradicts its

internal control procedures and 2) issue guidance regarding farm credit system institutions to ensure requirements were met.

On February 22, 2021, the White House announced changes to the PPP to target the smallest businesses and businesses that were not helped in previous relief efforts. SBA implemented four of the five White House announced changes by issuing an Interim Final Rule, Frequently Asked Questions, and updated applications. However, SBA could not provide sufficient evidence that it established the \$1 billion set aside as required to provide additional assistance to sole proprietors, independent contractors, and self-employed individuals located in low- and moderate-income areas.

OIG Recommendations

We recommend SBA assess affiliation for faith-based organizations to ensure only eligible faith-based organizations receive the applicable PPP loans. We are not making any recommendations regarding the farm credit system institution requirements and the \$1 billion set aside because the PPP ended on May 31, 2021. We advised SBA that if future stimulus funds are made available with such requirements, SBA should ensure it implements the requirements accordingly.

Agency Response

SBA disagreed with the recommendation, stating it committed to not assessing or requiring lenders to assess the reasonableness of the faith-based organization's determination, which they believe met the intent of Congress. However, SBA clarified its PPP loan review plan and updated its affiliation worksheet to reflect that affiliation rules do not apply for faith-based organizations. This recommendation is considered resolved and closed upon issuance of this report based on SBA's final decision not to assess the reasonableness of faith-based determinations and its revised updated affiliation worksheet.



Office of Inspector General

U.S. Small Business Administration

DATE: August 12, 2021

TO: Isabella Casillas Guzman
Administrator

FROM: Hannibal "Mike" Ware
Inspector General

A handwritten signature in black ink, appearing to read "H. Ware".

SUBJECT: Small Business Administration's Implementation of Recommended Controls and the Economic Aid Act

This report presents the results of our analysis of the Small Business Administration's Implementation of Recommended Controls and the Economic Aid Act. We considered management's comments on the draft of this report when preparing the final report. Management disagreed with the recommendation.

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, contact Teresa Gray, Director of Credit Programs Group, or Andrea Deadwyler, Assistant Inspector General for Audits, at (202) 205-6586.

cc: Patrick Kelley, Associate Administrator, Office of Capital Access
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Introduction

On December 27, 2020, Congress enacted the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act to continue financial assistance through the Paycheck Protection Program (PPP) for small businesses impacted by the coronavirus pandemic. The PPP had been established in late March 2020 by the Coronavirus Aid, Relief, and Economic Security (CARES) Act.

Under the Economic Aid Act, the PPP was extended through March 31, 2021 to provide over \$284 billion in guaranteed SBA loans. The loans can be used for a small business' payroll, rent, utility payments, and other limited uses and can be forgiven if loan proceeds were used in accordance with the law. In addition, certain eligible borrowers who had previously received a PPP loan could apply for additional PPP funds. The PPP Extension Act of 2021 extended the program through June 30, 2021 although additional funds remain available until September 30, 2021. However, the PPP ended on May 31, 2021 and lenders approved over \$277 billion in PPP funds under the Economic Aid Act.

Office of Inspector General Key Recommendations

In response to a request from the former Administrator of the Small Business Administration and in anticipation of the imminent passage of the Economic Aid Act, the Office of Inspector General (OIG) issued a memorandum, "Key Recommendations Based on Lessons Learned from Prior COVID-19 Economic Injury Disaster and Paycheck Protection Program Loan Programs," on December 23, 2020. We offered SBA several recommendations based on our previous and ongoing reviews to strengthen internal controls to prevent fraud and ensure only eligible businesses receive PPP funds.

Economic Aid Act Requirements

SBA was required to issue PPP-related regulations to carry out certain provisions of the Act within 10 days of enactment of the Economic Aid Act. The Act made several changes to PPP, including the processes for making PPP loans, loan increases, loan forgiveness, additional eligible expenses, loan eligibility, and conflict of interest disclosures.

The Act also allowed eligible existing PPP borrowers to access funds as a "second draw" PPP loan. The borrowers were required to meet specific requirements, including having 300 or fewer employees and a decrease in gross receipts.

