FULL COMMITTEE HEARING ON OVERSIGHT OF THE SMALL BUSINESS ADMINISTRATION AND ITS PROGRAMS

HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS UNITED STATES HOUSE OF REPRESENTATIVES

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FULL COMMITTEE HEARING ON OVERSIGHT OF THE SMALL BUSINESS ADMINISTRATION AND ITS PROGRAMS

Wednesday, April 21, 2010

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The Committee met, pursuant to call, at 10:00 a.m., in Room 2360 Rayburn House Office Building, Hon. Nydia Velázquez [chairwoman of the Committee] presiding.

Present: Representatives Velázquez, Moore, Dahlkemper, Schrader, Kirkpatrick, Nye, Altmire, Halvorson, Graves, Bartlett, Buchanan, Luetkemeyer and Thompson.

Chairwoman VELÁZQUEZ. Good morning. This hearing is now called to order.

In January of last year, the House adopted Rule 11 requiring regular hearings on waste, fraud, and mismanagement of programs under the Committee's jurisdiction. Since then, we have held no fewer than 18 oversight hearings, spanning a broad range of issues from federal contracting to SBA disaster loans.

Today's discussion is in that vein. It will allow us to build on past oversight hearings, providing a much-needed opportunity to examine some of the agency's most critical programs, and it could not come at a more pressing time.

Over the last two years, our economy has endured a seemingly endless parade of challenges. While these setbacks have differed in scope and industry, they have managed to have the same impact on small firms. Even today, as we steadily climb back towards recovery, entrepreneurs face obstacles. Now, more than ever, they need the resources necessary to not only overcome those roadblocks, but to keep our recovery strong.

Historically, the SBA has helped deliver that support. It has served as a vital source of stability for small companies, particularly during periods of economic decline. But as this Committee is well aware, the agency has also struggled in areas ranging from lending to procurement.

After years of underfunding, SBA continues to wrestle with a legacy of neglect—one that has eroded its oversight mechanisms and left many office programs in disarray. With an emphasis on accountability, and a strong commitment from the Inspector General, we can tackle those issues directly.

As Judge Brandeis famously said, "Sunshine is the best possible disinfectant." And make no mistake—there is no better tool for scrubbing out waste than transparency. When it comes to holding agencies accountable, the Inspector General has a critical role to play, and I am pleased the IG is with us today.

It is my hope that our conversation will serve as a frank and open forum for examining SBA's problem areas, because until we have identified those concerns we can neither move forward with solutions, nor expect to see improvements.

When SBA programs are running at full capacity, they are true economic catalysts. Just look at the small business development centers. In 2008 alone, they helped generate 58,000 new jobs at a cost of $3,000 apiece. Or, consider the Recovery Act's SBA loan provisions. They have allowed the agency to support more than $23 billion in lending. At a time of historic declines in the small business capital markets, that particular effort has been nothing less than a lifetime. But, unfortunately, not all of SBA's initiatives have been quite so successful.

Later this morning we will look at a number of IG reports, all of which point to problems within SBA programs. In some instances, core initiatives have been racked by fraud. In other cases, they have been undermined by questionable practices. It is imperative that these troubled programs be restored to reflect their original mission—strengthening and supporting small businesses, because at the end of the day small firms aren't just the backbone of our economy, they are our greatest source of job growth.

According to a recent study by the Kauffman Foundation, virtually all new jobs created between 1980 and 2005 came from startup companies. With unemployment at 9.7 percent, it only makes sense to focus on these firms—the small and startup businesses that have always provided job security. With a portfolio of strong, well-managed SBA programs, we can do that very thing.

I know I speak for all members of the Committee when I say we are dedicated to upholding the integrity of the agency's programs and to ensuring small firms have the tools and resources they need to thrive.

I would like to thank our witnesses, both Administrator Mills and Ms. Gustafson, for being here today.

This marks the Committee's first hearing with the IG, and I know we are all looking forward to today's discussion.

I will now yield to Ranking Member Graves for his opening remarks.

Mr. GRAVES. Thank you, Madam Chair, and thank you also for holding this important hearing on the oversight of the Small Business Administration and its programs. I look forward to hearing from Administrator Mills and the Inspector General on the agency's lending programs.

