U.S. SMALL BUSINESS ADMINISTRATION

OFFICE OF INSPECTOR GENERAL

Report No. 12-01

Fiscal Year 2012
Report on the Most Serious Management and Performance Challenges
Facing the Small Business Administration

October 21, 2011
MEMORANDUM

TO: Karen G. Mills
   Administrator

FROM: Peggy E. Gustafson /s/
       Inspector General

SUBJECT: Fiscal Year 2012 Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration

In accordance with the Reports Consolidation Act of 2000, we are providing you with the Office of Inspector General’s (OIG) Fiscal Year (FY) 2012 Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration (SBA). This report represents our current assessment of agency programs and/or activities that pose significant risks, including those that are particularly vulnerable to fraud, waste, error, mismanagement, or inefficiencies. The Challenges are not presented in order of priority, as we believe that all are critical management or performance issues.

Our report is based on specific OIG, Government Accountability Office (GAO), and other official reports, as well as our general knowledge of SBA’s programs and operations. Our analysis generally considers those accomplishments that SBA reported as of September 30, 2011.

Within each Management Challenge, there are a series of “recommended actions” to resolve the Challenge. Each recommended action is assigned a color “status” score. The scores are as follows: Green for “Implemented”; Yellow for “Substantial Progress”; Orange for “Limited Progress”, and Red for “No Progress”. An arrow in the color box indicates that the color score either went up or down from the prior year. If a recommended action was added since last year’s report, no color score has been assigned and the recommended action has been designated as “New”.

As part of the OIG’s continuing evaluation of the Management Challenges, certain Challenges have been updated or revised. In addition, actions that were scored Green last year, and which remained Green this year, have been moved up to the “history bar” above the recommended actions. The history bar highlights any progress that the agency has made on a Challenge over
the past four FYs (or as long as the Challenge has existed, if shorter) by showing the number of actions that have moved to Green each year.

The following table provides a summary of the FY 2012 Most Serious Management and Performance Challenges Facing SBA.

**Table 1: Summary of the FY 2012 Most Serious Management and Performance Challenges Facing SBA.**

<table>
<thead>
<tr>
<th>Challenge</th>
<th>Status at End of FY 2011</th>
<th>Change from Prior Year</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Green</td>
<td>Yellow</td>
</tr>
<tr>
<td>1 Small Business Contracting</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>2 IT Security</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>3 Human Capital</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>4 Loan Guaranty Purchase</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>5 Lender Oversight</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>8(a) BD Program</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>8 Loan Management and Accounting System</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>9 Improper Payments</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>4</td>
<td>11</td>
</tr>
</tbody>
</table>

We would like to thank SBA’s management and staff for their cooperation in providing us with information needed to prepare this report. We look forward to continuing to work with SBA’s leadership team in addressing the agency’s Management Challenges.
Contents

Challenge 1. Procurement flaws allow large firms to obtain small business awards and agencies to count contracts performed by large firms towards their small business goals. ................................................................. 1

Challenge 2. Weaknesses in information systems security controls pose significant risks to the agency. 2

Challenge 3. Effective human capital strategies are needed to enable SBA to carry out its mission successfully and become a high-performing organization. ................................................................. 3

Challenge 4. SBA needs to implement a quality assurance program in its loan centers. ................................. 4

Challenge 5. SBA needs to further strengthen its oversight of lending participants. ......................................... 5

Challenge 6. The Section 8(a) Business Development program needs to be modified so more firms receive business development assistance, standards for determining economic disadvantage are justifiable, and SBA ensures that firms follow 8(a) regulations when completing contracts. .................. 6

Challenge 7. Effective tracking and enforcement would reduce financial losses from loan agent fraud. .. 7

Challenge 8. SBA needs to modernize its Loan Accounting System and migrate it off the mainframe. ..... 8

Challenge 9. SBA needs to accurately report, significantly reduce, and strengthen efforts to recover improper payments in the Disaster and 7(a) loan programs................................................................. 9

Appendix: Relevant Reports.................................................................................................................................. 10
The Small Business Act establishes a government-wide goal that 23 percent of the total value of all prime contract awards for each FY be awarded to small businesses. As the advocate for small business, SBA should strive to ensure that only small firms obtain and perform small business awards and that procuring agencies accurately report contracts awarded to small businesses when representing its progress in meeting small business contracting goals.

OIG audits and other governmental studies have shown widespread misreporting by procuring agencies since many contract awards that were reported as going to small firms have actually been performed by larger companies. While some contractors may misrepresent or erroneously calculate their size, most of the incorrect reporting results from errors made by government contracting personnel, including misapplication of small business contracting rules. In addition, contracting officers do not always review the on-line certifications that contractors enter into a governmental database prior to awarding contracts. SBA needs to ensure that contracting personnel are adequately trained on small business procurement and are reviewing this database prior to awarding contracts.

SBA also needs to address a loophole within General Services Administration (GSA) Multiple Awards Schedule (MAS) contracts that contain multiple industrial codes. Currently, a company awarded such a contract can identify itself as small on individual task orders awarded under that contract even though it does not meet the size criteria for the applicable task. Thus, agencies may obtain small business credit for using a firm classified as small, when the firm is not small for specific orders under the MAS contract.

