U.S. Small Business Administration
Office of Inspector General

FY 2015 Congressional Budget Justification

Overview

In fulfillment of the Inspector General Act of 1978, as amended, the Small Business Administration (SBA) Office of Inspector General (OIG) provides auditing, investigative, and other services to support and assist the SBA in achieving its statutory mission, and provides taxpayers with a significant return-on-investment (ROI) as it roots out fraud, waste, and abuse in SBA's programs. During Fiscal Year (FY) 2013, the OIG achieved $348 million in monetary recoveries and savings—a more than a twenty-fold ROI.

The SBA was established to maintain and strengthen the nation's economy by protecting the interests of and assisting small businesses, and by helping families and businesses recover from disasters. While SBA's programs are essential to strengthening America's economy, the Agency faces a number of challenges in carrying out its mission. These include fraudulent schemes affecting SBA programs, significant losses from defaulted loans, procurement flaws that allow large firms to obtain small business awards, excessive improper payments, and outdated legacy information systems. The OIG plays a critical role in addressing these and other challenges by conducting audits to identify wasteful expenditures and program mismanagement, investigating fraud and other wrongdoing, and taking other actions to deter and detect waste, fraud, abuse, and inefficiencies in SBA programs and operations.

For FY 2015, the OIG requests $19.4 million, plus an additional $1.0 million to be transferred from the Disaster Loan program, for a total of $20.4 million. These resources are necessary to provide independent oversight of SBA's programs and operations, including continuation of an initiative to effectively target early defaulted loans for fraud and lender negligence.

With the funds requested for FY 2015, the OIG will:

- Work an active caseload of about 250 criminal and civil fraud investigations of potential loan and contracting fraud and other wrongdoing. Many of these investigations involve complex, multimillion dollar fraudulent financial schemes perpetrated by multiple suspects. (During FY 2013, OIG investigations resulted in 64 indictments/informations, 51 convictions, and almost $280 million in potential recoveries, fines, asset forfeitures, civil fraud settlements, or loans/contracts not being approved or being canceled.)

- Conduct audits and reviews of high-risk SBA activities with a focus on systemic, programmatic, and operational vulnerabilities. (During FY 2013, the OIG issued 19 reports with 129 recommendations for improving the Agency's operations, recovering improper payments, and reducing fraud and unnecessary losses in SBA programs.)

- Contract with an independent public accountant to perform the audit of the SBA's financial statements. (In FY 2015, the financial statement audit is projected to cost $2 million—10 percent of the OIG's budget request.)

- Provide oversight and monitoring of the SBA's information technology (IT) security and application development activities, including new systems under development and the Agency's compliance with the Federal Information Security Management Act (FISMA). The OIG has identified systemic problems with SBA's IT systems, and this remains one of the most serious management challenges facing the Agency.

- Maintain a robust Hotline operation to receive and process allegations of waste, fraud, abuse, or serious mismanagement in the SBA or its programs from employees, contractors, and the public. (During FY 2013, the Hotline processed 853 complaints, which were reviewed and analyzed by Hotline staff to determine the appropriate course of action. This represented almost a 60 percent increase over the previous year.)

- Through a Whistleblower Ombudsman established pursuant to the Whistleblower Protection Enhancement Act of 2012, educate SBA employees about prohibitions on retaliation for whistleblowing, as well as employees' rights and remedies if anyone retaliates against them for making a protected disclosure.

- Perform required background investigations of SBA employees to achieve a high level of integrity in the Agency's workforce. New Office of Personnel Management regulatory changes issued pursuant to Executive Order 13488 mandate that agencies reinvestigate individuals in public trust positions (both high risk and moderate risk) every five years. It is estimated that several hundred SBA employees will be required to undergo reinvestigation to meet this requirement, effectively increasing the OIG's workload.

- Adjudicate SBA employees and contractors for issuance of Personal Identity Verification (PIV) cards pursuant to Homeland Security Presidential Directive 12 (HSPD-12) background investigation requirements.

- Conduct name checks and, where appropriate, fingerprint checks on program applicants to prevent known criminals and wrongdoers from participating in SBA programs. (During FY 2013, more than $25 million in loans were not approved as a result of the OIG's name check program, effectively protecting the taxpayer from potential loss.)

- Review proposed revisions to SBA regulations, policies, procedures, and other directives with an emphasis on strengthening internal controls to preclude potential fraud and wasteful, confusing, or poorly planned initiatives. (During FY 2013, the OIG provided recommendations to improve 60 of the 115 proposed revisions it reviewed.)

- Recommend debarments, suspensions, and other administrative enforcement actions to foster integrity in SBA programs. (During FY 2013, the OIG recommended 65 administrative enforcement actions to the Agency.)

