

U.S. SMALL BUSINESS ADMINISTRATION

OFFICE OF INSPECTOR GENERAL

Report No. 10-02

*Fiscal Year 2010 Report
on the Most Serious Management and
Performance Challenges Facing the
Small Business Administration*

October 16, 2009



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

October 16, 2009

MEMORANDUM

TO: Karen G. Mills
Administrator

FROM: Peggy E. Gustafson
Inspector General

A handwritten signature in black ink, appearing to read "Peggy E. Gustafson".

SUBJECT: Fiscal Year 2010 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) 2010 Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration (SBA). This report represents our current assessment of Agency programs and/or activities that pose significant risks, including those that are particularly vulnerable to fraud, waste, error, mismanagement or inefficiencies. The Challenges are not presented in order of priority, as we believe that all are critical management or performance issues.

Our report is based on specific OIG, Government Accountability Office (GAO), and other official reports, as well as our general knowledge of SBA's programs and operations. Our analysis generally considers those accomplishments that SBA reported as of September 30, 2009.

Within each Management Challenge there are a series of "recommended actions" to resolve the Challenge. Each recommended action is assigned a color "status" score. The scores are as follows: Green for Implemented; Yellow for Substantial Progress; Orange for 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. In addition, actions that were scored Green last year, and which remained Green this year, have been moved up to the "history bar" above the recommended actions. The history bar highlights any progress that the Agency has made on a Challenge over the past four FYs (or as long as the Challenge has existed, if shorter) by showing the number of actions that have moved to Green each year.

This year's report contains two new Management Challenges dealing with (1) SBA's Loan Management and Accounting System (LMAS) project, and (2) improper payments in the Disaster and 7(a) loan programs. Since these two Management Challenges are new, no color

scores have been assigned; the Agency's progress in resolving them will be assessed during FY 2010 and color scores will be assigned in next year's report.

Following is a summary of the FY 2010 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	1		1
2	IT Security		4			0
3	Human Capital		3			0
4	Loan Guaranty Purchase		1	1		0
5	Lender Oversight		2	4		0
6	8(a) BD Program	1	4			3
7	SBIC Program	2	2			2
8	Loan Agent Fraud			2		-- ²
9	Loan Management and Accounting System					New
10	Improper Payments					New
	TOTAL	3	18	8	0	6

We would like to thank SBA's management and staff for their cooperation in providing us with information needed to prepare this report. We look forward to working with SBA's new leadership team in addressing the Agency's Management Challenges.

Attachment

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

² Management Challenge 8, Loan Agent Fraud, was revised in FY 2009 to include two new recommended actions. Consequently, no color scores were shown for these two remaining recommended in last year's report against which to measure progress.

Table of Contents

	Page
Challenge 1. Procurement flaws allow large firms to obtain small business awards and agencies to count contracts performed by large firms towards their small business goals.....	1
Challenge 2. Weaknesses in information systems security controls pose significant risks to the Agency.....	2
Challenge 3. Effective human capital strategies are needed to enable SBA to successfully carry out its mission and become a high-performing organization.	3
Challenge 4. SBA needs better controls over loan purchase and liquidation processes.....	4
Challenge 5. SBA needs to further strengthen its oversight of lending participants.	5
Challenge 6. The Section 8(a) Business Development program needs to be modified so more firms receive business development assistance, standards for determining economic disadvantage are clear and objective, and SBA ensures that firms follow 8(a) regulations when completing contracts.....	6
Challenge 7. Insufficient and outdated SBA controls contribute to excessive risk of the SBIC program.	7
Challenge 8. Effective tracking and enforcement would reduce financial losses from loan agent fraud.....	8
Challenge 9. SBA needs to modernize its Loan Accounting System and migrate it off the mainframe	9
Challenge 10. SBA needs to accurately report, significantly reduce, and strengthen efforts to recover improper payments in the Disaster and 7(a) loan programs.....	10
Appendix: Relevant Reports	11

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 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 that procuring agencies accurately report contracts awarded to small businesses when representing its progress in meeting small business contracting goals.