SBA has made mixed progress on this challenge. In FY 2011, SBA progressed to a “Green” rating for its efforts to develop a program to ensure that contracting personnel are reviewing contractor size certifications. However, although they have been working on the development of training programs on small business procurement for contracting personnel, updated courses have not been implemented. SBA also has committed to improving the surveillance review process in response to an OIG audit to enhance its oversight of contract awards and performance on set-aside contracts, but has yet to implement tangible changes. SBA also made limited progress during FY 2011 in developing regulations to correct misapplication of industry codes on long-term and multiple award set-aside contracts.

<table>
<thead>
<tr>
<th>Challenge History</th>
<th>Actions Accomplished (Green Status) during Past 4 FYs</th>
<th>Status at end of FY 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fiscal Year (FY) Issued: 2005</td>
<td>07-0</td>
<td>08-1</td>
</tr>
<tr>
<td><strong>Recommended Actions for FY 2012</strong></td>
<td></td>
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<tr>
<td>1. Develop and take steps to provide reasonable assurance that agencies are providing adequate basic and continuing education training to contracting personnel on small business contracting procedures.</td>
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<tr>
<td>2. Revise the surveillance review process to ensure that they are conducted in a thorough and consistent manner</td>
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<tr>
<td>3. Develop and implement a program that promotes accurate contractor certifications and ensures that contracting personnel review contractor certifications. <em>(Previously action #2)</em></td>
<td>Green ↑</td>
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<tr>
<td>4. Issue regulations that require firms to meet the size standard for each specific order they receive under a GSA schedule and Government-wide Acquisition Contract (GWAC) and show that the regulations are being followed. <em>(Previously action #3)</em></td>
<td>Orange</td>
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</tbody>
</table>

Green - Implemented; Yellow - Substantial Progress; Orange - Limited Progress; Red - No Progress
Challeng Challenge 2. Weaknesses in information systems security controls pose significant risks to the agency.

The confidentiality, integrity, and availability of SBA’s information systems are vital to the continued successful operation of the agency. While information technology (IT) can result in a number of benefits, such as information being processed more quickly and communicated almost instantaneously, it can also increase the risk of fraud, inappropriate disclosure of sensitive data, and disruption of critical operations and services. SBA’s computer security program operates in a dynamic and highly decentralized environment and requires management attention and resources as weaknesses are identified.

SBA improved in information system security in some critical areas during FY 2011. SBA updated procedures disallowing users to connect unauthorized devices to the network and implemented network access controls at SBA headquarters and has plans to extend network access controls to SBA field offices. The Chief Information Security Officer instituted a review of all Plan of Action and Milestones (POA&M) for SBA IT systems and began acquisition of an application to manage SBA’s IT systems.

To show further progress, SBA needs to address both known and newly reported information security issues. For example, SBA needs to demonstrate a process that accomplishes timely mitigation of system risks that are identified as “medium” and “high;” enforce an enterprise-wide configuration management process; and ensure segregation of duties controls are in place and operating for all of its systems. SBA has improved in some areas, however, the FY 2011 Financial Statement Audit has identified new weaknesses and findings and are also anticipated for the FY 2011 Federal Information Security Management Act (FISMA) review.

<table>
<thead>
<tr>
<th>Challenge History</th>
<th>Actions Accomplished (Green Status) during Past 4 FYs</th>
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<tr>
<td>Fiscal Year (FY) Issued: 1999</td>
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<td></td>
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<tr>
<td></td>
<td>07-2</td>
<td>08-2</td>
</tr>
<tr>
<td>1. Access controls are in place and operating effectively, and contractors are not granted system access until they have obtained the required background investigations and/or security clearances.</td>
<td></td>
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<tr>
<td>2. System software controls are in place and operating effectively.</td>
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<tr>
<td>3. Segregation of duty controls are in place and operating effectively.</td>
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<tr>
<td>4. The POA&amp;M accurately reports all computer security weaknesses and corrective actions.</td>
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<tr>
<td>5. The IT security management program is effective to address information security in systems that support the operations and assets of the organization.</td>
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</table>

Green—Implemented Yellow—Substantial Progress Orange—Limited Progress Red—No Progress
During the past decade, facing budget constraints at the same time that virtually all of its programs were growing significantly, SBA restructured key agency operations, reengineered its largest loan programs, and downsized personnel levels. While these actions transformed the way SBA does business, the agency has not adequately analyzed priorities and allocated resources consistent with those priorities and its new business processes. As a result, there is no assurance that sufficient resources—in terms of both numbers of staff and the knowledge and skills possessed by the staff—are available and appropriately deployed to perform critical functions.

A recent review by the U.S. Office of Personnel Management (OPM) identified weaknesses in SBA’s human capital policies and practices that highlight the serious human capital challenges facing the agency. The review found that SBA did not meet over 40 percent of expected outcomes across five Human Capital Assessment and Accountability Framework (HCAAF) areas—Strategic Alignment, Leadership and Knowledge Management, Results-Oriented Performance Culture, Talent Management, and Accountability. OPM traced many of the problems to the absence of an OPM-approved human capital accountability system and a lack of leadership and direction when it comes to the strategic management of human capital at SBA. For example, the OPM found that SBA’s human capital policies and procedures were not aligned with the organizational objectives and strategic goals in its FY 2011-2016 Strategic Plan. Further, there was no evidence that SBA engaged in any recent agency-wide workforce planning or competency gap analyses to estimate the staffing and skill levels needed to achieve the agency’s performance goals and mission.