Budget Request

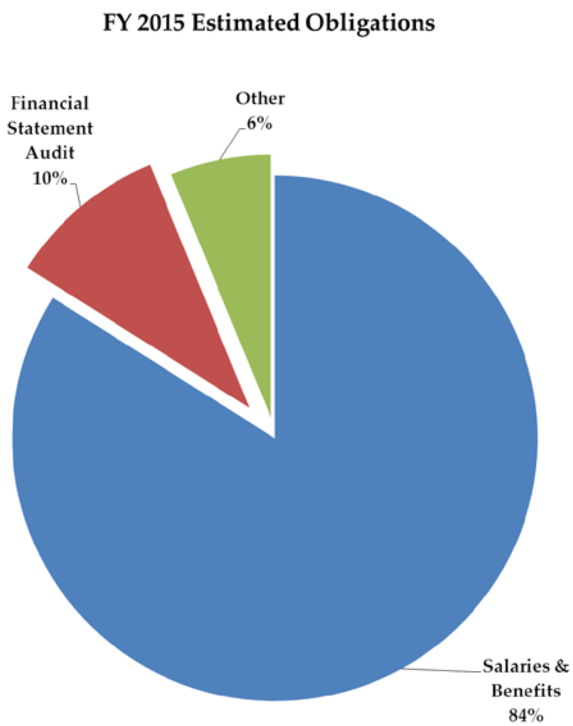
To address the challenges and risks discussed above and in the *Critical Risks* section below, the President's FY 2015 Budget requests a total of $20.4 million for the OIG—a direct appropriation of $19.4 million and $1.0 million to be transferred from the SBA's Disaster Loan program account for work on disaster program issues.

FY 2015 Budget Request

Dollars in Millions	FY 2013 Actual[1\]	FY 2014 Enacted	FY 2015 Request	FY 2015 Incr/Decr
New Budget Authority	$16.3	$19.0	$19.4	0.4
Transfer from Disaster Loan Program	1.0	1.0	1.0	--
Total	**$17.3**	**$20.0**	**$20.4**	**0.4**

1\ Amounts do not include impact of Sequestration, Across the Board Rescission, or funding provided under the Disaster Relief Appropriations Act of 2013.

The majority of the funds requested for FY 2015 will be used for salary and benefits for approximately 112 employees, as well as the cost of the annual audit of the SBA's financial statements by an independent public accountant.



Critical Risks Facing the SBA

Within available resources, the OIG must focus on the most significant risks to the SBA and the taxpayer. Some of the critical risks facing the SBA are discussed below. Many of these risks are addressed in the OIG's *Report on the Most Serious Management and Performance Challenges Facing the SBA*, which the OIG issues annually in accordance with the Reports Consolidation Act of 2000.

Risks Due to Limited Oversight and Controls in SBA Lending Programs

The SBA faces a heightened risk of losses and improper payments due to expedited loan processing initiatives and its considerable reliance on outside financial institutions over which the Agency does not always exercise adequate oversight. The Agency's business loan programs include (1) the Section 7(a) program, in which the SBA guarantees loans to small businesses made by lenders, and (2) the Section 504 program, in which the SBA guarantees repayment of debentures that are sold by Certified Development Companies (CDCs) to investors to create funds for loans to small businesses. The majority of loans made under the Section 7(a) program are made with little or no review by the SBA prior to loan approval because the Agency has delegated most of the credit decisions to lenders originating these loans.

Audits of early defaulted loans and improper payments have noted a number of lender errors in originating loans. In addition, OIG reviews have detected vulnerabilities in the SBA's Standard Operating Procedure (SOP) for the Section 7(a) program. These vulnerabilities include a provision that allows financing of large amounts of intangible assets, including goodwill, in change-of-ownership transactions where the entire equity injection can be provided in the form of seller take-back financing. A recent OIG audit also identified that the SBA had not implemented a program or process to effectively monitor risk in its loan portfolio (Report 13-17). Further, the OIG also has identified management challenges relating to the Agency's quality control process at the loan servicing centers and the National Guaranty Purchase Center, oversight of lenders and CDCs, efforts to prevent loan agent fraud in the Section 7(a) program, and improper payments under the Section 7(a) program.

In addition, numerous OIG criminal investigations have identified fraud by borrowers, loan agents, lenders, and other participants in SBA business loan programs. Criminals fraudulently obtain—or induce others to obtain—SBA-guaranteed loans through a variety of techniques. These include submitting fraudulent documents, making fictitious asset claims, manipulating property values, using loan proceeds contrary to the terms of the loans, and failing to disclose debts or prior criminal records. The result is a greater chance of financial loss to the Agency and its lenders.

Adding to these risks, the amount of 7(a) loans subject to an SBA guaranty was increased in FY 2010 from $2 million to $5 million, and Section 504 loans were increased from $2 million to $5 million for regular projects, and from $4 million to $5.5 million for manufacturing-related projects. These higher loan limits are likely to attract additional attention by criminals and increase the consequences of improper lending decisions.

Through the Disaster Loan program, the SBA makes direct loans to homeowners and businesses harmed by disasters to fund repair or replacement of damaged property and to businesses to provide needed working capital. This program is vulnerable to fraud and unnecessary losses because (1) loan transactions are often expedited in order to provide quick relief to disaster victims; (2) lending personnel hired in connection with a disaster declaration may lack sufficient training or experience; and (3) the volume of loans may overwhelm SBA resources and its ability to exercise careful oversight of lending transactions.

OIG investigations have led to numerous convictions of disaster loan borrowers for making fraudulent statements to obtain loans or misusing loan proceeds. OIG reviews of the SBA's loan processing activities have disclosed significant problems in making, disbursing, servicing, and liquidating disaster loans. For example, a recent OIG audit determined that the SBA did not effectively manage delinquent disaster loans to maximize recovery and minimize losses (Report 13-18). The OIG estimates that from June 2006 to June 2011, at least 7,198 loans, totaling $752.6 million, were charged off without using all appropriate collection tools to maximize recovery. Additionally, the OIG has identified a management challenge relating to improper payments in the Disaster Loan program. It is noted, however, that the Agency has developed a corrective action plan that specifically addresses root causes and provides specific remedies that, if properly implemented, should effectively reduce the rate in future years.