Office of Inspector General (OIG) audits and other governmental studies have shown widespread misreporting by procuring agencies; many contract awards recorded as going to small firms have actually been performed by larger companies. While some contractors may misrepresent or erroneously calculate their size, most incorrect reporting results from errors made by government contracting personnel. Noted errors include acceptance of questionable size self-certifications and misapplication of small business contracting rules. Also, it is unclear whether contracting officers always review the on-line certifications that contractors enter into the governmental Online Representations and Certifications Application (ORCA) prior to awarding contracts. SBA needs to do more to ensure that contracting personnel are adequately trained on small business procurement procedures and are reviewing ORCA data prior to awarding contracts.

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

While more remains to be done, SBA made some progress on this challenge as it: (1) developed a strategy for promoting and encouraging procurement officials to be trained on small business contracting procedures; (2) conducted surveillance reviews to assess whether procurement officials confirmed the small business size status prior to contract award, and (3) provided anomaly reports to Federal agencies procurement officials that identified potentially miscoded business size status for correction.

Challenge History Fiscal Year (FY) Issued: 2005	Actions Accomplished (Green Status) during Past 4 FYs			
	N/A	06-0	07-0	08-1
Remaining Recommended Actions for FY 2010				Status at end of FY 2009
1. Develop and take steps to provide reasonable assurance that agencies are providing adequate basic and continuing education training to contracting personnel on small business contracting procedures.				Yellow ↑
2. Develop and implement a program that promotes accurate contractor certifications and ensures that contracting personnel review contractor certifications.				Yellow
3. Issue regulations that require firms to meet the size standard for each specific order they receive under a GSA schedule and Governmentwide Acquisition Contract (GWAC) and show that the regulations are being followed. (Previously action # 4)				Orange

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

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

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

SBA continued to improve information system security in several critical areas during FY 2009. The Agency established a vulnerability assessment team (VAT) which performs monthly scans of network attached devices to identify and remediate network vulnerabilities; implemented procedures for requesting and granting remote access and for sanitization of used media prior to disposal; made progress documenting LAS and DCMS configuration baselines and implementing segregation of duties controls in LAS; and developed guidance on how contractor access vulnerabilities should be reported in the Plan of Actions and Milestones (POA&M) and now requires documentation justifying removal of prior vulnerabilities from the POA&M. To show further progress, SBA needs to address both known and newly-reported information security issues. For example, SBA needs to implement a process to more timely mitigate system risks that are identified as “medium” and “high” and ensure that all security weaknesses identified in risk assessments as “high” are included in the POA&M; further implement enterprise-wide and application level change control controls for both emergency and normal system changes; and ensure that critical controls such as patch management are addressed in service level agreements with contractors and hosting sites.

Challenge History Fiscal Year (FY) Issued: 1999	Actions Accomplished (Green Status) during Past 4 FYs			
	05-2	06-2	07-2	08-2
Remaining Recommended Actions for FY 2010				Status at end of FY 2009
1. Access controls are in place and operating effectively, and contractors are not granted system access until they have obtained the required background investigations and/or security clearances.				Yellow
2. System software controls are in place and operating effectively.				Yellow
3. Segregation of duty controls are in place and operating effectively.				Yellow
4. The POA&M accurately reports all computer security weaknesses and corrective actions. (Previously action #5)				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 constraints, 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 was no assurance that sufficient resources—in terms of both number of staff and the knowledge and skills possessed by staff—were available and appropriately deployed to perform critical functions. For example, audits showed that inadequate staffing of key functions resulted in limited oversight of lenders and inadequate monitoring of 8(a) program requirements.

