

U.S. SMALL BUSINESS ADMINISTRATION

OFFICE OF INSPECTOR GENERAL

Report No. 08-01

*Fiscal Year 2008 Report
on the Most Serious Management and
Performance Challenges Facing the
Small Business Administration*

October 16, 2007



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

October 16, 2007

MEMORANDUM

TO: Steven C. Preston
Administrator

FROM: *<Original signed by:>*
Eric M. Thorson
Inspector General

SUBJECT: Fiscal Year 2008 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) 2008 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 facing the Agency.

Our report is based on specific OIG, Government Accountability Office, 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, 2007.

The Agency continues to demonstrate substantial progress in resolving the Challenges. For example, SBA's efforts to identify and address the underlying causes of its financial management issues, improve the models for estimating the Agency's subsidy costs, strengthen controls over financial statement preparation, and adhere to all reporting deadlines has resulted in two successive unqualified audit opinions on its financial statements. Recognizing this accomplishment, our FY 2008 report reflects the elimination of one of the Challenges in last year's report: "SBA faces significant challenges in financial management and reporting, which affects its ability to provide reliable, timely, and accurate financial information" (formerly Challenge 2). The Challenges have been renumbered to reflect this change.

Within each Management Challenge there are a series of "recommended actions" to resolve the Challenge. Each recommended action is assigned a color "status" score, except for Management Challenge 3, which was substantially revised in May 2007 to

reflect our current assessment of the difficult issues facing the Agency's human capital management program. The scores are as follows: Green for Implemented; Yellow for Substantial Progress; Orange for Some Progress; and Red for No Progress. An upwards arrow in the color box indicates that the color score improved over last year's report. As part of the OIG's continuing evaluation of the Management Challenges, certain Challenges have been updated or revised.

Actions that were scored Green last year, and which remained Green this year, have been moved up to the "history bar," which is located above the action items. The history bar helps to show any progress that the Agency has made on the Challenge over the past four fiscal years (or as long as the Challenge has existed, if shorter) by reporting the number of actions that moved to Green each year.

Following is a summary of the FY 2008 report on the Agency's Most Serious Management and Performance Challenges.

	Topic	Status Score				Improved ¹
		Green	Yellow	Orange	Red	
1	Small Business Contracts		2	2		1
2	IT Security	2	5	1		4
3	Human Capital	n/a	n/a	n/a	n/a	
4	Loan Guaranty Purchase		3	1		2
5	Lender Oversight	1	5	5		4
6	8(a) BD Program	1	1	4	1	3
7	SBIC Program	1	3	2		5
8	Loan Agent Fraud	1	2	3		3
9	Directives System	3		1		3

We would like to extend our appreciation to SBA's management and staff for their courtesy and cooperation in providing us with the information needed to complete this report in a timely manner.

I want to thank you, and Deputy Administrator Carranza, for your dedicated efforts in promoting agency actions to address the Management Challenges. I think that the Agency's considerable progress this past year reflects the emphasis that you have placed on the OIG Challenges.

Please let me know if you have any questions.

Attachment

cc: Deputy Administrator

¹ "Improved" refers to a recommended action that showed progress this year over last year's score (as denoted by an "up" arrow).

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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.

The Small Business Act establishes a Government-wide procurement goal that 23 percent of the total value of all prime contract awards for each fiscal year (FY) be awarded to small businesses. As the advocate for small business, the Small Business Administration (SBA) should strive to ensure that only small firms obtain small business awards and agencies only receive small business credit for awards to small firms.

Large companies improperly obtain small business contracts due to a variety of problems. Some contractors obtain small business contracts for which they are not eligible by misrepresenting their size or by not diligently verifying whether they meet size criteria. In other cases, improper awards result from errors by contracting personnel, such as accepting questionable size self-certifications or possible unfamiliarity with small business contracting procedures. Although a new database, Online Representations and Certifications Application (ORCA), allows contractors to maintain current certification information electronically, it is unclear whether contracting officers are required to review on-line certifications prior to awarding contracts. SBA needs to do more to promote contractor accuracy, ensure that government contracting personnel receive adequate training on small business procurement procedures, and encourage greater accuracy in Federal agency small business contracting reports.

The Agency also needs to address a loophole with General Services Administration Multiple Awards Schedule (MAS) contracts that contain multiple industrial codes. 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 specific industrial code for the applicable contract. Thus, agencies may obtain small business credit for using a firm classified as small even if the firm is not small for the specific goods or services procured through a particular task order under such a MAS contract.