Under the Small Business Investment Company (SBIC) program, the SBA licenses and funds venture capital firms that provide financial assistance to small businesses. The SBA is at risk for significant losses in this program due to: factors related to the economic environment; declines in asset values of participating securities; and increasing amounts of debenture obligations made by the Agency. A recent OIG audit found that outdated guidance, incomplete examination checklists, and other challenges affected the quality of the SBIC examination process (Report 13-22). Past OIG investigations have identified fraud by certain SBIC managers and others participating in this program.

Risks Affecting the SBA's Oversight of Contracts for Small and Disadvantaged Businesses

The Small Business Act directs the SBA to promote the award of Federal contracts to small businesses and firms owned by disadvantaged individuals (such as minorities, service-disabled veterans, women, firms from areas of low economic activity, and others). For FY 2012—the latest year for which information is available—the SBA reported that small and disadvantaged firms were awarded $89.9 billion government-wide in prime contracting assistance. However, OIG audits and investigations have identified numerous instances where firms that do not meet the criteria to be either "small" or "disadvantaged" have improperly obtained contracts under these SBA contracting programs. In addition, the Government Accountability Office (GAO) has issued a series of reports documenting that ineligible companies had been admitted to these SBA contracting assistance programs and were seeking set-aside contracts. These improprieties have resulted from a variety of factors, including fraud by company managers; excessive control over small or disadvantaged firms by large companies or non-disadvantaged individuals; weak oversight by the SBA and Federal procurement personnel; and regulatory ambiguities and loopholes. The OIG has identified management challenges for the SBA to promote integrity in small business contract awards and oversight of the Section 8(a) Business Development program.

Risks Associated with the SBA's Information Security Controls and Other Operations

The SBA's IT systems play a vital role in the management of the Agency's operations and programs, including a loan portfolio in excess of $106 billion. However, OIG audits and other reviews have identified serious shortcomings in the SBA's information systems and related security controls. Most critical, the SBA's principal data processing and data collection tool for loan servicing, monitoring, and accounting—the Loan Accounting System—uses significantly outdated technology that increases vulnerability and security issues. This outdated technology undercuts the SBA's ability to meet the expanding requirements of new initiatives, such as the Small Business Jobs Act of 2010 and the reporting requirements of the Credit Reform Act. The Loan Management Accounting System (LMAS) is a system development project to move the Agency from its legacy mainframe environment to an updated web-based environment. While the LMAS project recently moved 44 percent of its legacy mainframe data entry to the updated web-based environment, which improves security of data entry of SBA transactions, major portions of this project remain to be completed. The SBA must reprogram its mainframe COBOL-based accounting software to run on a web-based operating platform, a project that is currently underway. Additionally, OIG reviews have found that the SBA has not fully implemented adequate oversight of its IT systems; has not established an effective process to remediate security vulnerabilities; and has not developed an effective process to upgrade IT capabilities. The OIG has issued management challenges recommending corrective actions in the SBA's IT security and acquisition processes.

OIG Oversight Activities

Through audits and other reviews, the OIG provides independent oversight of critical aspects of SBA's programs and operations to improve the Agency's efficiency and effectiveness. An important aspect of this work is identifying and following up on the SBA's major management and performance challenges, as required by the Reports Consolidation Act. The OIG also supports the SBA's mission by detecting, investigating, and deterring fraud and other wrongdoing in the Agency's programs and operations. These activities also help to ensure that SBA employees, loan applicants, and program participants possess a high level of integrity. This is critical to the proper administration of the SBA's programs because it helps ensure that the Agency's resources are utilized by those who deserve and need them the most.

FY 2013 Accomplishments

During FY 2013, the OIG issued 19 reports containing 129 recommendations for improving SBA operations and reducing fraud and unnecessary losses in the Agency's programs. In addition, OIG investigations resulted in 64 indictments/informations and 51 convictions. Overall, the OIG achieved monetary recoveries and savings of over $348 million from recommendations that funds be put to better use agreed to by management, disallowed costs agreed to by management, court ordered and other investigative recoveries and fines, and loans or contracts not made as a result of investigations and name checks. These results reflect a significant ROI as compared to the resources that are available for OIG operations.

Following are summaries of some key reports and investigations that demonstrate the complex nature of the OIG's work. It is noted that OIG investigations often involve multiple subjects, large dollar losses, various joint agencies, and substantial restitution and forfeiture monies returned to the Government.

Improving Stewardship through Compliance, Procedures, and Training

A number of OIG reports have identified instances in which the SBA did not comply with laws or established procedures. Other instances included the need for improved processes, quality assurance activities, improved oversight, and additional training. For example:

- An audit of the SBIC examination process found that outdated guidance and incomplete examination checklists affected the quality of the SBIC examination process. Further, the SBIC examiners were impacted by challenges in the areas of strategic planning, training, technology, communication and funding. These challenges, coupled with an emphasis on quantity resulted in examiners not identifying all findings during their examinations. (Report 13-22.)

- An evaluation of SBA's portfolio risk management program determined that the SBA had not implemented a program or process to effectively monitor risk in its loan portfolio. The OIG's limited analysis identified three high-volume franchises with historical default rates of at least 46 percent, default values over 38 percent, and loss rates over 18 percent. The OIG also identified five high-volume retail industries with historical default rates of at least 40 percent, default values over 30 percent, and loss rates over 16 percent. (Report 13-17.)

