

Congress of the United States
U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-6515

MEMORANDUM

TO: Members, House Committee on Small Business
FROM: Nydia Velázquez, Chairwoman
DATE: January 12, 2022
RE: Full Committee Hybrid Hearing: “Review of SBA’s Top Management and Performance Challenges in Fiscal Year 2022 and SBA OIG’s Semiannual Report to Congress”

On Wednesday, January 12, 2022, at 10:00 a.m. in Room 2360 of the Rayburn House Office Building, and virtually via the Zoom platform, the Committee on Small Business will convene for a hybrid hearing titled, “Review of SBA’s Top Management and Performance Challenges in Fiscal Year 2022 and SBA OIG’s Semiannual Report to Congress.”

Each year, the Small Business Administration’s (SBA) Office of Inspector General (OIG) releases a report on the most significant management and performance challenges facing SBA. The goal is to focus attention on issues to enhance the effectiveness of the agency and its programs. In addition, every six months the OIG submits a report on its independent oversight of the SBA. The hearing will cover issues related to SBA’s management of its programs related to pandemic relief, contracting and counseling, access to capital, and disaster assistance, as well as information technology (IT) controls. The sole witness for the hearing is:

- Mr. Hannibal “Mike” Ware, Inspector General, Office of the Inspector, U.S. Small Business Administration

Background

In accordance with the Reports Consolidation Act of 2000,¹ OIG annually assesses SBA’s programs and activities that pose significant risks, including those that are particularly vulnerable to fraud, waste, or abuse. In its report, OIG is required to summarize SBA’s most serious management and performance challenges and assess the agency’s progress in addressing those challenges.² OIG’s most recent report titled, “Report on the Most Serious Management and

¹ Pub. L. No. 106-531.

² See 31 U.S.C. § 3516(d).

Performance Challenges Facing the Small Business Administration in Fiscal Year 2022” identifies eight management and performance challenges.³

OIG, pursuant to the Inspector General Act of 1978,⁴ is also required to issue semiannual reports to Congress summarizing the activities of its office. The semiannual report must identify risks, problems, recommendations, and investigative outcomes related to the administration of SBA’s programs and operations during the preceding six months.⁵ OIG’s semiannual report for the period April 1, 2021 through September 30, 2021 details the audits and investigations related to SBA’s pandemic relief programs, access to capital program, disaster assistance program, and contracting and counseling programs.⁶

Oversight of PPP and COVID EIDL

The breadth of SBA’s pandemic relief programs and the speed at which the programs were implemented – coupled with lowered fraud protections and guardrails during the past Administration – led to a significant amount of potentially fraudulent behavior related to the Paycheck Protection Program (PPP) and the COVID-19 Economic Injury Disaster Loan program (COVID EIDL). Specifically, with regard to PPP, OIG wrote “[o]nce the laws were in place, SBA moved quickly to establish the new nationwide relief programs. *But the agency eased controls required in its lending programs to do so, increasing the risk of rampant fraud.*”⁷

SBA’s OIG has identified over 70,000 potentially fraudulent PPP loans totaling more than \$4.6 billion.⁸ In addition, OIG has identified over \$78 billion in potentially fraudulent loans and grants to ineligible entities related to COVID EIDL.⁹ OIG’s work on PPP and COVID EIDL fraud cases has resulted in 319 indictments and 145 convictions with associated amounts totaling more than \$460 million.¹⁰ Further, the U.S. Department of Justice has filed 79 PPP fraud cases against more than 140 defendants who are charged with stealing \$341 million.¹¹ Due to issues with PPP and COVID EIDL, OIG indicated in its FY22 Management Report that the pandemic relief programs are a top management and performance challenge.

PPP

As of May 2021, SBA has processed 11.8 million guaranteed PPP loans, totaling 700.9 billion.¹² The FY22 Management Report found that PPP has been susceptible to abuse and fraud, had deficiencies with internal controls to determine the eligibility of borrowers, and the program’s 2020 data was inaccurate and incomplete. In addition, some of the fraud schemes that were used

³ U.S. SMALL BUS. ADMIN., OFFICE OF INSPECTOR GEN., TOP MGMT. AND PERFORMANCE CHALLENGES FACING THE SMALL BUS. ADMIN. IN FISCAL YEAR 2022 (October 15, 2021), Top Management and Performance Challenges Facing the Small Business Administration for Fiscal Year 2022 (sba.gov) [hereinafter, FY22 Management Report].