Although more remains to be done, in FY 2007 SBA took a number of significant steps to begin to address this Challenge: (1) issuing final regulations requiring contractor size recertification on a regular basis on MAS and Government Wide Acquisition Contracts and when a firm has merged or been acquired; (2) issuing a Small Business Procurement Scorecard which grades agencies on their efforts to ensure accurate reporting, (3) issuing a letter jointly with the Office of Federal Procurement Policy to all procuring agencies emphasizing the importance of accurate contract reporting; (4) working to implement new governmental procedures to improve the validity and reliability of procurement data reporting, (5) developing small business procurement training course materials and conducting numerous training sessions for procuring agency personnel; and (6) working to establish requirements for procurement personnel to review on-line certifications.

Challenge History Fiscal Year Issued: 2005	Actions Accomplished (Green Status) during Past 4 FYs (Green actions move from “remaining actions” to this row after one year)			
			05-0	06-0
Remaining Actions Needed for FY 2008				Status at end of FY 2007
1. Develop and take steps to provide reasonable assurance that agencies are providing adequate basic and continuing education training to all contracting personnel on small business contracting procedures.				Orange
2. Develop and implement a program that promotes accurate contractor certifications, and which ensures that contracting personnel review contractor certifications.				Yellow↑
3. Develop and implement a plan that ensures that Federal agencies accurately report the number of contracts they award to small businesses.				Yellow
4. Issue regulations that require firms to meet the size standard for each specific order they receive under a GSA schedule contract.				Orange

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

Challenge 2. Information systems security needs improvement.

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 is a dynamic program requiring management attention and resources as weaknesses are identified.

In FY 2007, SBA demonstrated considerable progress in improving the security of its information systems. SBA centralized administration of its network accounts, revised SOP 90-47 to strengthen controls over access granted to contractors, established an Enterprise Change Control Board (ECCB), and standardized change control requests. It also converted a large number of its servers and desktop computers to Windows 2003 and Windows XP, which improved system controls and the control environment, and secured remote network access with two-factor authentication. Additionally, SBA improved the tracking of security weaknesses, centralized the tracking of IT security training, and demonstrated that technical training for individuals with significant security duties has improved. SBA is also to be commended for closing 71 of 104 OIG audit recommendations. To show further progress, SBA will need to install encryption access controls, and implement a process to more timely mitigate system risks that are identified as “high.” SBA will also need to identify users of the Loan Accounting System who have incompatible system access rights, demonstrate that service continuity controls over its contractor-operated systems are in place, address OIG audit recommendations more timely, and increase staff participation in computer security training.

Challenge History Fiscal Year Issued: 1999	Actions Accomplished (Green Status) during Past 4 FYs (Green actions move from “remaining actions” to this row after one year)			
	03-5	04-4	05-2	06-0
Remaining Recommended Actions for FY 2008				Status at end of FY 2007
<i>SBA needs to improve its Information Technology general and application control environment.</i>				
1. Access controls are in place and operating effectively (<i>previously action #2</i>).				Yellow↑
2. Application software development and program change controls are in place and operating effectively (<i>previously action #3</i>).				Green↑
3. System software controls are in place and operating effectively (<i>previously action #4</i>).				Orange↑
4. Segregation of duty controls are in place and operating effectively (<i>previously action #5</i>).				Yellow
5. Service continuity controls are in place and operating effectively (<i>previously action #6</i>).				Yellow
6. The SBA Certification and Accreditation (C&A) process is in compliance with NIST 800-37 (<i>previously action #7</i>).				Green↑
7. The Plan of Actions and Milestones (POA&M) accurately reports all computer security weaknesses and corrective actions (<i>previously action #8</i>).				Yellow
8. SBA ensures adequate and up-to-date computer security program training (<i>previously action #11</i>).				Yellow

Green

-Implemented Yellow-Substantial progress Orange-Limited Progress Red-No progress

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

Between 2001 and 2006, SBA’s staffing (excluding Disaster) decreased by more than 25 percent while virtually all of its programs grew significantly. For example, the number of loans made to small businesses doubled and the Agency’s oversight responsibilities over government contracting to small businesses increased as the value of these Federal contracts rose by more than 50 percent. In response to budget cuts, SBA restructured key Agency operations, reengineered its largest loan programs, and downsized personnel through attrition and directed transfers. While these actions transformed the way SBA does business, the Agency did not adequately analyze priorities and allocate resources consistent with those priorities and its new business processes. As a result, there has been no assurance that adequate procedures and resources, in terms of both staffing levels and the knowledge and skills possessed by staff, have been put in place and appropriately deployed to perform critical functions. For example, audits have shown that inadequate staffing of key functions resulted in limited oversight of lenders and inadequate monitoring of 8(a) program requirements. The Agency also did not communicate to its employees a transformation strategy or “blueprint” that would have helped them better understand the changes that were taking place. As a result, many employees have not been adequately informed about their future roles and how their work contributes to accomplishment of the Agency’s mission and strategic goals.