- A review of the SBA's quality control program for its loan centers determined that quality control activities were not being performed as required. The OIG found that Centers omitted required quality control reviews of significant functions and discontinued regularly scheduled quality reviews to focus on reviews required by the Improper Payments Elimination and Recovery Act (IPERA) of 2010. Further, the OIG determined that corrective actions were not appropriately tracked until resolution, as required. Finally, the OIG determined that the SBA's quality assurance program, responsible for ensuring that quality control activities at loan operation centers are working as intended, had not been established. (Report 14-08.)

- An audit of the SBA's management of delinquent disaster loans determined that the SBA did not effectively manage loans to maximize recovery and minimize losses. The OIG estimated that from June 2006 to June 2011, at least 7,198 of loans, totaling $752.6 million, were charged off without using all appropriate collection tools to maximize recovery. Specifically, the OIG found that the SBA did not: (1) transfer all non-exempt delinquent debts to Treasury for cross-servicing and offset; (2) analyze most delinquent debts for workout and restructuring potential; (3) liquidate loan collateral; (4) renew UCC financing statements to retain SBA's lien priority in non-real estate collateral; or, (5) refer offer-in-compromise settlements for debts above $500,000 to the Headquarters Claims Review Committee, as required by SBA Standard Operating Procedures (SOPs). (Report 13-18.)

- A review of the SBA's certification process of firms into the Historically Underutilized Business Zones (HUBZone) program found that 12 firms certified into the program, including 3 ineligible ones, received 94 percent ($34.9 million) of Federal contract dollars awarded during a 6-month period in 2012, even though 367 firms were certified during that period. 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. (Report 14-03.)

- A review of the SBA's contracting practices in the acquisition of a mission-critical IT system found that the Agency did not follow Federal contracting laws and, as a result, the Agency did not receive a system with full capabilities as originally designed. The original OneTrack system should have been completed in a 12-month period at a total cost of approximately $1.17 million. Instead, the SBA modified the task order to receive a system with the same, limited functions as the existing system—the Business Development Management Information System (BDMIS). However, the SBA still did not have a tested and approved system—that included existing BDMIS capabilities—to put into production when the task order expired. To date, the SBA has increased the total cost of the system by approximately $734,000 and extended the performance of the acquisition by 14 months. (Report 14-10.)

- An OIG review found that between November 2010 and May 2012, the SBA received invoices associated with 417 unauthorized commitments—more than $1.4 million in inappropriately expended Agency funds. The large number of unauthorized commitments directly impacted the ability of the Agency to legally and efficiently procure goods and services for its daily operations and limited its ability to provide needed support to small businesses. Also, the process of ratifying the large number of unauthorized commitments required additional staff resources and increased operating costs. (Report 13-14.)

In these reports, the OIG recommended that the SBA take specific corrective actions to develop and execute plans to improve the internal operations and processes, update procedures, ensure that guidance is readily accessible to employees, and provide sufficient and appropriate training. The OIG also recommended that the SBA take steps to ensure proper contract oversight of the development and implementation of a mission-critical IT systems, establish quality assurance activities at the SBA loan centers, and implement a portfolio risk management program to analyze risk across portfolio segments to support risk-based decision in its loan programs. These recommendations, once implemented, will further the SBA's ability to meet program objectives and improve stewardship through compliance, procedures, and training.

Preventing and Reducing Improper Payments

The SBA's efforts to prevent and reduce improper payments for 7(a) loan approvals, 7(a) loan purchases, Section 504 loans, and disbursements for its contacting activities were the focus of three OIG audits. The first audit disclosed that the SBA reported $41 million in improper payments for 7(a) loan purchases made in FY 2011, whereas the OIG's independent statistical sample determined that the improper payments could have been as high as $472 million (Report 13-07). Another audit found that due to improved testing procedures, the SBA's improper payments estimate for 7(a) loan guaranty approvals increased from $0 in FY 2011 to $233 million in FY 2012 (Report 13-13). A third audit found that the SBA's reported improper payments for acquisitions excluded certain payments with documentation errors from the SBA's improper payment calculations (Report 14-02). Consequently, the FY 2012 improper payment rate for disbursements and contracting exceeded 10 percent.

In addition, the OIG has developed new analytical techniques to identify fraudulent activity and prevent and reduce improper payments on 7(a) loans. During FY 2012 and FY 2013, the OIG conducted a series of audits focused on high-dollar early defaulted 7(a) loans funded under the Recovery Act. These audits utilized a new, internally developed, risk-based sample selection methodology. This methodology allocates rating points according to perceived risks. The perceived risks included time lapse between loan approval and its transfer to liquidation, loan amount, borrower equity injection, loan packager involvement, and the use of the loan proceeds. The results of this special project were significant. A total of 13 of the 17 loans reviewed, with payments totaling $16.3 million, were either referred for further investigation or recommended to the SBA for recovery. (Reports 13-16R and 14-09.)

Improving Systemic Reporting and Data Control Weaknesses

In a review of the SBA's controls and oversight over certain IT systems and processes, the OIG identified systemic reporting issues and data control weaknesses. These deficiencies resulted in an estimated $956 million overstatement of unpaid loan balances with an estimated $5.2 million effect on program subsidy. In addition to recommending that the SBA take action to correct the overstatement and collect outstanding late penalty fees, the OIG recommended that the SBA adhere to quality standards for systems development projects and ensure that systems are authorized to operate prior to being put into production. SBA recently initiated corrective actions in these areas by improving data quality and collecting late penalty fees**.** (Report 12-08.)