The SBA programs operate in coordination with the private sector by guaranteeing loans made by banks and certified development companies. Due to the possibility that taxpayers could have to pay on the guarantee, the programs should be overseen with the utmost care and transparency.

SBA regulations and procedures are supposed to be designed to protect the Federal Government. However, the Inspector General's recent report indicates that lenders have been failing to comply with SBA requirements. This should raise a red flag at the agency, but it appears that little has been done to correct the problem.

Additionally, the Inspector General's report raises some significant concerns about SBA program management. Poor oversight increases the risk to the taxpayer. And while I am generally supportive of programs designed to assist small businesses in obtaining scarce credit and capital, I cannot and will not maintain that support if the programs are not properly monitored to protect the taxpayers from unnecessary risk.

Ultimately, the issue of today's hearing is whether the SBA lending programs operate primarily for the benefit of the lenders or for the small business borrower. I believe that Congress wants these programs to assist small business borrowers. If that is in fact the case, the agency must take aggressive action to ensure that only the most responsible lenders are involved in these programs. Anything less would be unacceptable to Congress and the tax-paying public.

Again, I want to thank you, Madam Chair, for holding this hearing. I am looking forward to hearing the witnesses' recommendations on how we can increase the availability of capital to small businesses without placing the taxpayers in jeopardy for poor business management decisions.

Thanks.

Chairwoman VELÁZQUEZ. Thank you.

And it is my pleasure to welcome The Honorable Karen Mills. She was sworn in April 6, 2009, as the 23rd Administrator of the U.S. Small Business Administration. The SBA helps small business owners and entrepreneurs secure financing, technical assistance, and training on federal contracts.

Welcome.

STATEMENT OF KAREN MILLS

Ms. MILLS. Thank you very much. Chairwoman Velázquez, Ranking Member Graves, members of the Committee, it is an honor to be with you. In working with you over the past year, these meetings have been important and helpful. This is a shared endeavor to improve oversight and risk management while removing waste, fraud, and abuse.

I am pleased to say that we are making good progress. One tangible metric is that we have cut the number of overdue IG findings in half, from 97 last June to 48 this March. We also have less than 50 open recommendations from GAO, having closed six full audits since 2008.

And just last week we received an award from the Association of Government Accountants for excellence in accountability reporting. But there is more work to do.

It is now part of the SBA's strategic priorities to build on this progress in two particular areas. The first areas are government contracting and business development programs, where we have efforts aimed at all three steps in the process.

At the front end, it means more efforts with upfront certification and eligibility. For those already in the program, it means more emphasis on ongoing compliance and site visits. And, finally, if they are found to be out of compliance, it means pursuing and removing bad actors.

Already we have made dramatic increases in site visits and HUBZone firms from fewer than 100 in 2008 to over 900 in 2009, and we are on track to do more than 1,000 this year. We are working to ensure that only legitimate, eligible firms are benefiting from the HUBZone program.

In our 8(a) program, we agree with nearly all of GAO's recent recommendations, and we have begun to implement them. Already we are training our field staff to more quickly identify ineligible firms. And when it is clear that fraud exists, we are taking steps to debar and/or work with the Department of Justice to prosecute.

We also did the first comprehensive review of 8(a) in a decade, and proposed regulatory changes. We went to 10 cities. We held two tribal consultations and received extensive public comments. GAO has given us positive feedback on how we handled this process.

For all our contracting programs, the President's FY11 budget requests $2 million for strengthening efforts to prevent waste, fraud, and abuse.

The second area is lender oversight. We are working to instill best practices that will ensure compliance and manage risk more effectively, as we work with our lending partners.

In the 2011 budget, we request $2 million more for lender oversight and onsite reviews, as well as $1 million for stronger program assessments. This will help us address areas that the Inspector General has recently brought to our attention, including the premier certified lenders in the 504 program.

Overall, the entire SBA team is focused on continued vigilance in identifying, tracking, and reducing risk. Through our partnership with this Committee, and with insights from the GAO and our Inspector General, I know we have moved in the right direction this past year. And we commit to continue to take even bigger steps in the future.

Separately, an important issue has come up in the past few weeks that I want to bring to the Committee's attention. The SBA and the White House support the congressional intent of parity—equal treatment among our contracting programs, 8(a), HUBZone, service-disabled veterans, and soon women-owned small businesses.