⁴ Pub. L. No. 95-452.

⁵ See 5a U.S.C. § 5.

⁶ See U.S. SMALL BUS. ADMIN., OFFICE OF INSPECTOR GEN., SEMIANNUAL REPORT TO CONG. APRIL 1, 2021 – SEPT. 30, 2021 (November 30, 2021), https://www.sba.gov/sites/default/files/2021-11/SBA%20OIG%20Fall%202021%20Semiannual%20Report%20to%20Congress_Final%20508.pdf. [hereinafter, Semiannual Report].

⁷ FY22 MGMT. REPORT, *supra* note 3 at 2 (emphasis added).

⁸ *Id.* at 4.

⁹ *Id.* at 5.

¹⁰ SEMIANNUAL REPORT, *supra* note 6 at i.

¹¹ FY22 MGMT. REPORT, *supra* note 3 at 3.

¹² *Id.* at 1.

to defraud PPP include false statements on applications, corporate or personal identity theft, submission of fraudulent supporting documents, and misuse of PPP funds. The report also highlighted the need for the agency to provide better guidance to lenders on how to deal with fraudulent loans.

The OIG noted that SBA has made substantial progress to reduce fraud risks and prevent further losses with regard to PPP. Some of the corrective actions SBA undertook include developing and implementing a Master Review Plan that establishes guidelines for loan and forgiveness reviews, increasing post-disbursement antifraud controls for loans that originated in 2020, and increasing antifraud controls for loans originating in 2021. One of the antifraud controls is verifying that borrowers are not on Treasury's Do Not Pay List. This is important because OIG, in collaboration with the U.S. Department of Treasury, found that 57,473 PPP loans, totaling \$3.6 billion, were approved for borrowers that may have been on Treasury's Do Not Pay List.¹³ The OIG is continuing to evaluate and audit PPP, and a future challenge they will be examining is the PPP loan forgiveness activity. The Committee intends to track this work to ensure that forgiveness is not granted to ineligible borrowers.

COVID-19 EIDL

The FY22 Management Report also found that SBA has made moderate or limited progress in addressing fraudulent activity related to COVID EIDL. The report highlighted that SBA needs to improve its COVID EIDL process to prevent fraudulent activity. To address these issues, SBA has instituted internal control changes such as enabling fund holding at any time, requiring Internal Revenue Service (IRS) tax transcripts for all loan approvals, and verifying applicants are not on Treasury's Do Not Pay List. Validation that applicants are not on the Do Not Pay List is important since SBA under both PPP and COVID EIDL were approving borrowers who were on that list. In November 2021, OIG issued a report that found that \$3.1 billion in COVID EIDL and \$550 million in emergency COVID EIDL grants, distributed between March 2020 to November 2020, were potentially improperly distributed to recipients on Treasury's Do Not Pay List.¹⁴

Contracting

The Small Business Act¹⁵ established a government-wide goal that 23 percent of all prime contracts be awarded to small businesses each fiscal year (FY). Since FY13, SBA has reported that the federal government met or exceeded this goal. In addition, SBA has numerous programs to expand the opportunities for small businesses to receive federal contracts, such as women-owned, 8(a), HUBZone, and service-disabled veteran-owned. These programs help level the playing field between small and large firms on federal contracts.

Inaccurate Procurement Data and Eligibility Concerns

A top management and performance challenge listed in the FY22 Management Report is the accuracy of the small business contracting data that is reported by federal agencies. Over the years, OIG audits have found that SBA does not consistently detect ineligible firms in its small business

¹³ See U.S. SMALL BUS. ADMIN., OFFICE OF INSPECTOR GEN., PAYCHECK PROT. PROGRAM LOAN RECIPIENTS ON THE DEP'T OF TREASURY'S DO NOT PAY LIST (Jan. 11, 2021), <https://www.sba.gov/document/report-21-06-management-alert-paycheck-protection-program-loan-recipients-department-treasurys-do-not-pay-list>.

¹⁴ See U.S. SMALL BUS. ADMIN., OFFICE OF INSPECTOR GEN., COVID-19 EIDL RECIPIENTS ON THE DEP'T OF TREASURY'S DO NOT PAY LIST (Nov. 30, 2021), COVID 19 Program Recipients on the Department of Treasury's Do Not Pay List (sba.gov).