Major Bribery Case Involves Over $2 Billion in Government Contracts

As of September 30, 2013, an ongoing multi-agency investigation has resulted in 16 individuals and 1 company being charged and 9 individuals sentenced in a scheme involving more than $30 million in bribes and kickback payments. The individuals include government officials, executives of 8(a) contractors, and an employee of an Alaska Native Corporation (ANC) contractor. The conspiracy included the use of a $1.3 billion ANC sole source contract to pay for the bribes and the planned steering of a $780 million government contract to a favored Section 8(a) program participant. The individuals involved have thus far pled guilty to bribery, conspiracy, money laundering, and other charges. In the overall investigation, the United States has seized for forfeiture or recovered approximately $22.3 million in bank account funds, cash and repayments, 19 real properties, six luxury cars, and multiple pieces of fine jewelry. This is a joint investigation with the FBI, Internal Revenue Service Criminal Investigation, U.S. Army Criminal Investigation Command, and the Defense Criminal Investigative Service (DCIS).

Prosecutions in $31 Million Fraud Investigation Result in Over $8.8 Million in Penalties

A Florida man pled guilty to major fraud against the government, and seven individuals in Virginia were each sentenced in connection with fraudulently obtaining over $31 million in Section 8(a) and small business set-aside contracts. The investigation disclosed a scheme in which two Virginia businesses falsely represented to the government that the second firm was eligible for the Section 8(a) program when, in fact, it was operated and controlled by the first business. Although the second firm was required to perform at least 50 percent of the work on the contracts and had represented it would do so, no employees from the firm actually performed any work. Instead, the Florida man and others performed all of the work as independent contractors but concealed that fact from the government agencies. He also submitted fraudulent proposals and invoices to hide their scheme, used a third-party company's Federal Employer Identification Number to prevent reporting of his contractor income to the IRS, and did not pay any taxes on the income he received from the firm. Forfeitures in the case thus far total over $7.7 million. In addition, fines and restitution total over $1.1 million. This is a joint investigation with the National Aeronautics and Space Administration OIG, the DCIS, and the Department of Homeland Security OIG.

Loan Agents' Fraudulent Activity Leads to Losses of $100 Million in the Section 7(a) Program

As of September 30, 2013, an investment firm and eight individuals have been indicted, with six of them having been convicted and sentenced in connection with a scheme to fraudulently obtain SBA-guaranteed loans. Forfeiture orders in the case thus far total over $151 million, in addition to fines and restitution in excess of $42.3 million. The resulting losses totaled over $100 million. The investigation revealed a scheme in which prospective borrowers were encouraged to apply for Section 7(a) business loans through an investment firm specializing in securing loans for individuals interested in purchasing or refinancing small businesses in the Mid-Atlantic area. The firm's owners would then submit SBA loan applications and supporting documentation allegedly containing fraudulent personal financial statements, bank statements, tax documents, and other financial documents to loan originators and underwriters on their clients' behalf, thereby falsely enhancing the creditworthiness of the borrowers and their businesses. To date, the United States has recovered or seized for forfeiture over $52 million. This is a joint investigation with the FBI and United States Postal Inspection Service.

Procurement Fraud Results in Prison and a $6.8 Million Forfeiture

The owner of a Kansas construction firm was sentenced to 87 months in prison and 3 years of supervised release in addition to a personal forfeiture judgment of over $6.8 million. He had previously pled guilty to conspiracy, major program fraud, wire fraud, money laundering conspiracy, and making false statements. He and his business fraudulently claimed Service-Disabled Veteran-Owned Small Business (SDVOSB) status to obtain 11 Federal government contracts valued at approximately $6.8 million, which they would otherwise not have been entitled to receive. The owner also admitted to providing the Department of Veterans Affairs (VA) contracting officer with a fraudulent résumé in which he claimed to have served three tours in Southeast Asia as a highly decorated U.S. Army officer. Government records showed that he never left Missouri during his service in the Army and Missouri National Guard. This is a joint investigation with the General Services Administration OIG, the VA OIG, and the DCIS.

Additional information on the OIG's accomplishments during FY 2013 are provided in the Statistical Highlights section of this document and in the OIG's *Spring and Fall 2013 Semiannual Reports to Congress*.

FY 2015 Planned Performance

During FY 2015, in addition to conducting audits and reviews that are required by statutes and other directives, the OIG will continue to focus on the most critical risks facing the SBA. Several areas of emphasis are discussed below.

Financial Assistance

The SBA paid guaranty claims totaling $3.8 billion during FY 2012 and FY 2013 for defaulted 7(a) loans and 504 debentures. Some of the SBA losses correlate to similar root causes reported in the mortgage industry, such as limited SBA oversight of lenders and loan agents, poor lender loan processing, unscrupulous borrowers, and complicit brokers and lenders.

The OIG to will continue to address financial losses in SBA lending due to lender errors and various fraud schemes. The OIG will utilize an Early Defaulted Loan Review Group to perform in-depth analyses of loans that default within 18 months of final disbursement. When lender negligence is found, this group will recommend non-payment of the guaranty (or recovery if the guaranty is already paid). The OIG will also target the most offending lenders to attain corrective actions and identify trends for operational improvement by the SBA. When suspected fraud is identified, those loans will be investigated.

The OIG will continue to focus on detecting fraud committed by loan agents, such as packagers and brokers. A loan agent is sometimes hired by an applicant or lender to assist the applicant in obtaining an SBA loan. Although honest loan agents help small businesses gain access to capital, some dishonest ones have perpetrated fraudulent schemes involving tens of millions of dollars in loans. These fraudulent loans often default for non-payment, and the SBA is forced to use taxpayer funds to purchase the guaranteed portions of the loans. In a recent case, an OIG investigation led to the indictment of three loan brokers and their company for conspiring to provide false information to the SBA in order to obtain SBA loans. This is a complex fraud scheme involving over 120 loans valued at $100 million. Over the past decade, the OIG has obtained convictions and guilty pleas on numerous cases involving loan agent fraud on SBA-guaranteed loans, totaling in excess of $458 million.