SBA Formal Guidance

As of March 12, 2021, SBA issued four Interim Final Rules to carry out changes made to PPP by the Economic Aid Act, as follows:

1. Interim Final Rule on Paycheck Protection Program as Amended by Economic Aid Act, issued January 6, 2021
2. Interim Final Rule on Paycheck Protection Program Second Draw Loans, issued January 6, 2021
3. Interim Final Rule on Paycheck Protection Program – Loan Forgiveness Requirements and Loan Review Procedures as Amended by Economic Aid Act, issued January 19, 2021

4. Interim Final Rule on Paycheck Protection Program – Revisions to Loan Amount Calculation and Eligibility, issued March 3, 2021

In addition to the Interim Final Rules, SBA issued six Procedural Notices that addressed implementation of the Economic Aid Act, primarily related to eligibility, PPP loan increases, loan forgiveness, and loan reviews.

Other Guidance and Resources

As of March 12, 2021, SBA had also issued four borrower application forms, four lender forms, and three loan forgiveness applications. The agency also updated existing Frequently Asked Questions (FAQs) and issued guidance on how to calculate maximum loan amounts. In addition, SBA provided informational slides and PPP platform user guides.

Objective

Our objectives were to determine if SBA 1) considered prior key OIG recommendations to strengthen controls for ensuring eligibility and mitigating fraud and 2) implemented the PPP in accordance with the Economic Aid Act.

Results

SBA has either implemented or begun taking action on all of the OIG recommendations to strengthen internal controls related to the PPP, as outlined in the OIG Key Recommendations memorandum. SBA updated the PPP borrower application to include a field for the North American Industry Classification System code and borrower demographic information. The agency established controls to verify that the loan amount does not exceed the maximum amount per employee, the maximum number of employees, or other applicable size standards. SBA also required verifying that businesses were established before the mandated date and that loan applicants were not included on Treasury's Do Not Pay death records.

Overall, we determined SBA implemented the PPP in accordance with the Economic Aid Act. SBA accomplished this by issuing guidance and providing other resources, including informational slides and PPP platform user manuals, to clarify requirements and how to perform related tasks. However, we determined that SBA's guidance did not require an assessment of affiliation for faith-based organizations to ensure these borrowers met eligibility requirements. SBA also did not issue guidance for farm credit system institution requirements to ensure these institutions met requirements.

We also determined that SBA generally issued guidance in accordance with the February 22, 2021, White House announcement of changes to the PPP.¹ However, SBA did not provide sufficient evidence that it created the required a \$1 billion set-aside or that it issued related guidance for eligible sole proprietors, independent contractors, and self-employed individuals.

¹ ["Fact Sheet: Biden-Harris Administration Increases Lending to Small Businesses in Need. Announces Changes to PPP to Further Promote Equitable Access to Relief."](#) Executive Office of the President, February 22, 2021. Accessed February 23, 2021.

OIG Key Recommendations

SBA implemented two recommendations on updating borrower applications and began taking action on two recommendations to strengthen internal controls to prevent fraud and ensure only eligible businesses receive PPP funds, as outlined in the *OIG Key Recommendations memorandum*.

Updating Borrower Application

OIG recommended SBA update the PPP borrower application to include a field for the North American Industry Classification System code for the business category and the business description to prevent potentially ineligible loan approvals. SBA updated the PPP borrower application to include a field for the code that can be used to identify the business description.

OIG also recommended SBA revise the borrower application to include borrower demographic information. SBA updated the PPP borrower application to include a request for borrower demographic information.

Assessing Vulnerabilities in Internal Controls

OIG recommended SBA assess vulnerabilities in internal controls and strengthen or implement necessary internal controls to address ineligible loans and potential fraud. OIG found that, at minimum, it was critical for SBA to implement a process to ensure lenders validate the following:

- The loan amount does not exceed the maximum amount per employee.
- The business was established before the mandated date. Verifying the date may require coordination with the Treasury to confirm what dates the business applied for and received a Taxpayer Identification Number.
- The loan amount does not exceed the maximum number of employees or other applicable size standards.

SBA management began taking action by establishing controls to verify that the maximum loan amount calculation did not include annual salary of any individual employee in excess of \$100,000. SBA also established controls to verify that monthly payroll costs were accurately calculated and verified against supporting documentation.