The results of the Federal Human Capital Surveys—now called the Employee Viewpoint Survey (EVS)—also have highlighted SBA’s serious human capital challenges. SBA has consistently ranked near the bottom on all four human capital indices—Leadership and Knowledge Management, Results-Oriented Performance Culture, Talent Management, and Job Satisfaction. While the agency showed some improvement in the 2011 EVS, it still fell below the government wide average on the four human capital indices. In addition, SBA was 29 out of 31 large agencies in the Partnership for Public Service’s 2010 “Best Places to Work” rankings (the 2011 rankings will be available in November 2011).

### Challenge History
**Fiscal Year (FY) Issued:** 2001 (Revised 2007)

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<tr>
<th>Challenge History</th>
<th>Actions Accomplished (Green Status) during Past 4 FYs</th>
<th>Recommended Actions for FY 2012</th>
<th>Status at end of FY 2011</th>
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<tbody>
<tr>
<td><strong>Recommended Actions for FY 2012</strong></td>
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<tr>
<td>1. Ensure the agency has an effective, comprehensive workforce and succession plan that aligns talent needs and capabilities with SBA’s FY 2011-2016 Strategic Plan. SBA’s workforce and succession planning goals should reflect the need to recruit and retain the appropriate talent, and should establish appropriate metrics to gauge SBA’s success at having the right people, in the right jobs, at the right time. <em>(Previously action #3)</em></td>
<td></td>
<td>Red ↓</td>
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<tr>
<td>2. Ensure the Office of Human Capital Management (OHCM) is structured and equipped so as to add value by delivering needed strategic support and services such as continuity planning, talent management, organizational development, and strategic consulting to implement the agency’s human capital plan and its mission.</td>
<td></td>
<td>New</td>
<td></td>
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<tr>
<td>3. Ensure that Human Capital Management Standard Operating Procedures (SOPs) are updated and appropriately structured to support the agency’s long-term goals and objectives and government-wide Human Capital Management initiatives.</td>
<td></td>
<td>New</td>
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<tr>
<td>4. Take steps to correct problems identified in the 2010 EVS. Demonstrate improvement by increasing overall scores/agency rankings in the 2011 EVS. <em>(Previously action #2)</em></td>
<td></td>
<td>Yellow</td>
<td></td>
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*Green*-Implemented *Yellow*-Substantial Progress *Orange*-Limited Progress *Red*-No Progress
The initial focus of this challenge was on improving deficiencies identified in SBA loan liquidation and guaranty purchase processes. Over the last decade, the agency has made significant progress to improve these processes at its loan centers, but a significant deficiency continues to exist in the area of quality assurance.

The Office of Financial Program Operations has made progress in developing a Quality Assurance Review (QAR) program for all of its loan centers to verify and document compliance with the loan process, from origination to close-out, and to identify where material deficiencies may exist so that remedial action can be taken. A QAR project guide has been developed and agreed upon by relevant parties within the Office of Capital Access. The QAR program will assess the overall quality of the centers’ deliverables to provide confidence to its stakeholders. SBA hired a quality control (QC) manager to oversee the development of the program and identified a QC specialist for each center. Furthermore, a QC team was established and has (1) identified existing processes and ranked the functions within the centers as high, moderate and low risk, (2) identified and ranked critical areas that the centers will focus on for quality control, and (3) developed and documented Quality Program Manuals for each center. The QC team has also developed and implemented checklists for each critical center function and developed quality and risk element databases to be utilized for quality metrics.

While SBA has made substantial progress in its development of a quality assurance program, additional work remains before SBA can demonstrate that all elements of the program are being completed and followed. For example, an ongoing audit found that the early default QAR checklist used at the National Guaranty Purchase Center does not require an adequate review of lender compliance with material loan origination and closing requirements including eligibility, creditworthiness, and use of loan proceeds. Prior OIG audits identified material noncompliance in these areas, which resulted in improper payments and significant loss to SBA. Therefore, a thorough review of eligibility, creditworthiness, and use of loan proceeds is critical to the quality of the center’s deliverables and the integrity of the 7(a) loan program.

<table>
<thead>
<tr>
<th>Challenge History</th>
<th>Fiscal Year (FY) Issued: 2001</th>
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<tr>
<td></td>
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<td>07-0</td>
<td>08-2</td>
<td>09-0</td>
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</tbody>
</table>

Green - Implemented Yellow - Substantial Progress Orange - Limited Progress Red - No Progress
Challenge 5. SBA needs to further strengthen its oversight of lending participants.

Since its inception in 1953, SBA has loaned or guaranteed billions of dollars to finance and spur investment in small businesses. In fiscal year 2011, approximately 67 percent of the 7(a) loan dollars guaranteed by SBA were made by lenders using delegated authorities with limited oversight. Prior OIG and GAO reports, including an OIG report issued in May 2008 disclosed that (1) onsite lender examinations did not adequately assess lender risk and were limited in scope, (2) reviews were not conducted of high-risk, medium sized lenders, and (3) SBA did not take adequate risk mitigation measures to hold lenders accountable for their performance. High-risk lenders account for approximately 35 percent of SBA’s 7(a) outstanding loan dollars made by active lenders. The risks inherent in delegated lending require an effective oversight program to (1) monitor lenders compliance with SBA policies and procedures, and (2) take corrective actions when a material noncompliance is detected.