The results of the 2002, 2004, and 2006 Federal Human Capital Surveys (FHCS), which were administered by the Office of Personnel Management (OPM), illustrate the serious human capital challenges SBA is facing. These surveys, which measured Federal employees’ perceptions about how effectively agencies have managed their workforces, have shown significant problems at SBA. For example, in the most recent survey, positive responses to 36 of 80 questions were far below the government-wide average, and 7 items trended significantly downward since the previous survey. Out of 36 agencies, SBA ranked near the bottom on all four human capital indices measured by the FHCS: Leadership and Knowledge Management (33rd); Results-Oriented Performance Culture (32nd); Talent Management (35th); and Job Satisfaction (34th). Individual survey questions for which SBA’s scores were particularly low included those concerned with the adequacy of job-related knowledge and skills, the reasonableness of workload, sufficiency of information needed to go a good job, and employee morale. These results clearly demonstrate a need for SBA to develop, communicate, and implement immediate and ongoing measures to address the serious human capital issues that are affecting the Agency’s ability to successfully carry out its mission.

Challenge History Fiscal Year Issued: 2001 (Completely Revised: 2007)	Actions Accomplished (Green Status) during Past 4 FYs (Green actions move from “remaining actions” to this row after one year)			
	03-0	04-1	05-0	06-0
Remaining Recommended Actions for FY 2008				Status at end of FY 2007
1. Allocate appropriate staffing toward Agency priorities – perform an analysis of Agency priorities and develop, communicate, and implement a comprehensive plan (including responsibilities, metrics, and timeframes) for allocating appropriate staffing (in terms of staffing levels and requisite knowledge, skills, and abilities) toward those priorities.				New
2. Take steps to correct problems identified by the FHCS – develop, communicate, and implement a corrective action plan (including priorities, responsibilities, metrics, and timeframes) to address the underlying causes of SBA’s poor results on the FHCS.				New
3. Plan for the future of SBA – develop and implement an effective succession planning program to ensure that there are qualified staff available to perform SBA’s mission-critical functions and meet identified priorities for the foreseeable future.				New

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

Challenge 4. SBA’s National Guaranty Purchase Center needs better controls over the 7(a) loan guaranty purchase process.

The majority of loans made under the 7(a) loan-guaranty program are made with little or no review by SBA prior to loan approval because SBA has delegated most of the credit decisions to lenders originating these loans. SBA’s review of lender requests for guaranty purchases on defaulted loans is, therefore, the Agency's primary tool for assessing lender compliance on individual loans and protecting SBA from making erroneous purchase payments. However, OIG audits of early defaulted loans and SBA’s guaranty purchase process have shown that reviews made by the National Guaranty Purchase Center (NGPC) have not consistently detected lender failures to administer loans in full compliance with SBA requirements and prudent lending practices, resulting in improper payments.

SBA has taken actions to correct many of the deficiencies identified by the OIG, such as centralizing the 7(a) loan guaranty purchase process to improve the efficiency of the program. SBA has also revised Standard Operating Procedures on loan servicing and loan liquidation, developed training modules, and trained individuals responsible for making purchase decisions. Further, the Agency recently completed a reengineering study of the NGPC to determine the appropriate staffing levels for operational effectiveness and developed a statistical sampling methodology to identify improper payments in accordance with OMB requirements. While improvements have been made, additional actions are needed to strengthen the guaranty purchase decisions and effectively reduce improper payments, such as fully staffing the NGPC at the appropriate level, fully implementing the new sampling methodology, and ensuring corrective actions are taken when deficiencies in the purchase review process are identified. Also, the Agency needs to implement policies and procedures that are required in recommended action 4 below, including: (1) review of the entire lender loan file for early-defaulted loans; (2) verification of financial information; (3) identification of collateral at loan inception and after loan default; and (4) verification of borrower equity injections.

Challenge History Fiscal Year Issued: 2001	Actions Accomplished (Green Status) during Past 4 FYs (Green actions move from “remaining actions” to this row after one year)			
	03-4	04-0	05-2	06-0
Remaining Recommended Actions for FY 2008				Status at end of FY 2007
1. Devote adequate resources to the purchase process.				Yellow ↑
2. Determine the level of improper payments for the entire loan portfolio in compliance with the Improper Payments Information Act of 2002 and OMB guidance.				Yellow ↑
3. Establish a process to identify and address the risks of improper payments.				Orange
4. Implement effective policies and procedures governing the guaranty purchase process (previously action #5).				Yellow

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 business concerns, and over the years has shifted from being an organization that processes loans to one that relies on program participants to originate, service and liquidate loans. This reliance requires an effective participant oversight program to monitor participant noncompliance with SBA policies and procedures and take corrective action when material noncompliance is detected.