In addition, SBA required lenders to validate that any self-employed individual, independent contractor, or sole proprietor was established before the mandated date of February 15, 2020. Through automated and manual PPP loan reviews, SBA verified all businesses were in operation on or before February 15, 2020.

SBA established controls through Interim Final Rules, FAQs, and related guidance documents to ensure borrowers met standards, such as having 500 or fewer employees and SBA's alternative size standards for borrower eligibility. Related guidance documents included the Paycheck Protection Program Loan Review Plan, Forgiveness Review Guide, and PPP maximum eligible amount calculator.

In addition, SBA established a hold code for disqualifying businesses not in operation before February 15, 2020, and two hold codes for borrower eligibility size standard requirements in an SBA Procedural Notice that was effective on February 10, 2021.

According to the SBA Procedural Notice, the hold codes are part of SBA's front-end compliance checks on PPP loans.

Using Treasury's Do Not Pay Database

OIG recommended SBA coordinate with Treasury to develop a technical solution to enable use of Treasury's Do Not Pay database to determine loan applicant eligibility and prevent improper payments before the release of any federal funds. SBA has taken steps to coordinate with Treasury regarding access to the Treasury's Do Not Pay List.

In February 2021, SBA was able to obtain and use death source data sets in the Treasury's Do Not Pay database. SBA has continued to coordinate with Treasury to gain full access to other data sets in the Do Not Pay database, including the Treasury Offset Program Debt Check, which identifies potential borrowers who are delinquent on federal nontax debt and child support obligations. An SBA Procedural Notice effective February 10, 2021, established the following three hold codes related to the Treasury's Do Not Pay List subsets for front-end compliance checks on PPP loans:

- "46 – Death Sources" includes deceased records from the Department of Defense, Department of State, Social Security Administration, and obituary and probate death data.
- "47 – System for Award Management Exclusions" identifies persons excluded from receiving federal contracts, certain subcontracts, and federal financial and non-financial assistance and benefits.
- "48 – Treasury Offset Program and Credit Alert Interactive Verification Reporting System" shows persons delinquent on federal nontax debts and other debts owed to federal agencies, child support obligations, or in default on direct or guaranteed federal loans.

Economic Aid Act Implementation

Overall, we found SBA implemented the PPP in accordance with the Economic Aid Act. SBA accomplished this by issuing guidance and providing other resources including informational slides and PPP platform user manuals to understand requirements and how to perform related tasks. SBA issued Interim Final Rules, Procedural Notices, Frequently Asked Questions, and seven updated applications that include the North American Industry Classification System code as well as the applicant's demographic information.

However, SBA's January 6 Interim Final Rule did not require an assessment of affiliation for faith-based organizations, which contradicts SBA's internal control procedures. SBA also did not issue guidance on farm credit system institution requirements to comply with the Economic Aid Act.

We also determined SBA issued guidance in accordance with White House changes to the PPP. However, we identified one area that SBA did not address to ensure additional assistance was provided to eligible sole proprietors, independent contractors, and self-employed individuals.

Statutory Requirements

As of March 5, 2021, SBA had complied with six statutory deadlines for the issuance of regulations for the PPP. SBA met the deadlines by issuing Interim Final Rules, Procedural Notices, a letter from the SBA Administrator, a Forgiveness Audit Plan, and an updated forgiveness application. SBA also provided other resources, such as informational slides and updated PPP platform user manuals to implement the PPP.

The Economic Aid Act required SBA to issue PPP related regulations by January 6, 2021.² SBA met this deadline, issuing two Interim Final Rules on January 6. One of the interim rules outlined key PPP loan provisions, including eligibility of applicants, the PPP lending process, loan increases, and loan forgiveness. The second interim rule explained loan terms, eligibility requirements, and application process for second draw PPP loans.

SBA also met the following deadlines to comply with the Act:

- established a one-page certification for loan forgiveness by January 20, 2021³
- submitted a forgiveness audit plan to Congress by February 10, 2021⁴
- issued guidance addressing barriers to accessing capital for minority, underserved, veteran, and women-owned businesses by January 6, 2021⁵
- issued guidance on eligibility for the full and partial returns of PPP funds by January 13, 2021⁶

² Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act; Section 303, December 27, 2020.

³ Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act; Section 307(a)(3), December 27, 2020.

⁴ Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act; Section 307(a)(3), December 27, 2020.

⁵ Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act; Section 311(a), December 27, 2020.

⁶ Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act; Section 312(b), December 27, 2020.

- issued guidance on PPP loan forgiveness related to Economic Injury Disaster Loans by January 11, 2021⁷

Assessment of Affiliation for Faith-Based Organizations

We determined that SBA met the intent of the Economic Aid Act requirement on faith-based organizations by clarifying the eligibility of churches and religious organizations. SBA's January 6 Interim Final Rule states affiliation rules for faith-based organizations do not apply, including any relationship to a parent or subsidiary and other applicable aspects of organizational structure or form.

A faith-based organization applying for PPP loans may rely on a reasonable, good faith interpretation in determining whether its relationship to any other person, group, organization, or entity is exempt from the affiliation rules.⁸

SBA's Paycheck Protection Program Loan Review Plan requires an affiliation check to determine whether the borrower appropriately met PPP eligibility requirements. SBA's January 6 Interim Final Rule states it will not assess and will not require participating lenders to assess the reasonableness of a faith-based organization's affiliation determination, which contradicts SBA's internal control procedures. Without assessing the faith-based organization's determination, SBA cannot provide reasonable assurance that faith-based organizations meet affiliation exemption standards (See Appendix III). Although SBA management stated the affiliation check will include faith-based organizations, they did not provide support documentation as to how SBA will ensure it is done.

Farm Credit System Institution Requirements

We determined that SBA did not implement the Farm Credit System Institution requirements of the Economic Aid Act. The Act states, "with respect to the application of Farm Credit Administration capital requirements, a loan 1) shall receive a risk weight of zero percent and 2) shall not be included in the calculation of any applicable leverage ratio or other applicable capital ratio or calculation."⁹

An SBA official stated they did not issue the related guidance because the Farm Credit Administration is responsible for regulating Farm Credit System Institutions. However, SBA is responsible for implementation of the PPP and should have coordinated with the Farm Credit Administration to issue guidance to ensure correct application of capital requirements. We are not making a recommendation regarding this matter because the PPP ended on May 31, 2021. If future PPP funds are made available with a requirement for farm credit institutions, SBA should ensure it issues related guidance in coordination with the Farm Credit Administration (See Appendix III).

⁷ Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act; Section 333(e)(1), December 27, 2020.

⁸ Interim Final Rule – Paycheck Protection Program as Amended by Economic Aid Act, January 6, 2021.

⁹ Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act; Section 314(b)(3)(A), December 27, 2020.

Changes to the PPP

On February 22, 2021, the White House announced five significant changes to the PPP to target the smallest businesses.

SBA implemented four of the five changes by issuing an Interim Final Rule, Frequently Asked Questions, and updated applications. SBA did not fully implement changes related to providing assistance to eligible sole proprietors, independent contractors, and self-employed individuals.

The Administration's release called for additional assistance to sole proprietors, independent contractors, and self-employed individuals. SBA was required to establish a \$1 billion set aside for businesses without employees that are located in low- and moderate-income areas.

According to SBA, it established the \$1 billion set aside. However, SBA could not provide sufficient evidence to support that a set aside was established and that it issued related guidance for the eligible borrower's awareness. As a result, SBA cannot provide reasonable assurance that additional assistance was provided to sole proprietors, independent contractors, and self-employed individuals in accordance with the White House changes. We are not making a recommendation regarding this matter because the PPP ended on May 31, 2021. If future PPP funds are made available with a requirement for set asides, SBA should ensure it establishes the set asides and issues related guidance.

Recommendations

We recommend the Administrator direct the Associate Administrator of the Office of Capital Access to:

1. Assess affiliation for faith-based organizations to ensure only eligible faith-based organizations received the applicable PPP loans.

Analysis of Agency Response

SBA management provided formal comments to the draft report, which are included in their entirety in Appendix IV. Management disagreed with the recommendation. We considered management's comments when preparing this final report.