The agency has made significant progress in its oversight of lenders in its 7(a) and 504 loan programs since this management challenge was created in 2001. For example, SBA expanded the scope of its oversight by more than doubling the number of on-site reviews of large high-risk lenders. In September 2006, the agency issued SOP 51 00, On-site Lender Reviews and Examinations, to guide the on-site review process. The agency also modified its Lender Risk Rating System to further strengthen lender risk assessments. In October 2010, SBA issued SOP 50 53, Lender Supervision and Enforcement, which established an oversight framework including enforcement actions to be taken against lenders with unacceptable performance. SBA also recently completed its risk management assessment and plans to (1) re-stratify its oversight activities to better target high-risk lenders and Certified Development Companies (CDCs), (2) expand its assessment of risk, and (3) use statistical samples so that onsite review results can be extrapolated to the lenders’ total portfolios.

Although the agency has made progress, it needs to demonstrate consistent adherence to its procedures and ensure that corrective action plans effectively address material noncompliance and actually improves the performance of high-risk lenders.

<table>
<thead>
<tr>
<th>Challenge History Fiscal Year (FY) Issued: 2001</th>
<th>Actions Accomplished (Green Status) during Past 4 FYs</th>
<th>Status at end of FY 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Recommended Actions for FY 2012</td>
<td></td>
<td></td>
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<tr>
<td>1. Expand the scope of lender oversight and improve the process for reviewing lenders and CDCs for compliance risks.</td>
<td>07-7(a)-0 07-504-1 08-7(a)-2 08-504-2 09-7(a)-0 09-504-0 10-7(a)-0 10-504-0</td>
<td>Yellow  Yellow</td>
</tr>
<tr>
<td>2. Implement guidance providing for effective oversight of lending programs.</td>
<td></td>
<td>Yellow  Yellow</td>
</tr>
<tr>
<td>3. Ensure that effective corrective actions are implemented, monitored, and result in improvement in the performance of participants with unacceptable performance.</td>
<td></td>
<td>Orange  Orange</td>
</tr>
</tbody>
</table>

Green=Implemented Yellow=Substantial Progress Orange=Limited Progress Red=No Progress
**Challenge 6. The Section 8(a) Business Development program needs to be modified so more firms receive business development assistance, standards for determining economic disadvantage are justifiable, and SBA ensures that firms follow 8(a) regulations when completing contracts.**

SBA’s 8(a) Business Development (BD) program was created to assist eligible small disadvantaged business concerns to compete in the American economy through business development.

Previously, the agency did not place adequate emphasis on business development to enhance the ability of 8(a) firms to compete, and did not adequately ensure that only 8(a) firms with economically disadvantaged owners in need of business development remained in the program. Companies that were “business successes” were allowed to remain in the program and continue to receive 8(a) contracts, causing fewer companies to receive most of the 8(a) contract dollars and many to receive none.

SBA made progress in the past towards addressing issues raised by this management challenge that hinder the agency’s ability to deliver an effective 8(a) program. This progress included increased training of relevant SBA personnel, improvements in the agency’s ability to provide business development skills to program participants, and taking steps to ensure that owners of 8(a) firms that were no longer economically disadvantaged were removed from the program. However, during the past year it regressed. The BD Office had developed a data base (the BD Assessment Tool) to track participant progress, but it has now concluded that the system does not provide the best way to measure business success. Accordingly, SBA is planning to award a contract shortly to develop and deploy a new system to provide SBA employees to monitor program participants, which it expects to deploy by December 2012. SBA took a positive step by revising its regulations in March 2011 to ensure that companies that are “business successes” are graduated out of the program, and by working to update its SOP for the BD program to reflect these regulatory changes. The new regulations also establish additional standards to address the definition of “economic disadvantage,” however, the agency has not provided an economic analysis to justify these standards. A recent OIG audit also found that the agency was not effectively performing surveillance reviews to determine whether contracting activities complied with small business and 8(a) requirements. SBA needs to update the relevant SOP governing surveillance reviews for the BD program.

<table>
<thead>
<tr>
<th>Challenge History</th>
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<th>Status at end of FY 2011</th>
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<tbody>
<tr>
<td>Fiscal Year (FY) Issued: 2007</td>
<td>07-1</td>
<td>08-1</td>
</tr>
<tr>
<td><strong>Recommended Actions for FY 2012</strong></td>
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<tr>
<td>1. Develop and implement a plan, including SOP provisions, which ensures that the 8(a) BD program identifies and addresses the business development needs of program participants on an individualized basis.</td>
<td>Orange ↓</td>
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<tr>
<td>2. Develop and implement Regulations and SOP provisions to ensure that participants are graduated once they reach the levels defined as business success.</td>
<td>Yellow</td>
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<tr>
<td>3. Establish objective and reasonable criteria that effectively measures “economic disadvantage” and implement the new criteria.</td>
<td>Red ↓</td>
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<tr>
<td>4. On a regular basis, conduct surveillance reviews of procuring agencies to ensure they are effectively monitoring and enforcing compliance with specified 8(a) BD regulations on the contracts they administer.</td>
<td>Orange ↓</td>
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</table>
For more than a decade, OIG investigations have revealed a pattern of fraud in the 7(a) business loan guaranty program by loan packagers and other for-fee agents. Fraudulent schemes have involved hundreds of millions of dollars, yet SBA oversight of loan agents has been limited, putting taxpayer dollars at risk. The agency could reduce this risk by establishing effective loan agent disclosure requirements, a database or equivalent means to track loan agent involvement with its loans, and a more effective agent enforcement program.