The Agency improved its oversight process by establishing a Loan and Lender Monitoring System (L/LMS) that identifies potential and actual financial risks at the portfolio, lender and loan levels. L/LMS uses internal and external information to develop credit scores for each loan, aggregates the scores by lender, and produces ratings that measure lender loan portfolio performance. In addition, the Agency has established the responsibilities and authorities of the Office of Credit Risk Management (OCRM), established Portfolio Analysis and Lender Oversight committees to assess the portfolio and individual lender performance, commenced on-site reviews of large lenders and 504 program certified development companies (CDCs) and established a corrective action process for lenders requiring improved performance. OCRM also issued guidance for on-site lender and CDC reviews, including fees to be charged to support the oversight process.

To further improve the oversight program, among other things, the Agency needs to revise the lender rating process to ensure it accurately reflects each lender’s risk to SBA, conduct all required on-site reviews and examinations, identify and satisfy the staffing needed by OCRM to fully support the participant oversight mission, issue and abide by guidance designed to achieve the objectives of the lender oversight process, and demonstrate that corrective actions required of participants address the deficiencies noted.

Challenge History Fiscal Year Issued: 2001	Actions Accomplished (Green Status) during Past 4 FYs (Green actions move from “remaining actions” to this row after one year)				
	03-7(a)-3 03-SBIC-2 03-504-4	04-7(a)-7 04-504-7	05-7(a)-0 05-504-3	06-7(a)-2 06-501-1	
Remaining Recommended Actions for FY 2008				Status at end of FY 2007	
				7(a)	504
1. Implement a process that effectively assesses the level of financial risk of the portfolio, of participants, and of loans.				Yellow	Yellow
2. Implement a program to review lenders and CDCs for compliance risks (<i>previously action #3</i>).				Yellow	Yellow
3. Provide adequate personnel resources for the Office of Credit Risk Management (<i>previously action #4</i>).				Orange	Orange
4. Implement a formal training program for SBA and contractor personnel (<i>previously action #5</i>).				n/a	Green↑
5. Implement guidance providing for effective oversight of lending programs (<i>previously action #6</i>).				Orange↑	Orange↑
6. Ensure that effective corrective actions are implemented, monitored and result in improvement in the performance of participants with unacceptable performance (<i>previously action #7</i>).				Yellow↑	Orange

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

Challenge 6. The 8(a) program needs enhanced business development processes, objectively defined eligibility standards, upgraded training and information systems, improved graduation procedures, and better oversight of contractor compliance with program regulations.

SBA has not placed adequate emphasis on business development to enhance 8(a) firms' ability to compete, and does not adequately ensure that only 8(a) firms with economically disadvantaged owners in need of business development remain in the program. Allowing companies that are "business successes" to remain in the program and continue to receive 8(a) contracts can be a reason why a few companies receive most of the 8(a) contract dollars and many receive none. Recent data has shown that only a limited number of 8(a) firms are receiving a large percentage of dollars obligated against 8(a) contracts. Additionally, the program's primary database is ineffective and inefficient, and does not contain the information needed to successfully manage the program. Finally, while SBA has delegated its contract execution authority to 26 Federal procuring agencies, it has not conducted regular surveillance reviews to ensure that agencies were effectively monitoring compliance with program regulations on awarded contracts.

In FY 2007, SBA took the following steps to address this Challenge: (1) developed a process under which 8(a) firms would receive an individualized business development plan and SBA would track the level of assistance firms received from SBDCs and other entities; (2) drafted proposed regulations and internal procedures to improve graduation procedures; (3) provided regular training to SBA 8(a) employees; (4) revised its partnership agreements with procuring agencies to identify responsibilities for monitoring contract compliance with 8(a) regulations; and (5) clarified the responsibilities for SBA to undertake surveillance reviews to ensure that procuring agencies are monitoring compliance. However, much more work is needed.

Challenge History Fiscal Year Issued: 2003	Actions Accomplished (Green Status) during Past 4 FYs (Green actions move from "remaining actions" to this row after one year)			
	03-0	04-0	05-0	06-1
Remaining Actions Needed for FY 2008				Status at end of FY 2007
1. Develop and implement a plan, including Standard Operating Procedure (SOP) provisions, which ensures that the 8(a) program identifies the business development needs of the program participants on an individualized basis.				Orange↑
2. Develop and implement SOP provisions to ensure that participants are graduated once they reach the levels defined as "business success."				Orange↑
3. Establish criteria for reasonably redefining "economic disadvantage" using objective and reasonable criteria that effectively measures capital and credit opportunities, and implement the new definition.				Red
4. Provide sufficient financial and analytical training to business development specialists (BDS) to enable them to evaluate a company's business profile and competitive potential.				Yellow↑
5. Determine data needs to support and manage the 8(a) program and implement a management information system (MIS) that will support the program mission and objectives, provide useful information, and enable SBA to measure program results.				Orange
6. Revise the partnership agreements with procuring agencies to clearly require agencies to (1) monitor 8(a) companies compliance with program requirements, and (2) take steps to ensure that contracting officers and technical representatives are adequately advised of their responsibilities concerning 8(a) compliance.				Green
7. On a regular basis, conduct surveillance reviews of procuring agencies to ensure they are effectively monitoring and enforcing compliance with specified 8(a) regulations on the contracts they administer.				Orange

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

Challenge 7. Insufficient and outdated SBA controls continue the excessive risk of the SBIC program.