Summary of Actions Necessary to Close the Recommendations

The following details the status of our recommendations and the actions necessary to close them.

Recommendation 1

Assess affiliation for faith-based organizations to ensure only eligible faith-based organizations received the applicable PPP loans.

Status: Resolved

SBA management disagreed with this recommendation stating the agency committed that it would not assess nor require participating lenders to assess the reasonableness of the faith-based organization's determination. Management stated it allowed an exemption for faith-based organizations and would rely on their reasonable, good faith interpretation to determine if the exemption would apply. Further, management stated the exemption

properly met the intent of Congress by clarifying the eligibility of these organizations. According to management, reversing course on this commitment would violate policies set in Interim Final Rules and be challenged as contrary to the intent of Congress.

In the report, we acknowledge that SBA met the intent of Congress by clarifying the eligibility of faith-based organizations. We also noted that SBA's PPP Loan Review Plan was not consistent with its Interim Final Rule regarding affiliation for faith-based organizations. During our review, SBA indicated it would perform eligibility assessments of faith-based organizations as indicated in its PPP Loan Review Plan. However, in management's comments, SBA reversed its position, stating it will not assess, nor require lenders to assess the reasonableness of the faith-based organization's determination. In subsequent correspondence, SBA clarified its PPP loan review plan and updated its affiliation worksheet in June 2021 to reflect that affiliation rules do not apply for faith-based organizations, which is consistent with its Interim Final Rule.

This recommendation is considered resolved and closed upon issuance of this report based on SBA's final decision not to assess the reasonableness of faith-based determinations and its revised updated affiliation worksheet that corresponds to the Interim Final Rule. We will consider any potential risks associated with this decision as we plan and prioritize future oversight work in this area.

Appendix I: Objectives, Scope, and Methodology

Our objectives were to determine if SBA 1) considered prior OIG key recommendations to strengthen controls for ensuring eligibility and mitigating fraud and 2) implemented the PPP in accordance with the Economic Aid Act.

To accomplish our objectives, we reviewed all relevant federal regulations, policies, procedures, and guidance, including the:

- Economic Aid Act
- CARES Act
- Paycheck Protection Program and Health Care Enhancement Act
- Paycheck Protection Program Flexibility Act of 2020
- Interim Final Rules
- Frequently Asked Questions
- Procedural Notices
- PPP program forms
- PPP changes announced by the White House

We interviewed officials from the Office of Capital Access about implementation of PPP according to the Act. We also reviewed OIG's prior work on the PPP to determine whether SBA took OIG recommendations into account when meeting the Economic Aid Act's requirements.

We did not validate whether controls established by SBA accomplished intended outcomes. In addition, we did not test to ensure borrowers or lenders were complying with SBA's PPP guidance. This analysis does not take the place of audit follow-up for the key recommendations of related OIG projects. We undertook this analysis of SBA's consideration of key OIG recommendations to meet the objectives of this project only. Accordingly, to close recommendations from any related OIG reports, SBA must follow the standard OIG audit process.

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

Use of Computer-Processed Data

We did not rely on computer processed data for this review.

Appendix II: Prior Work

Inspection of SBA's Implementation of the Paycheck Protection Program (Report 21-07, January 14, 2021).

We found SBA's hurry to lend capital to businesses was at the expense of controls that could have reduced the likelihood of ineligible or fraudulent business obtaining a PPP loan. In addition, aspects of SBA's implementation of the PPP will prevent Congress and SBA management from having the information needed to determine if program objectives were fully met. We also determined some aspects of SBA's initial implementation of the PPP were not executed efficiently. We made six recommendations to improve SBA's program.

Paycheck Protection Program Loan Recipients on the Department of Treasury's Do Not Pay List (Report 21-06, January 11, 2021).

After receiving thousands of complaints of fraud, OIG collaborated with the U.S. Department of the Treasury to identify high-risk transactions related to financial assistance to small businesses. We found SBA needed to take immediate action to limit improper payments. We made three recommendations to establish more effective oversight controls related to the PPP and continue to work with SBA to resolve the recommendations.

Small Business Administration's Implementation of the Paycheck Protection Program Requirements (Report 20-14, May 8, 2020).