¹⁵ Pub. L. No. 83-163.

contracting certification programs. Moreover, in 2020, the General Services Administration (GSA), Office of Inspector General found \$89 million in procurements erroneously recoded as small business in the Federal Procurement Data System – Next Generation.¹⁶ SBA OIG found that the agency has made significant progress in addressing this matter by adjusting internal controls, such as requiring HUBZone firms to annually recertify, instituting procedures requiring SBA employees justify recommendations to admit firms into the 8(a) program, and tracking complaints against firms’ eligibility to participate in the 8(a) program.

The FY22 Management Report found that SBA’s online certification management platform for Women Owned Small Businesses and Economically Disadvantaged Women Owned Small Businesses, Beta.Certify.sba.gov has been plagued by technical challenges. Of the 15,000 applications that were received in 2020, 12,000 or 80% of the applications were returned requesting more information from the applicant, which has slowed the prompt certification of these businesses.¹⁷

Management and Monitoring of the 8(a) Business Development Program

SBA’s struggle to provide effective business development assistance to 8(a) firms continues to be a top management and performance challenge. Even though SBA has made significant improvements in the services it provides 8(a) firms, the OIG found that SBA failed to establish an IT system to monitor program participant performance and ensure that businesses are receiving effective development assistance. In 2016, in order to address the decline in the number of firms participating in the 8(a) program, SBA moved to streamline the application process. There were concerns raised in previous OIG audits that the streamlined application process that some eliminated documentation requirements would erode safeguards, resulting in allowing ineligible firms to participate in the program. SBA has resolved this issue by taking corrective actions outlined in the audits, including having the business opportunity specialist submit a request to the IRS for tax transcripts to verify an applicant’s financial information.

In 2018, OIG found that SBA did not sufficiently ensure that 8(a) firms met continuing eligibility requirements in order to take part in the 8(a) program and SBA failed to remove firms that were no longer eligible. In FY20, SBA implemented new processes to evaluate the continuing eligibility of 8(a) firms and updated its process for removing firms that were no longer deemed eligible to participate in the 8(a) program. Due to these corrective actions, OIG determined SBA has resolved or appropriately reduced the risk with this matter.

Information Technology

Of particular importance, the OIG concluded that IT issues arising during agency implementation of the COVID pandemic relief funds highlights the significant need for the agency to invest in IT upgrades to improve portal interfaces and the need to establish and maintain IT security control baselines essential to protect against cybersecurity threats. OIG recommended the agency update its system development policy because it has not been updated since 2009 and does not fully address changes in IT development to include the use of third-party application service providers. Due to these problems and the issues listed below, IT continues to be a top management and performance challenge for SBA.

¹⁶ FY22 MGMT. REPORT, *supra* note 3 at 7.

¹⁷ *Id.* at 10.

One major ongoing project, which was supposed to be completed by the end of 2021, is the implementation of Certify.gov. According to OIG, in working with its IT investment board, the agency has made substantial progress in its oversight of beta.Certify.gov., which is the agency's gateway to all of SBA's contracting programs. OIG will continue to monitor the agency's progress on this project in FY22.

In the FY22 Management Report, OIG determined that SBA's information security was not effective and continues to experience security challenges in areas of user access, configuration management, and security training. The agency only received a Federal Information Security Management Act¹⁸ maturity model Level 4 (*i.e.*, area is managed and measurable) in incident security, but in seven other areas the agency is only at a Level 2 or Level 3.¹⁹ OIG noted that the agency made substantial progress and improvements in protecting personal identifiable information (PII).²⁰ This is notable because in March 2020, SBA discovered that it experienced a data breach and that some EIDL applicants' PII was accidentally disclosed to other applicants.²¹ The Committee has held a number of hearings on the IT systems at SBA and intends to continually monitor IT progress.

Access to Capital

As of June 30, 2021, SBA has a financial assistance portfolio of guaranteed and direct loans that totaled around \$854 billion, which includes loans made through PPP.²² The Office of Credit Risk Management (OCRM) is responsible for assessing the risk levels of SBA lending partners and oversees the 7(a) and 540 loan portfolios. SBA's 7(a) program is the agency's flagship loan program that provides commercial and working capital loans of up to \$5 million to small businesses who cannot access credit elsewhere.