The Small Business Investment Company (SBIC) Program is designed to stimulate and supplement the flow of private equity capital and long-term debt to small business concerns. SBA uses both guaranteed debt (debentures) and equity interest (participating securities) to provide government-backed financing to SBICs. No new participating security SBICs have been licensed since funding for this program ended on September 30, 2004. As of September 2007, SBA had about \$10 billion of such financings at risk. The financial performance of the program for FY 1993 to FY 2004 resulted in about \$2 billion in higher costs to the Federal Government than originally anticipated. Government Accountability Office and Office of Inspector General (OIG) audits attributed these unanticipated costs to the structure of the SBIC program, the funding process, and the lack of focus on limiting costs when liquidating SBICs. The audits determined that: (1) the subsidy model underestimated the cost of the program; (2) SBA's profits were not proportional to its investments in the participating security SBICs; (3) insufficient incentives existed to encourage participating security SBICs to repay principal debt as quickly as possible; (4) SBA allowed too much time for financially troubled SBICs to attempt rehabilitation; (5) better performance goals and indicators were needed to show how well and how timely recoveries were maximized for liquidated SBICs; (6) Standard Operating Procedures (SOPs) for SBIC operations and liquidations were outdated; and (7) existing guidance did not provide a systematic approach for estimating the level of financial risk, implementing restrictive operations, transferring capially-impaired SBICs to liquidation status, liquidating SBICs with participating securities, and monitoring the liquidation of SBIC receiverships.

To address the Management Challenge, the Agency developed a new subsidy estimation methodology, issued a revised SOP for SBIC operations, is revising the SOP for SBIC Liquidations, revised contracts for receivership agents, and is filling personnel vacancies. Additional Agency actions required include demonstrating that SBICs are timely transferred into liquidation in accordance with revised guidance, ensuring quarterly risk assessments are performed and documented, and demonstrating timely and consistent implementation of restrictive operations. The Agency also must issue performance goals and indicators for the SBIC liquidation process and implement procedures for the liquidation of participating security SBICs and monitoring of SBICs in receivership.

Challenge History Fiscal Year Issued: 2004	Actions Accomplished (Green Status) during Past 4 FYs (Green actions move from "remaining actions" to this row after one year)		
	04-2	05-0	06-1
Remaining Recommended Actions for FY 2008			Status at end of FY 2007
1. Provide documented analysis justifying the capital impairment percentages (CIP) (<i>previously action #2</i>).			Green↑
2. Develop systematic criteria and implement a timely approach for transferring SBICs to liquidation status (<i>previously action #3</i>).			Yellow↑
3. Revise SOP 10 06 to include a process to perform and document quarterly risk assessments, including an analysis of repayment potential, and recommended actions (<i>previously action #4</i>).			Yellow↑
4. Incorporate into SOP 10 06 a requirement for the timely and consistent implementation of restrictive operations (<i>previously action #5</i>).			Yellow↑
5. Develop and implement performance goals and indicators that address the efficiency, cost-effectiveness, and timeliness of the SBIC liquidation process (<i>previously action #6</i>).			Orange
6. Develop and implement procedures, to be included in a revised version of SOP 10 07, that address the liquidation of participating security SBICs, and SBA monitoring of the liquidation of SBICs in receivership (<i>previously action #7</i>).			Orange↑

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

Challenge 8. Effective tracking and enforcement would reduce financial losses from loan agent fraud.

For years, 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 is limited, putting taxpayer dollars at risk. The Agency could reduce this risk if it established 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.

In response to this Challenge, SBA revised its E-Tran system, which is designed to collect loan data electronically from participating lenders as to whether a loan agent was involved with a loan. However, this process has proven to be an inefficient method of capturing data on loan agent involvement due to limitations in the E-Tran system and communication issues between the lender personnel that are involved in the loan decisions and those performing E-Tran data entry. Using E-Tran also did not resolve the issue of capturing data on loan agent activity from those lenders that did not use the system. Late in FY 2007, SBA proposed a new approach to address the Challenge. The Agency intends to integrate the collection of data from the Form 159 (which asks for information about loan agents) into the Form 1502 process. The Form 1502 is an electronically submitted report that lenders submit to describe the status of all SBA-guaranteed loans in their portfolio. This method of capturing the data is superior to using the E-Tran system because the 1502 is first submitted after the initial loan disbursement, so the lender should be aware of and able to report on loan agent activity, and because it is submitted by all 7(a) lenders. The approach is in the early planning stages, and the Agency will have to do a lot of work to make this an effective method of tracking loan agents.