We found SBA's Interim Final Rules for implementing the PPP and the Frequently Asked Questions mostly aligned with the CARES Act. We found four areas that did not fully align with CARES Act's provisions: 1) prioritizing underserved and rural markets, 2) loan proceeds eligible for forgiveness, 3) guidance on loan deferments, and 4) registration of loans. We suggested five actions to address our findings.

Appendix III: Comparison of the Economic Aid Act and Issued Guidance

This comparison is based on the finding titled Economic Aid Act Implementation and does not include the entirety of the Economic Aid Act.

Economic Aid Act Requirements	Interim Final Rule	Other Related Guidance
<p>Section 311. Paycheck protection program second draw loans.</p> <p>(c) Eligible Churches and Religious Organizations.</p> <p>(1) Sense of Congress. - It is the sense of Congress that the interim final rule of the Administration entitled “Business Loan Program Temporary Changes; Paycheck Protection Program” (85 Fed. Reg. 20817 (April 15, 2020)) properly clarified the eligibility of churches and religious organizations for loans made under paragraph (36) of section 7(a) of the Small Business Act (15 U.S.C. 636(a)).</p>	<p>Interim Final Rule: Paycheck Protection Program as Amended by the Economic Aid Act Effective January 6, 2021 (IFR1) Section B.3.</p> <p>c. Faith-Based Organizations</p> <p>This rule exempts otherwise qualified faith-based organizations from the SBA’s affiliation rules, including those set forth in 13 CFR part 121, where the application of the affiliation rules would substantially burden those organizations’ religious exercise. For the reasons described in 85 Fed. Reg. 20817, the SBA’s affiliation rules, including those set forth in 13 CFR part 121, do not apply to the relationship of any church, convention or association of churches, or other faith-based organization or entity to any other person, group, organization, or entity that is based on a sincere religious teaching or belief or otherwise constitutes a part of the exercise of religion. This includes any relationship to a parent or subsidiary and other applicable aspects of organizational structure or form. A faith-based organization seeking loans under this program may rely on a reasonable, good faith interpretation in determining whether its relationship to any other person, group, organization, or entity is exempt from the affiliation rules under this provision, and SBA will not assess, and will not require participating lenders to assess, the reasonableness of the faith-based organization’s determination.</p>	<p>SBA did not issue any additional guidance to address Section 311 clause (c) of the Economic Aid Act.</p>

<p>(Continued from previous page)</p>	<p>Interim Final Rule: Paycheck Protection Program Second Draw Loans Effective January 6, 2021 (IFR2) Section III.</p> <p>B. Affiliation Rules</p> <p>SBA also adopted a religious exemption to the affiliation rules by regulation (See section (B)(3)(c) of IFR1), which applies to Second Draw PPP loans.</p>	<p>(Continued from previous page)</p>
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<p>Section 314. Farm credit systems institutions.</p> <p>(b) Facilitation of Participation in PPP and Second Draw Loans</p> <p>(3) RISK WEIGHT. —</p> <p>(A) IN GENERAL. —With respect to the application of Farm Credit Administration capital requirements, a loan described in subparagraph (B)—</p> <p>(i) shall receive a risk weight of zero percent; and</p> <p>(ii) shall not be included in the calculation of any applicable leverage ratio or other applicable capital ratio or calculation.</p> <p>(B) LOANS DESCRIBED. —A loan referred to in subparagraph (A) is—</p> <p>(i) a loan made by a Farm Credit Bank described in section 1.2(a) of the Farm Credit Act of 1971 (12 U.S.C. 2002(a)) to a Federal Land Bank Association, a Production Credit Association, or an agricultural credit association described in that section to make loans under paragraph (36) or (37) of section 7(a) of the Small Business Act (15 U.S.C. 636(a)) or forgive those loans in accordance with section 7A of the Small Business Act, as redesignated and transferred by section 304 of this Act, and subparagraph (J) of such paragraph (37); or (ii) a loan made by a Federal Land Bank Association, a Production Credit Association, an agricultural credit association, or the bank for cooperatives described in section 1.2(a) of the Farm Credit Act of 1971 (12 U.S.C. 2002(a)) under paragraph (36) or (37) of section 7(a) of the Small Business Act (15 U.S.C. 636(a)).</p>	<p>SBA did not issue an Interim Final Rule to address Section 314 clause (b)(3) of the Economic Aid Act.</p>	<p>SBA did not issue any additional guidance to address Section 314 clause (b)(3) of the Economic Aid Act.</p>
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Appendix IV: Management Comments