Tracking Loan Agent Data. Over the years, in response to this Management Challenge, SBA has proposed various methods of tracking loan agent activity. At one point, SBA proposed to revise its E-Tran system (which collects loan data electronically from participating lenders) to collect loan agent information. The agency later concluded that this approach was not feasible. At the end of FY 2007, SBA proposed a new approach to integrate information from the Form 159 (which asks for information about loan agents) into the Form 1502 electronic data collection process by SBA’s Fiscal and Transfer Agent (FTA). The OIG revised recommended action #1 below, but SBA made no progress on it during FY 2008, in part due to a protest of the award of the FTA contract. At the end of FY 2009, SBA presented a succinct plan for implementing the 1502 approach. However, during FY 2010, SBA again changed its position, and advised that it would capture the data by having the Form 159 faxed to the FTA. At the end of FY 2010, SBA issued a notice with directions on how this data was to be submitted. During FY 2011, the agency instructed lenders how to submit Form 159 data (including loan identification numbers) to the FTA, analyzed the data, and updated loan review guidance so that the Office of Credit Risk Management (OCRM) could identify loan agent-related problems. Although loan agent data does not appear in the Loan Accounting System (LAS), SBA officials stated that it could be linked to LAS through a virtual database. It is not yet clear whether such a process would be user-friendly for non-technical users. Finally, SBA issued the loan agent data collection requirement in an SOP effective October 1, 2011.

Loan Agent Enforcement Procedures. In FY 2007, the agency made progress by issuing its Lender Oversight SOP and by previously revising the guaranty purchase checklist (which lists the records that lenders need to provide when requesting SBA to pay a guaranty) to include the submission of the Form 159. However, the agency also needed to establish a more effective enforcement program to deter fraudulent loan agent activity. Effective October 1, 2010, SBA issued a Lender Supervision and Enforcement SOP with provisions for loan agent enforcement actions and a delegation of authority to the Director of OCRM. However, the agency recently advised that this SOP needed to be revised to implement more effective procedures.

**Challenge History**  
**Fiscal Year (FY) Issued: 2000**

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<tr>
<th>Actions Accomplished (Green Status) during Past 4 FYs</th>
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<th>08-1</th>
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<th>10-0</th>
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<tbody>
<tr>
<td><strong>Recommended Actions for FY 2012</strong></td>
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<tr>
<td>1. Develop an effective method of disclosing and tracking loan agent involvement in SBA business loan programs.</td>
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<tr>
<td>2. Implement procedures for enforcement actions against loan agents for improper and fraudulent conduct.</td>
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</table>

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

Challenge 7. Effective tracking and enforcement would reduce financial losses from loan agent fraud.
In November 2005, SBA initiated the Loan Management and Accounting System (LMAS) project to update the agency’s Loan Accounting System and migrate it off of the mainframe. Previous OIG reports noted that the system was close to the end of its expected useful life, relied on obsolete technology, contained major security vulnerabilities that could not be addressed until the system was moved to a new operating platform, and was costly to operate. Additionally, the OIG reported concerns about SBA’s management of the project; the project’s noncompliance with the agency’s System Development Methodology (SDM) in key areas, which impacts SBA’s ability to control project costs and quality; and the lack of an enterprise-wide or project-level Quality Assurance (QA) function to ensure that LMAS deliverables met SBA’s requirements and quality standards. Finally, the OIG reported that the LMAS QA contractor had not performed all of the activities stipulated in its contract and that none of the issued LMAS task orders had undergone Independent Validation and Verification (IV&V) testing.

In 2009, SBA contracted with McKinsey & Company to conduct a review of the LMAS project. This review identified multiple weaknesses in SBA’s LMAS project management activities and recommended (1) focusing on core mainframe legacy platform replacement, (2) strengthening project governance, (3) increasing project team resources, (4) focusing on COTS capabilities while minimizing customization, and (5) improving vendor management.

In 2010, OMB issued Memorandum 10-26, recommending that Federal agencies split large-scale modernization efforts into smaller, simpler segments with clear deliverables. In response, SBA changed its strategy for LMAS going forward to accelerate the migration of user interfaces from the mainframe legacy platform to the agency’s current architecture, and convert batch COBOL systems from the mainframe to a more current and platform-independent environment. SBA staffed its IT QA function and created a new SOP to provide guidance for its IT QA program. However, to show further progress, SBA needs to implement its QA/IV&V process that encompasses all of the requirements of its enterprise SDM, and provide sufficient evidence that all LMAS work products undergo IV&V activities in accordance with the agency’s Enterprise Quality Assurance Plan.