The results of the 2002, 2004 and 2006 Federal Human Capital Surveys (FHCS) illustrated SBA’s serious human capital challenges. For example, in 2006 SBA ranked near the bottom on all four human capital indices—Leadership and Knowledge Management, Results-Oriented Performance Culture, Talent Management, and Job Satisfaction. SBA’s scores were particularly low related to the adequacy of job-related knowledge and skills, the reasonableness of workload, sufficiency of information needed to go a good job, and employee morale.

SBA was proactive in addressing the results of the 2006 FHCS. As a result, the 2008 survey showed significant improvement. For example, on the four indices identified above, SBA’s rankings moved from 33rd to 22nd, 32nd to 26th, 35th to 31st, and 34th to 27th, respectively. In addition, the Partnership for Public Service, in its 2009 rankings of the best places to work in the Federal Government, recognized SBA as the most improved agency, although SBA still ranked 26 out of 30 large agencies. SBA has also focused considerable attention on improving workforce planning and employee development. Human capital management continues to be a significant challenge, however, requiring continued attention to ensure that qualified staff are available and appropriately allocated toward SBA’s mission-critical functions and identified priorities.

Challenge History Fiscal Year (FY) Issued: 2001 (Revised 2007)	Actions Accomplished (Green Status) during Past 4 FYs			
	05-0	06-0	07-0	08-0
Remaining Recommended Actions for FY 2010				Status at end of FY 2009
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.				Yellow
2. Take steps to correct problems identified by the Federal Human Capital Survey (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.				Yellow
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.				Yellow

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

Challenge 4. SBA needs better controls over loan purchase and liquidation processes.

The majority of loans 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. Furthermore, as lenders are delegated the responsibility for servicing and liquidating SBA loans, SBA’s liquidation process, including the comprehensive charge-off review, is the last opportunity to identify lender noncompliance. However, OIG audits of defaulted loans and SBA’s guaranty purchase and liquidation processes have shown that reviews performed by the loan centers have not consistently detected failures by lenders 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. SBA reengineered the 7(a) loan guaranty purchase processes at the National Guaranty Purchase Center (NGPC) and the Little Rock and Fresno Service Centers to improve the efficiency and consistency of the process; increased staffing levels at the centers; developed a comprehensive operations manual for the NGPC; trained individuals responsible for making purchase decisions; and made significant progress in developing a quality assurance program. While improvements have been made, additional actions are needed to strengthen guaranty purchase and liquidation decisions to effectively reduce improper payments, such as implementing effective policies and procedures governing the guaranty purchase and liquidation processes and fully implementing the quality assurance program at the centers.

Challenge History Fiscal Year (FY) Issued: 2001	Actions Accomplished (Green Status) during Past 4 FYs			
	05-2	06-0	07-0	08-2
Remaining Recommended Actions for FY 2010				Status at end of FY 2009
1. Implement a Quality Assurance Program for all SBA loan centers. <i>(Previously action #3)</i>				Orange
2. Implement policies and procedures governing the guaranty purchase and liquidation processes to ensure lender compliance before honoring SBA loan guaranties. <i>(Previously action #4)</i>				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 businesses. Over the years, SBA has shifted from processing loans to overseeing lenders originate, service, and liquidate loans. This requires an effective oversight program to: (1) monitor lender compliance with SBA policies and procedures, and (2) take corrective actions when material noncompliance are detected.

The Agency has made substantial progress in its oversight of lenders in the 7(a) and 504 loan programs, reducing action items within this Management Challenge from 8 in FY 2006 to 3 in FY 2009. With authority to charge fees to cover the cost of on-site lender reviews, SBA expanded the scope of its oversight by more than doubling the number of on-site reviews of large high-risk lenders. It also issued a Lender Review Standard Operating Procedure (SOP) to guide the on-site review process and modified the Lender Risk Rating System to further strengthen lender risk assessments. In January 2009, SBA published an Interim Final Rule that outlined its policy on enforcement actions against nonperforming lenders. This rule identified the types of enforcement actions that could be exercised, grounds for enforcement action, and processes for implementing such actions. Subsequent to publishing the rule, the Agency drafted, but did not finalize, a Lender Enforcement SOP, which contains guidance for implementing enforcement actions. Finally, in FY 2009, SBA evaluated the sufficiency of over 180 corrective actions proposed by lenders and developed guidelines for establishing lender performance measures that will be incorporated into the Lender Enforcement SOP. The guidelines will assist the Office of Credit Risk Management (OCRM) in establishing lender performance goals and target dates for inclusion in lender corrective action plans.