SBA RESPONSE TO INSPECTION REPORT



U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

TO: Hannibal “Mike” Ware, Inspector General
The Office of Inspector General (OIG)

FROM: Patrick Kelley /s/ *Patrick Kelley*
Associate Administrator, Office of Capital Access

SUBJECT: Response to OIG Draft Report entitled “The Small Business Administration’s Implementation of Recommended Controls and the Economic Aid Act”

DATE: June 22, 2021

Thank you for providing the Office of Capital Access the opportunity to respond to OIG’s Draft Report entitled, “The Small Business Administration’s Implementation of Recommended Controls and the Economic Aid Act”, dated May 25, 2021. The OIG’s audit objective for this draft report was to determine if SBA 1) considered prior key OIG recommendations to strengthen controls for ensuring eligibility and mitigating fraud and 2) implemented the PPP in accordance with the Economic Aid Act.

The Office of Capital Access (OCA) has the following comments with respect to the OIG recommendation:

OIG Recommendation – We recommend the Administrator direct the Associate Administrator of the Office of Capital Access to assess affiliation for faith-based organizations to ensure only eligible faith-based organizations receive the applicable PPP loans.

SBA Response: SBA did not concur with this recommendation because SBA committed that SBA will not assess, and will not require participating lenders to assess, the reasonableness of the faith-based organization’s determination.

On April 15, 2020, SBA published an Interim Final Rule (IFR-2) in the Federal Register, 85 FR 20817, to exempt faith-based organizations from the application of SBA’s affiliation rules for the Paycheck Protection Program (PPP) where such organizations would “otherwise be disqualified from participation in PPP because of affiliations that are a part of their religious exercise.” SBA concluded that an exemption was required, or at a minimum authorized, by the Religious Freedom Restoration Act (RFRA) (Pub. L. 103-141). To effectuate the exemption, SBA authorized faith-based organizations to rely on a “reasonable, good faith interpretation” to determine whether the exemption would apply. SBA committed that “SBA will not assess, and will not require participating lenders to assess, the reasonableness of the faith-based organization’s determination.” 85 FR at 20820 (emphasis added.)

SBA further explained in changes to its affiliation regulation, 13 C.F.R. § 121.103(b)(10)(ii), that “[n]o specific process or filing is necessary to claim the benefit of the exemption....”

Congress addressed IFR-2 in section 311(c)(1) of the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (Economic Aid Act), Pub. L. 116-260. In a Sense of Congress provision, the Economic Aid Act states that IFR-2 “properly clarified the eligibility of churches and religious organizations for [PPP] loans. . . .”

To implement the Economic Aid Act, SBA issued another Federal Register Interim Final Rule on January 14, 2021. Addressing the provision that Congress had found to have “properly clarified . . . eligibility,” SBA advised that SBA’s affiliation rules do not apply to the relationship of any church, convention or association of churches, or other faith-based organization or entity to any other person, group, organization, or entity that is based on a sincere religious teaching or belief or otherwise constitutes a part of the exercise of religion. SBA reiterated the agency’s commitment that “SBA will not assess, and will not require participating lenders to assess, the reasonableness of the faith-based organization’s determination.” 85 FR at 3699 (emphasis added).

[To renege on its commitment not to “assess . . . the reasonableness of [a] faith-based organization’s determination,” SBA would need to contravene policies issued twice through public Federal Register interim final rules. Congress specifically called out IFR-2’s policy as “properly clarify[ing] the eligibility of churches and religious organizations.” Therefore, reversing course would be challenged as contrary to the sense of Congress, as well as thwarting the legitimate expectations of borrowers that relied on SBA’s public policy statements.]

Enclosed: Federal Register 85 FR 20817 20-04-15 and 86 FR 3692 21-01-14