The OIG will also continue to conduct audits of SBA's internal loan program operations and oversight, including audits of SBA's loan origination, servicing and liquidation processes, as well as audits of SBA's oversight of loan agents and loan officers. Past work has shown that loans were not always properly originated and that effective controls and procedures were not in place to prevent improper payments.

Government Contracting and Business Development

The SBA directs significant efforts toward helping small businesses obtain Federal contracts and providing other business development assistance. The SBA's Office of Government Contracting and Business Development is tasked with helping small businesses obtain Federal contracting opportunities and helping small, disadvantaged, veteran-owned, and women-owned businesses build their potential to compete more successfully in a global economy. During FY 2015, the OIG will focus on the SBA's oversight of and current issues affecting Government Contracting and Business Development programs, including investigating allegations that ineligible companies are fraudulently benefitting from these programs (as of September 30, 2013, the OIG had 88 open government contracting cases, with potential dollar losses of over $2 billion based on the total dollar value of the contracts). The funding requested for FY 2015 will allow the OIG to continue investigating fraudulent schemes that take improper advantage of SBA's contracting assistance programs. In addition, the OIG will continue to investigate qui tam False Claims Act suits filed by private sector parties alleging fraud in SBA government contracting programs and will assist the Department of Justice in prosecuting claims when warranted.

Aside from these issues, there are other reasons to be concerned about government contracting programs.

- There is a high level of congressional interest in the government meeting its small business contracting goals. The OIG will continue to assess whether the SBA is taking adequate steps to ensure the integrity of small business contracting. The OIG's work will focus on issues such as: the accuracy of reporting small business contract activity; large businesses being classified as small businesses; adherence to regulations to protect small businesses; training of government contracting personnel; deterring fraudulent acquisition of government contracts; and bundling of contracts.

- The Section 8(a) Business Development program continues to be susceptible to major vulnerabilities. These include limited program oversight; inequitable distribution of contracting opportunities among participants; a lack of reasonable, measurable, consistent, and mandatory criteria pertaining to economic disadvantage; a lack of implemented criteria defining business success for purposes of program graduation; and misrepresentation by companies as small, minority-owned, or disadvantaged businesses to gain an unfair advantage in the Federal marketplace. The OIG will continue to review these issues and the SBA's management of the Section 8(a) program. The OIG is currently conducting a number of fraud investigations relating to the Section 8(a) program and will continue to devote resources to these investigations in FY 2015.

- The HUBZone program provides Federal contracting assistance to small businesses located in economically distressed areas with the intent of stimulating economic development. The SDVOSB program provides more opportunities in Federal contracting for disabled veterans who own small businesses. The GAO has identified significant control weaknesses in these programs that have allowed ineligible firms to receive millions of dollars in contracts. The OIG is examining the SBA's claim that it has implemented a more rigorous HUBZone certification and recertification process in the hopes of preventing ineligible firms from achieving certification. In addition, the OIG plans to review the HUBZone decertification process once the SBA completes its reengineering of this process. The OIG is currently investigating numerous fraud cases under the HUBZone and SDVOSB programs and will continue to pursue prosecution, civil fraud recovery, and debarment of contractors who improperly obtain HUBZone, SDVOSB, and other preferential contracts.

- The OIG has conducted a number of fraud investigations involving the mentor/protégé programs under the Section 8(a) program. The SBA is close to implementing a statutory mandate by issuing regulations that will expand mentor protégé programs to other disadvantaged contractors. The OIG anticipates that these arrangements will create opportunities for additional fraud by large, non-disadvantaged contractors, requiring OIG resources to investigate this fraud.

Financial Management and Information Technology

The OIG will continue to oversee the audits of the SBA's financial statements, as well as FISMA and Federal Information Systems Controls Audit Manual (FISCAM) reviews, which are conducted by an independent public accountant under a contract with the OIG. The financial statement audit contract will expire in FY 2015, and the OIG will work with the Agency on a new contract solicitation. The OIG also will continue its review of the SBA's compliance with IPERA. The OIG anticipates that the scope and cost of financial statement audits will continue to expand as a result of growing direct and guaranteed loan portfolios. The OIG will continue its review of SBA's actions to implement the requirements of the GPRA Modernization Act of 2010. The review will examine the sources and use of performance information in program decision-making and evaluate the effectiveness of corrective actions deployed to address long-standing challenges, needs, and problems.

The OIG also will continue to monitor systems development activities related to improvements to LMAS, a system that is critical to SBA's ability to administer its $106 billion loan portfolio. The OIG's efforts will include determining whether adequate system development lifecycle controls are in place as the SBA endeavors to move its recently developed software from the mainframe to a new hosting environment. We will also assess the adequacy of testing and quality assurance processes. As threats to disrupt cyber-based systems continue to escalate, the Agency must take steps to improve controls to prevent outages and loss of sensitive data and to ensure the continuity of mission critical operating systems. The OIG will conduct audits to assess the security of the SBA's computer operating system, network, and hosted applications by performing assurance reviews. The OIG also will review the sufficiency of SBA resources used to manage computer security, maintain systems, provide technical support, and administer security training.