To progress further, SBA will need to conduct agreed-upon-procedure reviews of medium-sized, high-risk lenders and ensure that its on-site reviews are based on statistically-valid samples of lender loan files. While OCRM has drafted agreed-upon-procedures for the reviews of medium-sized lenders and has developed possible statistical approaches for reviewing loan files, it has not finalized its plans in either area. SBA will also need to finalize the Lender Enforcement SOP so that it can establish performance measures in lender corrective action plans.

Challenge History Fiscal Year (FY) Issued: 2001	Actions Accomplished (Green Status) during Past 4 FYs			
	05-7(A)-0 05-504-3	06-7(a)-2 06-504-1	07-7(a)-0 07-504-1	08-7(a)-2 08-504-2
Remaining Recommended Actions for FY 2010	Status at end of FY 2009			
	7(a)	504		
1. Expand the scope of lender oversight and improve the process for reviewing lenders and Certified Development Companies (CDCs) for compliance risks. <i>(Previously action #2)</i>	Yellow	Yellow		
2. Implement guidance providing for effective oversight of lending programs. <i>(Previously action #4)</i>	Orange	Orange		
3. Ensure that effective corrective actions are implemented, monitored, and result in improvement in the performance of participants with unacceptable performance. <i>(Previously action #5)</i>	Orange	Orange		

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

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

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

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

The Agency has made considerable progress in addressing issues that challenge its ability to deliver an effective 8(a) program. The Office of Business Development has developed a Business Development Assessment Tool, as well as a plan to provide 8(a) firms with individualized business development assistance. In addition, the Office of Business Development has strengthened its policies and procedures and revised its regulations to ensure that companies that are “business successes” are graduated from the program. Further, the Agency has issued proposed regulations establishing objective standards to address the definition of “economic disadvantage,” and has addressed the need to identify the skills necessary for Business Development Specialists to adequately evaluate a company’s business plan and assess a participant’s competitive potential. The Agency needs to ensure that procuring agencies enforce contractors’ compliance with 8(a) BD program regulations and finalize regulations to complete the recommended actions.

Challenge History Fiscal Year (FY) Issued: 2003	Actions Accomplished (Green Status) during Past 4 FYs			
	05-0	06-1	07-1	08-1
Remaining Recommended Actions for FY 2010				Status at end of FY 2009
1. Develop and implement a plan, including SOP provisions, which ensures that the 8(a) BD program identifies and addresses the business development needs of program participants on an individualized basis.				Yellow ↑
2. Develop and implement Regulations and SOP provisions to ensure that participants are graduated once they reach the levels defined as business success.				Yellow
3. Establish objective criteria that reasonably measures “economic disadvantage” and implement the new criteria.				Yellow ↑
4. Provide sufficient financial and analytical training to business development specialists to enable them to evaluate a company’s business profile and competitive potential.				Green ↑
5. On a regular basis, conduct surveillance reviews of procuring agencies to ensure they are effectively monitoring and enforcing compliance with specified 8(a) BD regulations on the contracts they administer. (Previously action #6)				Yellow

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

Challenge 7. Insufficient and outdated SBA controls contribute to 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. As of September 30, 2009, SBA had about \$8.2 billion of such financings at risk. From FY 1993 to FY 2004, program costs were about \$2 billion more than anticipated. Prior audits performed by the Government Accountability Office (GAO) and the OIG attributed the unanticipated costs to the structure of the 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) SOPs for SBIC operations and liquidations were outdated; and (7) existing guidance did not provide a systemic approach for estimating the level of financial risk, implementing transfers to restrictive operation status, transferring capitally-impaired SBICs to liquidation status, liquidating SBICs with participating securities, and monitoring the liquidation of SBIC receiverships.