SBA Risk Management and Oversight Practices

A top management and performance challenge is OCRM's oversight of the lenders that take part in its 7(a) and 504 loan portfolios. The FY22 Management Report found that SBA has made moderate or limited progress in its oversight of high-risk lenders. These concerns were also raised in an OIG audit that provided that OCRM did not always identify and mitigate risks as it relates to high-risk lenders.²³ Since FY20, OCRM has been addressing these issues by communicating deficiencies identified during loan file reviews with stakeholders, improving its use of data to identify and manage high-risk lenders, and reorganizing the structure of the office to strengthen lender oversight. However, OCRM needs to continue to develop policies, procedures, and a workflow management system to provide proper oversight over high-risk lenders.

SBA has resolved or appropriately reduced concerns OIG had of its ability to identify and track loan agent involvement in its 7(a) and 504 loan portfolios. SBA was able to resolve this issue by

¹⁸ Pub. L. 107-347.

¹⁹ FY22 MGMT. REPORT, *supra* note 3 at 13.

²⁰ *Id.*

²¹ See Rachel Siegel, *Data breach may have exposed personal information of thousands of SBA emergency loan applicants*, The Washington Post, (April 21, 2020), <https://www.washingtonpost.com/business/2020/04/21/sba-data-loan-small-business/>.

²² SEMI-ANNUAL REPORT, *supra* note 6 at 5.

²³ See U.S. SMALL BUS. ADMIN., OFFICE OF INSPECTOR GEN., AUDIT OF SBA'S OVERSIGHT OF HIGH-RISK LENDERS (Nov. 12, 2019), <https://www.sba.gov/sites/default/files/2019-11/SBA-OIG-Report-20-03.pdf>.

enhancing its Form 159 (Loan Agent Disclosure Form) process to better track loan agents and to provide more data to evaluate loan agent performance. Additionally, a March 2015 OIG audit found that outsourcing of traditional lender functions to Lender Service Providers (LSP), a type of loan agent, has increased significantly in recent years.²⁴ Since then, SBA began assigning an identifying number for all LSPs that access SBA's systems and records all SBA-approved LSP agreements, which has allowed OCRM to develop initial metrics on LSP participation in the 7(a) program. In FY20, SBA worked on developing a performance analysis report for LSP portfolios and looking at whether the information from the report can show whether an LSP adds to the risk in the lender's portfolio of loans. With its work addressing this issue, OIG has found that SBA has made significant progress in addressing this matter.

Identification of Improper Payments in SBA's Loan Programs

OCA has made significant progress addressing a top management and performance challenge by improving its 7(a) loan program to reduce improper payments. In FY20, SBA provided more time for loan specialists to review complex early defaulted loans, improved training for loan specialists, and updated its loan review checklist. The FY22 Management Report recommends that to continue its progress, SBA should finalize and issue its revised 7(a) loan servicing and liquidation requirements, which are designed to reduce improper payments.

Disaster Assistance Program

SBA's disaster loan program provides long-term low interest loans to homeowners, renters, businesses, and nonprofit organizations in the aftermath of a disaster. There are a variety of disaster assistance programs available, and each has its own requirements.

Staffing

To respond to large-scale disasters the agency must hire additional loan officers to handle the increase in applications. For example, during the COVID-19 pandemic, SBA had to hire 9,000 additional permanent and temporary staff.²⁵ In addition, the agency must ensure that the proper quality assurance and financial controls are in place. OIG has indicated that the agency's challenges in staffing, quality assurance, and financial controls as it relates to the disaster assistance program continues to be a top management and performance challenge. Of note, the agency had to hire more permanent and temporary staff to respond to the COVID-19 pandemic than any other previous disaster. The substantial increase in hiring and training staff and the issues with the processing of millions of COVID EIDLs during this disaster continues to highlight the management challenge the agency faces when ramping up and responding to major disasters. OIG recommends that the agency should conduct an after-action evaluation after the pandemic is over and assess how they can develop staff training to improve customer service and ensure that applicants get the assistance they need in a timely manner.

Improper Payments

The Payment Integrity Information Act of 2019²⁶ requires SBA to use a risk-based approach for financial and administrative control to counter fraud risks and prevent improper payments. The

²⁴ See U.S. SMALL BUS. ADMIN., OFFICE OF INSPECTOR GEN., IMPROVEMENT IS NEEDED IN SBA'S OVERSIGHT OF LENDER SERV. PROVIDERS (March 12, 2015), https://www.sba.gov/sites/default/files/oig/OIG_Report_15-06_Lender_Service_Providers.pdf.