Disaster Assistance

The OIG's audits will continue to focus on loan origination, disbursement, repayment, servicing, and liquidation activities related to disaster loans. In October 2012, Superstorm Sandy struck the northeastern United States. It was the second costliest storm in U.S. history. The OIG received $5 million in appropriated funds to conduct oversight of SBA disaster loan making to businesses and individuals. To meet this oversight responsibility, the OIG will investigate and audit disaster loans made in the aftermath of Superstorm Sandy to prevent and minimize losses in this program. Such audits will assess whether the SBA processed homeowner and business loans in accordance with the Agency's procedures and established goals, verified uses of loan proceeds before loans were fully disbursed, and appropriately identified duplicate benefits. The OIG will also perform targeted reviews of Superstorm Sandy loans to identify errors in SBA's loan processing and indications of fraud. When suspected fraud is identified, those loans will be investigated.

The OIG also will continue to investigate allegations of unauthorized use of loan proceeds; overstatement of financial losses; material false statements in the application process; false or counterfeit supporting documentation; and false assertions regarding primary residency in affected areas at the times of the disasters. As of September 30, 2013, the OIG had 19 open cases involving disaster loans with potential dollar losses of over $10.1 million.

In response to the increase in fraud following Hurricanes Katrina, Wilma, and Rita, the OIG joined other law enforcement organizations in establishing the National Center for Disaster Fraud. From FY 2006 through FY 2013, the OIG, in conjunction with other law enforcement agencies, has produced 86 arrests, 96 indictments/informations, and 96 convictions related to wrongdoing in SBA's Disaster Loan program for these three hurricanes. Investigations for these disasters—to date—have resulted in over $6.6 million in court-ordered restitution and related recoveries, as well as the denial of nearly $4.5 million in loans to potentially fraudulent borrowers. In addition, the OIG has investigated fraud related to 2008 Hurricanes Ike and Gustav.

Agency Management Challenges

As required by the Reports Consolidation Act, the OIG annually develops the *Report on the Most Serious Management and Performance Challenges Facing the SBA*. The management challenges focus on areas that are particularly vulnerable to fraud, waste, error, and mismanagement, or otherwise pose a significant risk and generally have been the subject of one or more OIG or GAO reports. The OIG will continue to identify serious management challenges facing the SBA and will work throughout the year with Agency management to resolve identified issues as quickly and efficiently as possible.

Security Operations

The OIG's Office of Security Operations will continue processing name checks and, where appropriate, fingerprint checks to ensure that applicants meet certain character standards before participating in programs involving business loans, disaster assistance loans, Section 8(a) certifications, surety bond guarantees, SBICs, and CDCs. As a result of OIG referrals during FY 2013, SBA business loan program managers declined 39 applications totaling over $21.9 million, and disaster loan program officials declined 58 applications totaling over $3.9 million, due to character issues of loan applicants. In addition, the Section 8(a) program declined 10 applications for admission. Over $310 million in loans have been declined during the last 10 years due to character problems identified by the OIG, thereby making credit and SBA assistance available to other applicants with no such issues. The OIG will also perform required background investigations for covered SBA employees and adjudicate SBA employees and contractors for issuance of PIV cards pursuant to HSPD-12 background investigation requirements. During FY 2013, the OIG initiated 322 background investigations and issued 36 security clearances for SBA employees and contractors.

The OIG Hotline

The Hotline is staffed by OIG employees who process allegations of waste, fraud, abuse, or serious mismanagement in the SBA or its programs from employees, contractors, and the public. The Hotline also coordinates reviews with internal audit and investigative units and with SBA program offices. The OIG receives the majority of its Hotline complaints through its electronic Hotline complaint form located on the OIG website. Those who report information can do so openly, anonymously and confidentially without fear of reprisal.

During FY 2013, the Hotline processed 853 complaints, compared with 535 in FY 2012—an increase of almost 60 percent. Hotline staff conduct a preliminary review and analysis of all complaints received to determine the appropriate course of action. As part of the review process, Hotline staff coordinates the analysis of allegations within the OIG and SBA program offices. Investigations that are initiated as a result of a Hotline complaint are monitored by the Hotline staff throughout the course of the investigation. If additional investigation is not warranted, complaints may be referred to SBA program offices for appropriate action or informational purposes.

Pursuant to the Whistleblower Protection Enhancement Act of 2012, the OIG has designated a Whistleblower Ombudsman within the Hotline function to educate SBA employees about prohibitions on retaliation for whistleblowing, as well as employees' rights and remedies if anyone retaliates against them for making a protected disclosure. In addition, the National Defense Authorization Act of 2013 extends whistleblower protections to government contractors, subcontractors, and grantees. These provisions may result in an increase in the number of complaints received by the Hotline.

Review of Proposed Regulations and Initiatives

As part of the OIG’s proactive efforts to promote accountability and integrity and reduce inefficiencies in SBA programs and operations, the OIG reviews changes that SBA is proposing to make to its program directives such as regulations, internal operating procedures, policy notices, and SBA forms that are completed by lenders and the public. Frequently, the OIG identifies material weaknesses in these proposals and works with the Agency to implement recommended revisions to promote controls that are more effective and deter waste, fraud, or abuse. During FY 2013, the OIG reviewed 115 proposed revisions of program management or SBA reorganization documents.