From FY 2005 to FY 2009, however, the program has been self-sustaining, with fees covering all losses. SBA has also demonstrated that it transferred 30 of 33 SBICs into restrictive operations in a timely manner, that self-liquidation procedures for participating security SBICs were followed, and that effective monitoring of SBIC receiverships was accomplished through oversight reports and documented quarterly meetings with receivership personnel. These actions are sufficient to elevate to green the scores for two of the four remaining recommended actions for this Management Challenge.

To further reduce risk in the program, SBA needs to more timely transfer debenture funded SBICs into liquidation and implement performance goals and indicators that address the efficiency, cost-effectiveness, and timeliness of the SBIC liquidation process. An analysis of 12 debenture funded SBICs transferred into liquidation status between September 2007 and 2009 showed that the majority of these transfers were not timely; the OIG found that at least 7 were transferred into liquidation status 12 months or more after exceeding their maximum capital impairment percentage. Also, after establishing goals and performance indicators to evaluate the liquidation of SBICs, SBA must demonstrate their effectiveness.

Challenge History Fiscal Year (FY) Issued: 2004	Actions Accomplished (Green Status) during Past 4 FYs			
	05-0	06-1	07-1	08-1
Remaining Recommended Actions for FY 2010				Status at end of FY 2009
1. Develop systematic criteria and implement a timely approach for transferring SBICs to liquidation status.				Yellow
2. Incorporate into SOP 10 06 a requirement for the timely and consistent implementation of restrictive operations. <i>(Previously action #3)</i>				Green↑
3. Develop and implement performance goals and indicators that address the efficiency, cost-effectiveness, and timeliness of the SBIC liquidation process. <i>(Previously action #4)</i>				Yellow
4. 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 #5)</i>				Green↑

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 has been limited, putting taxpayer dollars at risk. The Agency could reduce this risk by establishing effective loan agent disclosure requirements, a database or equivalent means to track loan agent involvement with its loans, and a more effective agent enforcement program.

In response to this Management Challenge, SBA had proposed to revise its E-Tran system (which is designed to collect loan data electronically from participating lenders) to collect information on loan agent involvement. The Agency concluded, however, that this would not address the problem due to limitations in the E-Tran system and communication issues between lender personnel involved in loan decisions and those performing E-Tran data entry. In addition, many lenders were not using E-Tran. In late FY 2007, SBA proposed a new approach. 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 SBA’s Fiscal and Transfer Agent (FTA) to describe the status of all SBA-guaranteed loans in their portfolios. This method of capturing the data is superior to using the E-Tran system because: (1) the 1502 is first submitted after the initial loan disbursement, so a lender should be aware of and able to report on loan agent activity, and (2) the 1502 is submitted by all 7(a) lenders. Accordingly, in FY 2008, the OIG issued the revised recommended action #1 below. SBA made no progress on this action during FY 2008, in part due to a protest of the award of the FTA contract to what would have been a new vendor. At the end of FY 2009, SBA devised a succinct plan for implementing the 1502 approach.

In FY 2007, the Agency made progress by issuing its Lender Oversight SOP and by previously revising the guaranty purchase checklist (which lists the records that lenders need to provide when requesting SBA to pay a guaranty) to include the submission of the Form 159. However, the Agency also needs to establish a more effective enforcement program to deter fraudulent loan agent activity. As a first step, SBA issued for clearance at the end of FY 2009 a draft SOP revision with loan agent enforcement procedures.