The Agency has also 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, SBA needs to formally issue this checklist to make this official. The Agency must also make certain that it captures loan agent information electronically and links it to individual loans. SBA could then identify patterns of loan agent fraud and assess the various risks that loan agents present to the SBA’s portfolio of guaranteed loans. SBA also needs to establish a more effective enforcement program to deter fraudulent loan agent activity.

Challenge History Fiscal Year Issued: 2000	Actions Accomplished (Green Status) during Past 4 FYs (Green actions move from “remaining actions” to this row after one year)			
	03-0	04-0	05-0	06-0
Remaining Recommended Actions for FY 2008				Status at end of FY 2007
1. Ensure that the E-Tran system’s data fields require adequate disclosure of loan agent involvement and identity to track agent participation.				Orange
2. Ensure that SBA Form 159 or another SBA form requires disclosure of loan agent involvement and sufficient loan agent identity information to track agent participation.				Green↑
3. Provide guidance to lenders to ensure they enter correct loan agent data.				Orange
4. Compile loan agent information obtained from lenders not using E-Tran in a database or equivalent means that can link loan agents with individual loans.				Orange↑
5. Formally issue the guaranty purchase checklist to require that lenders submit the Form 159 to SBA at the time the Agency purchases a loan.				Yellow
6. Review loans for irregularities that could indicate loan agent fraud and abuse, and show that SBA is promptly and effectively exercising its regulatory authority to deter loan agent misconduct when warranted.				Yellow↑

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

Challenge 9. SBA needs to continue updating its system of directives to provide proper guidance and control over its operations.

SBA’s system of directives – used to implement policies and procedures that govern Agency programs – continues to need revision. SBA rules require that all long-term policies and procedures be implemented through permanent directives known as Standard Operating Procedures (SOPs). Yet, over the years, a number of Agency program offices had issued dozens of temporary notices to manage their programs either in lieu of SOPs or in conflict with existing SOPs, and had relied upon these notices even after they had expired. In other cases, obsolete directives (some dating back to the 1970s) had been neither cancelled nor updated even though they applied to programs that no longer exist or that had been substantially altered. The result has been an often incoherent and inefficient system that generated confusion and uncertainty in both SBA employees and the resource partners that rely on these directives, leading to uneven and potentially arbitrary application of policies and procedures, and reducing the effectiveness of the Agency’s internal controls system.

Fortunately, the Agency has made significant progress in resolving these issues. SBA revised its internal directive procedures to eliminate procedural deficiencies that contributed to these problems. The Agency has also implemented a system in which program managers must certify on an annual basis that SOPs for their respective programs are current or implement any needed update. Finally, the Agency is also methodically trying to keep SOPs current on both the internal and publicly available Web sites, although a limiting factor is the fact that a number of SOPs are still in the process of review and revision.

However, the remaining issue for the Agency is the update and revision of SOP 50 10, which governs SBA’s multi-billion dollar business loan programs. This SOP is currently over 700 pages long (including appendixes) and has not been updated for over almost seven years despite the introduction of several new lending programs. This SOP often provides outdated and confusing guidance to SBA employees that administer the small business loan programs and lenders participating in those programs. Since the last revision of the SOP in 2000, the Agency issued dozens of temporary notices implementing new policies and procedures, which has made it difficult to determine which policy or procedure applies. SBA has begun a revision of SOP 50 10, with a projected completion date of 12/31/2007.

Challenge History Fiscal Year Issued: 2004	Actions Accomplished (Green Status) during Past 4 FYs (Green actions move from “remaining actions” to this row after one year)			Status at end of FY 2007
	04-0	05-0	06-1	
Remaining Recommended Actions for FY 2008				
1. Complete the updating of all SOPs and incorporate relevant temporary directives into the SOPs (<i>previously action #2</i>).				Green↑
2. Update SOP 50-10 so that it contains current and clear guidance and is applicable only to loan making policies (<i>previously action #3</i>).				Orange
3. Implement a regular review mechanism to maintain SOPs so that they are up-to-date (<i>previously action #4</i>).				Green↑
4. Make current versions of all SOPs available electronically on SBA’s internal and publicly available Web sites and delete obsolete SOPs (<i>previously action #5</i>).				Green↑

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: www.sba.gov/ig/igreadingroom.html.