Debarment and Administrative Enforcement Actions

As a complement to the OIG’s criminal and civil fraud investigations, the OIG continually promotes the use of suspensions, debarments, and other administrative enforcement actions as a means to protect taxpayer funds from those who have engaged in fraud or otherwise exhibited a lack of business integrity. The OIG regularly identifies individuals and organizations for debarment and other enforcement actions and submits detailed recommendations with supporting evidence to the responsible SBA officials. During FY 2013, the OIG sent 65 suspension and debarment referrals to SBA. Most OIG administrative referrals involve the abuse of SBA’s loan and preferential contracting programs. When appropriate, the OIG recommends that the SBA suspend the subject of an ongoing OIG investigation given program risk presented by the continued participation of those individuals and entities.

Fraud Awareness Briefings

The OIG will continue to conduct briefings on topics related to fraud in government lending and contracting programs. During FY 2013, the OIG provided 19 fraud awareness presentations for more than 900 attendees, including SBA and other Government employees, lending officials, and law enforcement representatives. Topics included types of fraud; fraud indicators and trends; and how to report suspicious activity that may be fraudulent.

FY 2013 Statistical Highlights

Summary of Office-Wide Dollar Accomplishments

As a Result of Investigations & Related Activities:	
– Potential Investigative Recoveries & Fines	$92,917,594
–Asset Forfeitures Attributed to OIG Investigations	$185,659,456
–Loans/Contracts Not Approved or Canceled as a Result of Investigations	$950,000
–Loans Not Made as a Result of Name Checks	$25,834,020
Investigations Sub-Total	**$305,361,070**
As a Result of Audit Activities:	
–Disallowed Costs Agreed to by Management	$2,126,145
–Recommendations that Funds Be Put to Better Use Agreed to by Management	$40,700,000
Audit Sub-Total	**$42,826,145**
TOTAL	**$348,187,215**

Efficiency and Effectiveness Activities Related to Audit, Other Reports, and Follow-Up Activities

Reports Issued	
Recommendations Issued	129
Dollar Value of Costs Questioned	$45,884,433
Dollar Value of Recommendations that Funds be Put to Better Use	$40,700,000
Recommendations for which Management Decisions Were Made	109
Recommendations Without a Management Decision	59
Collections as a Result of Questioned Costs	$1,932,999

Indictments, Convictions, and Case Actions

Indictments from OIG Cases	64
Convictions from OIG Cases	51
Cases Opened	50
Cases Closed	65

SBA Personnel Actions Taken as a Result of Investigation

Dismissals	0
Resignations/Retirements	1
Suspensions	1
Reprimands	0
Other	0

Legal Reviews and Program Actions*

Legislation, Regulations, Standard Operating Procedures, and Other Issuances Reviewed	115
	65
—Pending at the Agency as of September 30, 2013**	79
S	10
P	34
F	16
P	0
A	3
S	17
P	
—	3
—	1
—	1

* The SBA agreed to allow another agency to take lead agency status on 8 of the 49 OIG referrals. Under Federal debarment procedures, when more than one agency has an interest in pursuing a debarment, those agencies confer and determine which agency will take the action.

** Some of these referrals have been pending for more than six months. As of September 30, 2013, the SBA had initiated action on 33 of the 51 pending referrals from the OIG.

Reporting Requirements Under the Inspector General Reform Act of 2008

The following information is provided in accordance with the Inspector General Reform Act of 2008, as amended (P.L. 110-409).

Dollars in Millions	**FY 2013 Actual[1\]**	**FY 2014 Enacted**	**FY 2015 Initial Agency Submission**	**FY 2015 President's Budget**
New Budget Authority	$16.3	$19.0	$19.4	$19.4
Transfer from Disaster Loan Program Account	1.0	1.0	1.0	1.0
Total	**$17.3**	**$20.0**	**$20.4**	**$20.4**

1\ Amounts do not include impact of Sequestration, Across the Board Rescission, or funding provided under the Disaster Relief Appropriations Act of 2013.

The OIG's FY 2015 budget request includes $120,000 for training, which is sufficient to satisfy all training needs for the fiscal year, and $50,000 for the operation of the Council of Inspectors General on Integrity and Efficiency.

OIG Organizational Structure

The OIG is comprised of the immediate office of the Inspector General and four divisions: Auditing, Investigations, Counsel, and Management and Policy.

The **Auditing Division** performs and oversees audits and reviews to promote the economical, efficient, and effective administration of SBA programs and operations. Key areas of emphasis are SBA's loan programs, disaster assistance, business development and government contracting programs, as well as mandatory and other statutory audit requirements involving computer security, financial reporting, and other work. The balance of the engagements is discretionary and focuses on high-risk activities and management issues facing the SBA.

The **Investigations Division** manages a program to detect and deter illegal and improper activities involving SBA programs, operations, and personnel. The criminal investigations staff carries out a full range of traditional law enforcement functions. The security operations staff ensures that SBA employees and contractors have appropriate background investigations and security clearances to achieve a high level of integrity in the Agency's workforce, and that loan applicants and other potential program participants are of good character.

The **Counsel Division** provides legal and ethics advice to all OIG components; represents the OIG in litigation arising out of or affecting OIG operations; assists with the prosecution of criminal, civil, and administrative enforcement matters; processes subpoenas; responds to Freedom of Information and Privacy Act requests; and reviews and comments on proposed policies, regulations, legislation, and procedures.

The **Management and Policy Division** provides business support (e.g., budget and financial management, human resources, IT, and procurement) for the various OIG functions; coordinates preparation of the OIG's *Semiannual Report to Congress* and other OIG-wide reports and documents; maintains the OIG website; and operates the OIG's Hotline.

An organizational chart for the OIG is provided on the next page.

Small Business Administration
Office of Inspector General