Challenge History Fiscal Year (FY) Issued: 2000	Actions Accomplished (Green Status) during Past 4 FYs			
	05-0	06-0	07-1	08-1
Remaining Recommended Actions for FY 2010				Status at end of FY 2009
1. Develop an effective method of disclosing and tracking loan agent involvement in the SBA business loan programs.				Orange
2. Implement procedures for enforcement actions against loan agents for improper and fraudulent conduct. (Previously action #3)				Orange

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

Challenge 9. SBA needs to modernize its Loan Accounting System and migrate it off the mainframe.

In November 2005, SBA initiated the Loan Management and Accounting System (LMAS) project, which is the latest in a series of attempts to update the Agency’s Loan Accounting System (LAS) and migrate it off of the mainframe. With an estimated cost of over \$250 million, LMAS is SBA’s largest IT project. When completed, it will increase functionality, reduce data entry redundancies, and allow real-time updates and inquiry of loan data. Previous OIG reports have stressed the urgency of replacing the current loan accounting system, which presents substantial risk to SBA. The system is dangerously close to the end of its expected useful life, relies on obsolete technology, contains major security vulnerabilities that cannot be addressed until the system is moved to a new operating platform, and is costly to operate.

Despite the cost and risks associated with the current system, SBA was unable to replace LAS prior to the expiration of the mainframe contract in February 2007, and subsequently extended the contract to 2012. SBA also revised its acquisition strategy in May 2008 from a requirements-based approach to one that relies on a provider to design a system that best meets SBA’s business objectives. Consequently, the project is still in the planning phase. Additionally, recent OIG reports have raised concerns about how the project was being managed. The OIG reported that the project did not comply with SBA’s System Development Methodology in key quality assurance and earned value management areas, which threatened SBA’s ability to control LMAS costs and quality. The OIG also reported that SBA had not established either an enterprise-wide or project-level Quality Assurance (QA) function to ensure that project deliverables meet SBA’s requirements and quality standards. Finally, the OIG reported that the project lacked a defined process for reviewing and accepting deliverables that complied with SBA’s Systems Development Methodology.

Challenge History Fiscal Year (FY) Issued: 2010	Actions Accomplished (Green Status) during Past 4 FYs			
	N/A	N/A	N/A	N/A
Recommended Actions for FY 2010				Status at end of FY 2009
1. Migrate LAS to a new operating platform before the current mainframe contract expires in 2012.				New
2. Modify the LMAS QA/IV&V contract to require the contractor to report all findings and recommendations to the Program Manager <i>and</i> an independent QA manager.				New
3. Establish a process for reviewing and accepting LMAS deliverables that complies with SDM requirements.				New

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

Challenge 10. SBA needs to accurately report, significantly reduce, and strengthen efforts to recover improper payments in the Disaster and 7(a) loan programs.

Recent OIG audits of SBA’s Disaster and 7(a) Loan Programs determined that the improper payment rates reported for these programs were significantly understated. SBA estimated that improper payments in the Disaster Loan Program were about \$4.5 million, or 0.55 percent of the \$819.7 million in loans approved in FY 2007, while the OIG reported that it was at least 46 percent, or approximately \$1.5 billion. SBA also reported that the improper payment rate for the 7(a) program was 0.53 percent of FY 2008 program outlays, although the OIG estimated the rate to be 27 percent, or approximately \$234 million. SBA’s improper payment rates were understated because the Agency did not adequately review sampled loans, used flawed sampling methodologies, and did not accurately project review findings for both programs. Additionally, the Office of Financial Assistance inappropriately overturned improper payments identified by reviewers.

OIG audits in prior years have also identified high percentages of disaster and business loans that were made to borrowers who were ineligible, lacked repayment ability, or did not provide the required supporting documentation required for loan disbursement. In 2008, we reported that 63 percent of early defaulted Gulf Coast loans reviewed went to individuals who lacked repayment ability, and that half of the loans reviewed in another audit were disbursed without securing all the documentation needed to secure SBA’s interest in the property. In 2009, we reported that over 30 percent of reviewed disaster loans were disbursed for properties that were not the applicant’s primary residence. Further, audits in 2009 of SBA’s post purchase and liquidation processes for 7(a) loans identified an estimated \$30 million in improper loan guaranty purchases. Finally, SBA has not aggressively pursued recovery of improper payments, recovering only about 1 percent of the improper payments identified during its FY 2007 and FY 2008 improper payment reviews.