Challenge 1:

- SBA Advocacy, Analysis of Type of Business Coding for the Top 1,000 Contractors Receiving Small Business Awards in FY 2002, December 2004.
- 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.
- The Center for Public Integrity, The Pentagon's \$200 Million Shingle: Defense data shows billions in mistakes and mislabeled contracts, September 29, 2004.
- SBA OIG, Audit of SBA's Administration of the Procurement Activities of Asset Sale Due Diligence Contracts and Task Orders, Report #4-16, March 17, 2004, pp. 8-9.
- GAO, Contract Management: Reporting of Small Business Contract Awards Does Not Reflect Current Business Size, GAO-03-704T, May 7, 2003.
- The Small Business Committee, U.S. House of Representatives Hearing, Are Big Businesses Being Awarded Contracts Intended for Small Businesses? Testimony of Mr. Fred C. Armendariz, Associate Deputy Administrator, SBA, May 7, 2003.
- The Small Business Committee, U.S. House of Representatives Hearing, Are Big Businesses Being Awarded Contracts Intended for Small Businesses? Testimony of Mr. Felipe Mendoza, Associate Administrator, Office of Small Business Utilization, U.S. General Services Administration, May 7, 2003.
- SBA OIG, SBA Small Business Procurement Awards Are Not Always Going to Small Businesses, Report #5-14, February 24, 2005.
- SBA OIG, Review of Selected Small Business Procurements, Report #5-16, March 8, 2005.

Challenge 2:

- SBA OIG, Results of KPMG Vulnerability Assessment, Report #7-16, March 6, 2007
- SBA OIG, FISMA Independent Evaluation for FY 2006, Report #7-14, February 9, 2007
- SBA OIG, Memorandum Advisory Report on SBA's Protection of Sensitive Information, Report #7-13, February 9, 2007
- Audit of SBA OIG, Audit of SBA's Financial Statements for FY 2006, Report #7-03, November 15, 2006
- SBA OIG, FISMA Independent Evaluation for FY 2005, Report #6-01, October 7, 2005
- SBA OIG, Memorandum Advisory Report on SBA needs to Implement a Viable Solution to its Loan Accounting System Migration Problem, Report #5-29, September 30, 2005.
- SBA OIG, Audit of SBA's Information System Controls for FY 2004, Report #5-12, February 24, 2005.
- SBA OIG, Audit of SBA's Exchange Email System, Report #4-42, September 10, 2004.
- SBA OIG, Audit of Selected SBA General Support Computer Operating Systems, Report #4-41, September 10, 2004.
- SBA OIG, Audit of SBA's Information System Controls for FY 2003, Report #4-19, April 29, 2004.
- SBA OIG, Audit of SBA's Information System Controls for FY 2002, Report #3-20, March 31, 2003.

Challenge 3:

- OPM, 2006 Federal Human Capital Survey (FHCS), <http://www.fhcs2006.opm.gov/>
- 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, Small Business Administration: Progress Made, but Transformation Could Benefit from Practices Emphasizing Transparency and Communication, GAO-04-076, October 2003
- OMB, The President's Management Agenda and OMB's Human Capital Scorecard, <http://www.results.gov/agenda/fiveinitatives.html> <http://www.results.gov/agenda/departmentsupdates12.html>
- 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
- SBA OIG, Modernizing Human Capital Management, Report #2-20, May 31, 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, Audit of the Guarantee Purchase Process for Section 7(a) Loans at the National Guaranty Purchase Center, Report 37-23, May 8, 2007
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #7-17, March 12, 2007
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #7-15, February 12, 2007
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #7-10, January 16, 2007
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #7-09, January 9, 2007
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #7-07, December 29, 2006
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #7-06, December 28, 2006
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #7-05, December 20, 2006
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #7-02, October 23, 2006
- SBA OIG, Audit of Deficiencies in OFA's Purchase Review Process for Backlogged Loans, Report #6-35, September 29, 2006
- 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, Audit of an SBA Guaranteed Loan, Report #6-22, May 17, 2006
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #6-17, March 20, 2006
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #6-16, March 20, 2006
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #6-14, March 2, 2006
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #5-26, September 28, 2005
- SBA OIG, Audit of an SBA Guaranteed Loan, Report #5-21, July 15, 2005
- SBA OIG, Management Advisory Report on the Transfer of Operations to the National Guaranty Purchase Center, Report #4-39, August 31, 2004
- SBA OIG, Audit of an Early Defaulted Loan, Report #4-38, August 24, 2004
- SBA OIG, Audit of an Early Defaulted Loan, Report #4-33, July 30, 2004
- SBA OIG, Audit of an Early Defaulted Loan, Report #4-28, July, 9, 2004
- SBA OIG, Audit of an Early Defaulted Loan, Report #4-25, June 22, 2004
- SBA OIG, Audit of an Early Defaulted Loan, Report #4-06, January 8, 2004
- SBA OIG, Audit of an Early Defaulted Loan, Report #3-38, September 22, 2003
- SBA OIG, Audit of an Early Defaulted Loan, Report #3-30, June 19, 2003
- SBA OIG, Audit of an Early Defaulted Loan, Report #3-27, May 22, 2003
- SBA OIG, Audit of the Guaranty Purchase Process, Report #3-15, March 17, 2003
- SBA OIG, Audit of an Early Defaulted Loan, Report #3-07, January 23, 2003
- SBA OIG, Audit of an Early Defaulted Loan, Report #2-32, September 30, 2002
- SBA OIG, Audit of an Early Defaulted Loan, Report #2-30, September 24, 2002
- SBA OIG, Audit of an Early Defaulted Loan, Report #2-23, August 7, 2002