### Challenge History

**Fiscal Year (FY) Issued: 2010**

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<thead>
<tr>
<th>Actions Accomplished (Green Status) during Past 4 FYs</th>
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</thead>
<tbody>
<tr>
<td>N/A</td>
<td>N/A</td>
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<table>
<thead>
<tr>
<th><strong>Recommended Actions for FY 2012</strong></th>
<th><strong>Status at end of FY 2011</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Migrate LAS to a new operating platform before the current mainframe contract expires in 2012.</td>
<td>Orange</td>
</tr>
<tr>
<td>2. Modify the LMAS QA/IV&amp;V contract and establish an effective Quality Assurance (QA) process which provides senior management independent assurance that LMAS development activities and related project deliverables meet SBA Quality standards.</td>
<td>Orange</td>
</tr>
<tr>
<td>3. Establish a process for reviewing and accepting LMAS deliverables that complies with Systems Development Methodology requirements.</td>
<td>Orange</td>
</tr>
<tr>
<td>4. Implement a Quality Assurance process in LMAS in accordance with SBA’s Enterprise Quality Assurance Plan.</td>
<td>Orange</td>
</tr>
</tbody>
</table>

- **Green** - Implemented
- **Yellow** - Substantial Progress
- **Orange** - Limited Progress
- **Red** - No Progress
OIG audits of SBA’s Disaster and 7(a) Loan programs determined that the improper payment rates reported for these programs were significantly understated. SBA estimated that improper payments in the Disaster Loan program were about $4.5 million, or 0.55 percent of loans approved in FY 2007, while the OIG reported that it was at least 46 percent, or approximately $1.5 billion. SBA also reported that the improper payment rate for 7(a) purchases was 0.53 percent of FY 2008 program outlays, although the OIG estimated the rate to be 27 percent, or approximately $234 million. SBA’s improper payment rates were understated because the agency did not adequately review sampled loans, used flawed sampling methodologies, and did not accurately project review findings for both programs. Additionally, the Office of Financial Assistance (OFA) inappropriately overturned improper payments identified by reviewers.

OIG audits in prior years have also identified high percentages of disaster and business loans that were made to borrowers who were ineligible, lacked repayment ability, or did not provide the required support for loan disbursement. In 2009, we reported that over 30 percent of reviewed disaster loans were disbursed for properties that were not the applicant’s primary residence and identified an estimated $30 million in improper loan guaranty purchases in the 7(a) program. Furthermore, a recent OIG audit estimated that at least 1,196 7(a) Recovery Act loans were not originated and closed in compliance with SBA requirements, resulting in at least $869.5 million in inappropriate or unsupported loan approvals. SBA also has not aggressively pursued recovery of 7(a) improper payments.

The Office of Capital Access (OCA) has taken actions to correct many of the deficiencies identified by the OIG. For example, the agency has (1) acquired a statistician to ensure its sample selection and projection of results are in compliance with Office of Management and Budget (OMB) requirements, (2) established a pilot program for disputed denial, repair and improper payment decisions on 7(a) loans, and (3) developed and implemented a corrective action plan. However, additional actions are needed to accurately report, significantly reduce, and recover improper payments. OCA needs to incorporate into formal policy (1) the improper payment review processes, (2) the denial, repair and improper payment dispute resolution process, and (3) the improper payment recovery process. Furthermore, while OCA and the Office of Disaster Assistance (ODA) have acceptable corrective action plans in place, they need to demonstrate that the corrective action plans are effective in reducing improper payments in the 7(a) and Disaster Loan programs.

<table>
<thead>
<tr>
<th>Challenge History Fiscal Year (FY) Issued: 2010</th>
<th>Actions Accomplished (Green Status) during Past 4 FYs</th>
<th>Status at end of FY 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Recommended Actions for FY 2012</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Ensure that processes used to calculate the improper payment rate for disaster and 7(a) loans are designed to effectively identify improper payments as defined by OMB Circular A-123.</td>
<td>N/A</td>
<td>Green↑ Orange</td>
</tr>
<tr>
<td>2. Reassign responsibility for final approval of disputed denial, repair, and improper payment decisions from OFA to OCRM to ensure an adequate and timely resolution of disputes.</td>
<td>N/A</td>
<td>Orange</td>
</tr>
<tr>
<td>3. Develop and implement corrective action plans to reduce improper payments in the 7(a) and Disaster Loan programs. (Previously action #4)</td>
<td>Green↑</td>
<td>Green↑</td>
</tr>
<tr>
<td>4. Establish a process and time standards to expeditiously recover improper payments identified during agency reviews and OIG audits. (Previously action #5)</td>
<td>N/A</td>
<td>Orange</td>
</tr>
<tr>
<td>5. Demonstrate that corrective action plans are effective in reducing improper payments in the 7(a) and Disaster Loan programs.</td>
<td>New</td>
<td>New</td>
</tr>
</tbody>
</table>

Green—Implemented Yellow—Substantial Progress Orange—Limited Progress Red—No Progress
Appendix: Relevant Reports

Most of the SBA OIG Reports listed can be found at http://www.sba.gov/office-of-inspector-general.

Challenge 1:

- SBA OIG, SBA’s Planning and Award of the Customer Relationship Management Contracts, ROM 10-16, June 29, 2010.
- The Center for Public Integrity, The Big Business of Small Business: Top defense contracting companies reap the benefits meant for small businesses, September 29, 2004.