Challenge History Fiscal Year (FY) Issued: 2010	Actions Accomplished (Green Status) during Past 4 FYs			
	N/A	N/A	N/A	N/A
Recommended Actions for FY 2010	Status at end of FY 2009			
	Disaster	7(a)		
1. Ensure that processes used to calculate the improper payment rate for disaster and 7(a) loans are designed to identify all potential improper payments as defined by Office of Management and Budget (OMB) Circular A-123.	New	New		
2. Reassign responsibility for final approval of disputed denial, repair, and improper payment decisions from the Office of Financial Assistance to the Office of Risk Management.	New	New		
3. Develop a process to ensure that reviewers are properly trained to perform improper payment reviews.	New	New		
4. Develop and implement corrective action plans to reduce improper payments in the 7(a) and Disaster Loan programs.	New	New		
5. Establish a process and time standards to expeditiously recover improper payments identified during Agency reviews and OIG audits.	New	New		

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

Appendix: Relevant Reports

Most of the SBA OIG reports listed can be found at
<http://www.sba.gov/ig/onlinelibrary/oigreports/index.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, Review of Allegations Concerning How the LMAS Modernization Project is Being Managed, Report #9-17, July 30, 2009
- SBA OIG, System Access By Contractors Without Security Clearances, Report #9-07, January 26, 2009
- SBA OIG, SBA's FY2008 Financial Statements-Management Letter, Report #9-05, December 17, 2008
- SBA OIG, SBA's FY2008 Financial Statements, Report #9-03, November 14, 2008
- SBA OIG, SBA's Implementation of an HSPD-12 Card Issuance System, Report #9-01, October 6, 2008
- SBA OIG, Planning for the Loan Management and Accounting System Modernization and Development Effort, Report #8-13, May 14, 2008
- SBA OIG Audit of SBA's FY 2007 Financial Statements, Report #8-03, November 15, 2007.
- SBA OIG, Audit of Controls Over Access to Employee Emails by SBA Managers, Report #8-02, October 19, 2007.
- 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:

- Partnership for Public Service, Best Places to Work in the Federal Government 2009, <http://data.bestplacetowork.org/bptw/index>
- OPM, 2008 Federal Human Capital Survey (FHCS), <http://www.fhcs.opm.gov/>
- GAO, Opportunities Exist to Build on Leadership's Efforts to Improve Agency Performance and Employee Morale, GAO-08-995, September 2008
- SBA OIG, Non-Native Managers Secured Millions of Dollars from 8(a) Firms Owned by Alaska Native Corporations through Unapproved Agreements that Jeopardize the Firms' Program Eligibility, Report #8-14, August 7, 2008
- 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
- 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, SBA's Management of the Backlog of Post-purchase Reviews at the National Guaranty Purchase Center, #9-18, August 25, 2009
- SBA OIG, , The Small Business Administration's Fiscal Year 2008 Improper Payment Rate for the 7(a) Guaranty Loan Program #9-16, July 10, 2009
- SBA OIG, Review of Key Unresolved OIG Audit Recommendations in Program Areas Funded by the American Recovery and Reinvestment Act and Related Activities Need to Safeguard Funds, #ROM 09-1, April 30, 2009
- SBA OIG, Audit of the Liquidation Process at the National Guaranty Purchase Center, #9-08, January 30, 2009
- SBA OIG, Audit of Six SBA Guaranteed Loans, #8-18, September 8, 2008
- SBA OIG, Audit of Loan Classifications and Overpayments on Secondary Market Loans, #8-09, March 26, 2008
- SBA OIG, Audit of UPS Capital Business Credit's Compliance with Selected 7(a) Lending Requirements, #8-08, March 21, 2008
- SBA OIG, Audit of the Guarantee Purchase Process for Section 7(a) Loans at the National Guaranty Purchase Center, Report #7-23, May 8, 2007
- SBA OIG, 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:

- SBA OIG, SBA's Oversight of SBA Supervised Lenders, Report #8-12, May 9, 2008
- SBA OIG, UPS Capital Compliance with Selected 7(a) Lending Requirements, Report #8-08, March 21, 2008
- GAO, Small Business Administration: Additional Measures Needed to Assess 7(a) Loan Program's Performance, GAO-07-769, July 13, 2007
- 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 Two 8(a) Sole –Source Contracts Awarded to Contractors in SBA’s Mentor Protégé Program, Report #7-19, March 30, 2007.
- SBA OIG, Audit of Monitoring Compliance with 8(a) Business Development Regulations During 8(a) Business Development Contract Performance, Report #6-15, March 16, 2006.
- SBA OIG, Business Development Provided by SBA’s 8(a) Business Development Program, Report #4-22, June 2, 2004.
- SBA OIG, SACS/MEDCOR: Ineffective and Inefficient, Report #4-15, March 9, 2004.
- SBA OIG, Section 8(a) Program Continuing Eligibility Reviews, Report #4-3-H-006-021, September 30, 1994

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, Review of Allegations Concerning How the Loan Management and Accounting System Modernization Project is Being Managed, Report #9-17 July 30, 2009
- SBA OIG, Planning for the Loan Management and Accounting System Modernization and Development Effort, Report #8-13, May 14, 2008
- SBA OIG, SBA Needs to Implement a Viable Solution to its Loan Accounting System Migration Problem, Report #5-29, September 20, 2005
- GAO, Information Technology: Agencies Need to Improve the Accuracy and Reliability of Investment Information, GAO-06-250, January 12, 2006.
- GAO, Major Management Challenges and Program Risks: Small Business Administration, GAO-03-116, January 1, 2003
- GAO, SBA Loan Monitoring System: Substantial Progress Yet Key Risks and Challenges Remain, Testimony of Joel C. Willemsen, Director, Civil Agencies Information Systems Accounting and Information Management Division, Before the Subcommittee on Government Programs Statement Committee on Small Business, House of Representatives, GAO/T-AIMD-00-113, February 29, 2000
- GAO, SBA Needs to Establish Policies and Procedures for Key IT Processes, Accounting and Information Management Division, GAO/AIMD-00-170, May 31, 2000

Challenge 10:

- SBA OIG, SBA's Management of the Backlog of Post-Purchase Reviews at the National Guaranty Purchase Center, Report #9-18, August 25, 2009
- SBA OIG, The Small Business Administration's Fiscal Year 2008 Improper Payment Rate for the 7(a) Guaranty Loan Program, Report #9-16, July 10, 2009
- SBA OIG, Audit of Borrower Eligibility for Gulf Coast Disaster Loans, Report #9-09, March 31, 2009
- SBA OIG, The Small Business Administration's Fiscal Year 2007 Improper Payment Rate for the Disaster Loan Program, Report #9-10, March 26, 2009
- SBA OIG, Audit of the Liquidation Process at the National Guaranty Purchase Center, Report #9-08, January 30, 2009
- SBA OIG, The Use of Proceeds From Gulf Coast Disaster Loans, Report #9-06, January 15, 2009
- SBA OIG, Disaster Loss Verification Process, Report #8-15, June 17, 2008
- SBA OIG, Review of the Adequacy of Supporting Documentation for Disbursements, Report #8-07, January 29, 2008
- SBA OIG, The Quality of Loans Processed Under the Expedited Disaster Loan Program, Report #7-34, September 28, 2007
- SBA OIG, SBA's Quality Assurance Reviews of Loss Verifications, Report #7-29, July 23, 2007
- SBA OIG, Securing Collateral for Disaster Loan Disbursements, Report #7-22, May 9, 2007