- SBA OIG, Audit of an Early Defaulted Loan, Report #2-15, March 29, 2002
- SBA OIG, Improvements are Needed in Small Business Lending Company Oversight Process, Report #2-12, March 21, 2002
- SBA OIG, Audit of an Early Defaulted Loan, Report #2-03, February 27, 2002
- SBA OIG, Audit of an Early Defaulted Loan, Report #2-05, February 27, 2002
- SBA OIG, Audit of an Early Defaulted Loan, Report #1-10, March 9, 2001
- GAO, Major Management Challenges and Program Risks, GAO-01-260, January 2001
- SBA OIG, Audit of an Early Defaulted Loan, Report #0-10, April 23, 2000
- SBA OIG, Audit of an Early Defaulted Loan, Report #0-12, March 28, 2000
- SBA OIG, Audit of an Early Defaulted Loan, Report #0-05, February 14, 2000

Challenge 5:

- GAO, Small Business Administration: Additional Measures Needed to Assess 7(a) Loan Program's Performance, GAO-07-769, July 13, 2007
- SBA OIG, SBA's Oversight of Business Loan Center, LLC, Report #7-28, July 11, 2007.
- SBA OIG, SBA's Use of the Loan and Lender Monitoring System, Report #7-21, May 2, 2007.
- SBA OIG, Audit of the Office of Lender Oversight Corrective Action Process, Report #7-18, March 14, 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, Small Business Administration: New Service for Lender Oversight Reflects Some Best Practices, But Strategy for Use Lags Behind, GAO-04-610, June 8, 2004
- 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 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.

Challenge 7:

- SBA OIG, Audit of SBIC Liquidations Process, Report #5-22, July 28, 2005
- SBA OIG, The SBIC Program: At Risk for Significant Losses, Report #4-21, May 24, 2004
- OMB, Small Business Administration: PART Assessment on the SBIC Program, February 2, 2004
- SBA OIG, FY 2003 Financial Statement Audit in the SBA FY 2003 Performance and Accountability Report, January 30, 2004, pp. 230-60
- SBA OIG, Audit of SBIC Oversight, Report #3-33, July 1, 2003
- GAO, Small Business: Update on SBA's Small Business Investment Company Program, GAO/RCED-97-55, February 1997
- GAO, Small Business Administration: SBA Monitoring Problems Identified in Case Studies of 12 SBICs and SSBICs, GAO/OSI-96-3, April 1996

- GAO, Small Business Administration: Better Oversight of SBIC Programs Could Reduce Federal Losses, GAO/T-RCED-95-285, September 28, 1995
- GAO, Small Business Administration: Inadequate Oversight of Capital Management Services, Inc.-An SSBIC, GAO/T-OSI-95-19, August 7, 1995
- GAO, Small Business Administration: Prohibited Practices and Inadequate Oversight in SBIC and SSBIC Programs, GAO/OSI-95-16, May 28, 1995
- GAO, Small Business Administration: Inadequate Oversight of Capital Management Services, Inc.-An SSBIC, GAO/OSI-94-23, March 1994
- SBA OIG, Audit Report on the Small Business Investment Company (SBIC) Liquidation Function, Report #3-2-E-004-031, March 31, 1993

Challenge 8:

- 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 9:

- SBA OIG, Audit of SBIC Oversight, Report #3-33, July 1, 2003
- SBA OIG, Problems with SBA's Directives System, Advisory Memorandum #3-28, May 22, 2003
- SBA OIG, Guaranty Purchase Processing: Directors' Survey Responses and Loan Officers' Survey Responses, Report #3-16, March 18, 2003
- SBA OIG, Audit of the Guaranty Purchase Process, Report #3-15, March 17, 2003
- SBA OIG, The Microloan Program: Moving Toward Performance Management, Report #3-26, May 13, 2003
- SBA OIG, Standard Operating Procedure 00-11, Memorandum, December 17, 2002
- SBA OIG, Travel of SBA's Former Regional Administrator, Report #2-22, August 7, 2002