²⁵ FY22 MGMT. REPORT, *supra* note 3 at 26.

²⁶ Pub. L. No. 116-117.

OIG found that the agency has made moderate or limited progress in preventing improper payments related to COVID EIDLs. This is a concern because COVID-EIDL is now the main loan in SBA's disaster assistance portfolio. SBA has moved to prevent improper payments by implementing a multitiered approach to flag fraud or improper payments when an application is submitted or before funds are awarded. While the OIG raised concerns that the new process is inadequate, unfortunately the OIG has not actually reviewed the updated approach and therefore the Committee intends to follow-up after a complete review.²⁷

OIG also raised an issue about SBA's verification of the extent of property damage that would be eligible for a disaster loan. In order to provide quicker financial assistance to victims of disasters, a new desktop loss verification process was established in 2017. This process was used in lieu of having on-site inspections for the initial estimate of cost repairs and allowed SBA to use Federal Emergency Management Agency (FEMA) on-site inspection reports for loans of \$25,000 or less to confirm the estimates. In 2019, OIG found that SBA did not always validate the damages and the repair costs before disbursing funds.²⁸ In response, SBA strengthened its internal controls and stopped using FEMA inspection reports to confirm the estimates. Due to these changes, OIG found in its FY22 Management Report that SBA has resolved or adequately addressed the issue and OIG plans to remove this top management and performance challenge in future reports.

Future Servicing

An issue the OIG has indicated as a new challenge but has not yet rated is the agency's ability to manage the COVID EIDL portfolio. By the end of 2021, the agency could have a disaster loan portfolio size of \$470 billion.²⁹ OIG contends that the agency does not have the staff or infrastructure to manage this volume. To address this issue, the agency has contracted with a vendor to determine the most effective way to service this portfolio and will develop a plan before the two-year deferment period for the COVID EIDLs end.

Grants Management Oversight

Due to SBA's pandemic relief programs, the agency's budget to administer grants to provide economic relief and technical assistance grew from \$180 million in FY20 to \$45.3 billion in FY21.³⁰ OIG listed SBA's oversight of its grants programs as a top management and performance challenge. OIG noted that in recent audits that it found systemic issues with SBA's accuracy of grant data and ineffective oversight of its grant recipients.

According to the FY22 Management Report, SBA has made substantial progress in modernizing its grants management system. In FY20 and FY21, SBA's Office of Grants Management implemented the GrantsSolutions.gov system for program office use as part of the agency's continuing transition from the federal Procurement Request Information System Management (PRISM) to manage its grant awards. The next step is for the agency integrate the financial interface with GrantSolutions.gov so program offices will stop utilizing the PRISM system, which has hindered the agency's ability to manage its grants programs.

²⁷ FY22 MGMT. REPORT, *supra* note 3 at 29.

²⁸ See U.S. SMALL BUS. ADMIN., OFFICE OF INSPECTOR GEN., AUDIT OF SBA'S DESKTOP LOSS VERIFICATION PROCESS (September 26, 2019), <https://www.sba.gov/sites/default/files/oig/SBA-OIG-Report-19-23.pdf>.

²⁹ FY22 MGMT. REPORT, *supra* note 3 at 30. Before the pandemic, SBA was servicing about 263,000 disaster loans (around \$9 billion) and now the agency is servicing around 4 million disaster loans (around \$216.3 billion). *Id.*

³⁰ *Id.* at 32.

Furthermore, OIG also raised three new issues that SBA must focus on to improve its oversight its grants programs; the progress for addressing these issues has not been rated yet. OIG recommended: (1) SBA institute performance measures for the \$16.25 billion Shuttered Venue Operators Grant (SVOG) program and more clearly define the performance goals for the funds provided to Small Business Development Centers, Women’s Business Centers, and the Resource Partner Training Portal in the CARES Act; (2) enhance its audit plan for the SVOG program to prevent the potential misuse of funds; and (3) leverage and maintain a skilled workforce to properly manage the agency’s new multibillion dollar grants programs.

Conclusion

This hearing will give Members an opportunity to ask questions about the concerns raised by OIG in these reports, as well as to inquire about the agency’s implementation of OIG’s recommendations.