Challenge 2:

- SBA OIG, Audit of SBA’s FY 2010 Financial Statements, Report 11-03, November 12, 2010
- SBA OIG, Audit of SBA’s Financial Statements for FY 2006, Report #7-03, November 15, 2006
- SBA OIG, Audit of SBA’s Information System Controls for FY 2004, Report #5-12, February 24, 2005

Challenge 3:

- OPM, 2011 Federal Employee Viewpoint Survey
- Partnership for Public Service, Best Places to Work in the Federal Government 2010
- OPM, 2010 Federal Employee Viewpoint Survey
- SBA OIG, Adequacy of Procurement Staffing and Oversight of Contractors Supporting the Procurement Function, ROM 10-13, April 9, 2010
- SBA OIG, SBA’s Administration of the Microloan Program under the Recovery Act, ROM 10-10, December 28, 2009
- Partnership for Public Service, Best Places to Work in the Federal Government 2009
- OPM, 2008 Federal Human Capital Survey
- GAO, Agency Should Assess Resources Devoted to Contracting and Improve Several Processes in the 8(a) Program, GAO-09-16, November 2008
- GAO, Opportunities Exist to Build on Leadership’s Efforts to Improve Agency Performance and Employee Morale, GAO-08-995, September 2008
- SBA OIG, Non-Native Managers Secured Millions of Dollars from 8(a) Firms Owned by Alaska Native Corporations through Unapproved Agreements that Jeopardize the Firms’ Program Eligibility, Report #8-14, August 7, 2008
- GAO, Opportunities Exist to Improve Oversight of Women’s Business Centers and Coordination Among SBA’s Business Assistance Programs, GAO-08-49, November 2007
- SBA OIG, Audit of Two 8(a) Sole-Source Contracts Awarded to Contractors in SBA’s Mentor Protégé Program, Report #7-19, March 30, 2007
- SBA OIG, Management Advisory Report on the Transfer of Operations to the National Guaranty Purchase Center, Report #4-39, August 31, 2004
- GAO, Results Oriented Cultures: Implementation Steps to Assist Mergers and Organizational Transformations, GAO-03-699, July 2003
- GAO, Small Business Administration: Workforce Transformation Plan is Evolving, GAO-02-931T, July 16, 2002
- GAO, Small Business Administration: Current Structure Presents Challenges for Service Delivery, GAO-02-17, October 2001
- GAO, Small Business Administration: Steps Taken to Better Manage its Human Capital, but More Needs to be Done, GAO/T-GGD/AIMD-00-256, July 20, 2000
- SBA OIG, A Framework for Considering the Centralization of SBA Functions, November 1996

**Challenge 4:**

- SBA OIG, Origination and Closing Deficiencies Identified In 7(a) Recovery Act Loan Approvals, Report #11-07, September 30, 2011
- SBA OIG, Material Deficiencies Identified in Five 7(a) Recovery Act Loans Resulted in $2.7 Million of Questioned Costs, Report #11-06, August 25, 2011
- SBA OIG, Banco Popular Did Not Adequately Assess Borrower Repayment Ability When Originating Huntington Learning Center Franchise Loans, Report #11-16, July 13, 2011
- SBA OIG, Material Deficiencies Identified in Four 7(a) Recovery Act Loans Resulted in $3.2 Million of Questioned Costs, Report #11-05, June 29, 2011
- SBA OIG, Material Deficiencies Identified in Early-Defaulted and Early-Problem Recovery Act Loans, #10-19, September 24, 2010
- SBA OIG, SBA’s Management of the Backlog of Post-purchase Reviews at the National Guaranty Purchase Center, #9-18, August 25, 2009
- SBA OIG, The Small Business Administration’s Fiscal Year 2008 Improper Payment Rate for the 7(a) Guaranty Loan Program #9-16, July 10, 2009
- SBA OIG, Review of Key Unresolved OIG Audit Recommendations in Program Areas Funded by the American Recovery and Reinvestment Act and Related Activities Need to Safeguard Funds, #ROM 09-1, April 30, 2009
- SBA OIG, Audit of the Liquidation Process at the National Guaranty Purchase Center, #9-08, January 30, 2009
- SBA OIG, Audit of Six SBA Guaranteed Loans, #8-18, September 8, 2008
- SBA OIG, Audit of Loan Classifications and Overpayments on Secondary Market Loans, #8-09, March 26, 2008
- SBA OIG, Audit of UPS Capital Business Credit’s Compliance with Selected 7(a) Lending Requirements, #8-08, March 21, 2008
• SBA OIG, Audit of the Guarantee Purchase Process for Section 7(a) Loans at the National Guaranty Purchase Center, Report #7-23, May 8, 2007
• SBA OIG, Survey of the Quality Assurance Review Process, Report #6-26, July 12, 2006
• SBA OIG, Audit of SBA’s Implementation of the Improper Payments Information Act, Report #6-25, June 21, 2006
• SBA OIG, Management Advisory Report on the Transfer of Operations to the National Guaranty Purchase Center, Report #4-39, August 31, 2004
• SBA OIG, Improvements are Needed in Small Business Lending Company Oversight Process, Report #2-12, March 21, 2002
• GAO, Major Management Challenges and Program Risks, GAO-01-260, January 2001

Challenge 5:

• SBA OIG, SBA’s Oversight of SBA Supervised Lenders, Report #8-12, May 9, 2008
• SBA OIG, UPS Capital Compliance with Selected 7(a) Lending Requirements, Report #8-08, March 21, 2008
• GAO, Small Business Administration: Additional Measures Needed to Assess 7(a) Loan Program’s Performance, GAO-07-769, July 13, 2007
• GAO, Small Business Administration: Improvements Made, But Loan Programs Face Ongoing Management Challenges, GAO-06-605T, April 6, 2006
• SBA OIG, SBA’s Administration of the Supplemental Terrorist Activity Relief (STAR) Loan Program, Report #6-09, December 23, 2005
• GAO, Continued Improvements Needed in Lender Oversight, Report #03-90, December 2002
• SBA OIG, Impact of Loan Splitting on Borrowers and SBA, Advisory Memorandum Report #2-31, September 30, 2002
• SBA OIG, Improvements needed in SBLC Oversight, Advisory Memorandum Report, #2-12, March 20, 2002
• SBA OIG, Preferred Lender Oversight Program, Report #1-19, September 27, 2001
• SBA OIG, SBA Follow-up on SBLC Examinations, Report #1-16, August 17, 2001

Challenge 6:

• SBA OIG, Audit on the Effectiveness of the SBA’s Surveillance Review Process, Report # 11-11, March 31, 2011
• SBA OIG, Audit of Two 8(a) Sole –Source Contracts Awarded to Contractors in SBA’s Mentor Protégé Program, Report #7-19, March 30, 2007
• SBA OIG, Audit of Monitoring Compliance with 8(a) Business Development Regulations During 8(a) Business Development Contract Performance, Report #6-15, March 16, 2006
• SBA OIG, Business Development Provided by SBA’s 8(a) Business Development Program, Report #4-22, June 2, 2004.
• SBA OIG, SACS/MEDCOR: Ineffective and Inefficient, Report #4-15, March 9, 2004
• SBA OIG, Section 8(a) Program Continuing Eligibility Reviews, Report #4-3-H-006-021, September 30, 1994

12
Challenge 7:

- SBA OIG, Applicant Character Verification in SBA’s Business Loan Program, Report #3-43, April 5, 2001
- SBA OIG, Summary Audit of Section 7(a) Loan Processing, Report #0-03, January 11, 2000
- SBA OIG, Loan Agents and the Section 7(a) Program, Report #98-03-01, March 31, 1998
- SBA OIG, Fraud Detection in SBA Programs, Report #97-11-01, November 24, 1997
- SBA OIG, Operation Cleansweep Memorandum, August 21, 1996

Challenge 8:

- SBA OIG, Adequacy of Quality Assurance Oversight of the Loan Management and Accounting System Project, Report 10-14, September 13, 2010
- SBA OIG, Review of Allegations Concerning How the Loan Management and Accounting System Modernization Project is Being Managed, Report #9-17 July 30, 2009
- SBA OIG, SBA Needs to Implement a Viable Solution to its Loan Accounting System Migration Problem, Report #5-29, September 20, 2005 – all recommendations closed
- GAO, Major Management Challenges and Program Risks: Small Business Administration, GAO-03-116, January 1, 2003
- GAO, SBA Loan Monitoring System: Substantial Progress Yet Key Risks and Challenges Remain, Testimony of Joel C. Willemssen, Director, Civil Agencies Information Systems Accounting and Information Management Division, Before the Subcommittee on Government Programs Statement Committee on Small Business, House of Representatives, GAO/T-AIMD-00-113, February 29, 2000
- GAO, SBA Needs to Establish Policies and Procedures for Key IT Processes, Accounting and Information Management Division, GAO/AIMD-00-170, May 31, 2000

Challenge 9:

- SBA OIG, Origination and Closing Deficiencies Identified In 7(a) Recovery Act Loan Approvals, Report #11-07, September 30, 2011
- SBA OIG, Material Deficiencies Identified in Five 7(a) Recovery Act Loans Resulted in $2.7 Million of Questioned Costs, Report #11-06, August 25, 2011
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- SBA OIG, The Small Business Administration’s Fiscal Year 2008 Improper Payment Rate for the 7(a) Guaranty Loan Program, Report #9-16, July 10, 2009
- SBA OIG, Audit of Borrower Eligibility for Gulf Coast Disaster Loans, Report #9-09, March 31, 2009
- SBA OIG, The Small Business Administration’s Fiscal Year 2007 Improper Payment Rate for the Disaster Loan Program, Report #9-10, March 26, 2009
- SBA OIG, Audit of the Liquidation Process at the National Guaranty Purchase Center, Report #9-08, January 30, 2009
• SBA OIG, The Use of Proceeds From Gulf Coast Disaster Loans, Report #9-06, January 15, 2009
• SBA OIG, Disaster Loss Verification Process, Report #8-15, June 17, 2008
• SBA OIG, The Quality of Loans Processed Under the Expedited Disaster Loan Program, Report #7-34, September 28, 2007
• SBA OIG, Securing Collateral for Disaster Loan Disbursements, Report #7-22, May 9, 2007