However, a recent court decision potentially undermines this policy by interpreting the Small Business Act to provide for a HUBZone preference over the other programs. The administration supports legislative efforts to confirm Congress' original intent to provide for parity.

I welcome any questions. Thank you very much for having me here.

[The prepared statement of Ms. Mills is included in the appendix.]

Chairwoman VELÁZQUEZ. Thank you, Administrator Mills.

And now I welcome The Honorable Peggy Gustafson. She was worn in as the Inspector General of the U.S. Small Business Administration on October 2, 2009. The Office of Inspector General conducts and supervises audits, inspections, and investigations relating to SBA programs and supporting operations.

Welcome.

STATEMENT OF PEGGY GUSTAFSON

Ms. GUSTAFSON. Thank you. Madam Chairwoman, Ranking Member Graves, and distinguished members of the Committee. Thank you very much for allowing me to discuss the IG's current efforts to deter and detect waste, fraud, abuse, and inefficiencies in SBA programs.

Today I would like to focus on several recent audits, some recent criminal indictments and convictions, and two new management challenges that my office issued to the agency in October of 2009.

Regarding our audits, during the first seven months of FY2010, my office has issued 24 audit reports and other reviews. These reports contain 97 recommendations to SBA to promote efficiency and reduce waste. We recently issued a report on an audit of the underwriting practices and compliance of three of the largest premier certified lenders, or PCLs, that are authorized to approve loans in the CDC 504 loan program with limited prior SBA review.

My office found a high rate of errors on PCL loans involving poor loan underwriting and eligibility or loan closing issues. Based upon our sample, we project that for loans disbursed in fiscal year 2008 by the three PCLs, a total of $209 million worth of loans involved problems with borrower eligibility or loan closing issues, and that loans totaling nearly $56-1/2 million had weaknesses in underwriting.

We also found that a number of CDCs pay a sizable percentage of gross receipts to their executives, which reduces the amount of funds available to that CDC for economic development activity.

In response to the provisions of the Recovery Act, my office has developed a recovery oversight plan, created a separate recovery oversight group within our Auditing Division, and has so far issued 14 recovery oversight reports identifying programmatic and other deficiencies.

As part of this oversight work, my office recently reviewed origination and closing of Recovery Act loans made in the 7(a) Loan Program. We identified deficiencies in 53 percent of the sample of loans we reviewed made by lenders with no prior SBA approval, and errors in 23 percent of the loans, which SBA had themselves approved.

We also recently completed three audits that raised concerns with SBA's procurement of goods and services. To summarize the findings in these reports, we found that 92 percent of a sample of contract actions reported by SBA for fiscal year 2008 contained one or more inaccurate or incomplete data elements in the FPDS government database, and that fiscal year 2009 had a higher error rate of 97 percent of the sample contract actions having errors.

We determined that SBA's current workforce involved in procurement actions is insufficient to effectively award, administer, and oversee SBA contracts, and is increasing the risk of mismanagement and improper payments on SBA contracts. And we found that SBA did not report all non-competitive Recovery Act contracts to Recovery.gov and has mischaracterized some of the actions that have been reported to Recovery.gov.

During the first six months of this fiscal year, IG criminal investigations have resulted in 51 indictments and 14 convictions, and obtained approximately $16 million in potential recoveries and fines. Most of our investigations involve false statements to obtain SBA guaranteed loans, SBA disaster loans, or government contracts that are supposed to be set aside for disadvantaged small businesses.

Our investigations have identified an ongoing pattern of fraud by unscrupulous loan agents and other consultants who orchestrate multi-million dollar schemes where numerous SBA guaranteed loans are originated based on falsified information.

During the past decade alone, we have had numerous cases involving loan agent fraud on loans totaling over $260 million. Fraud in the 8(a) and HUBZone programs, and other SBA preferential contracting programs, is also a problem. Recent IG audits and investigations, and recent reports from the GAO, show that ineligible companies continue to obtain set-aside contracts, and that non-disadvantaged individuals are exploiting these programs.

We are working with the Justice Department to pursue criminal and civil fraud prosecution against companies that have improperly obtained contracts under the HUBZone and service-disabled veteran programs, and we are working with the agency to develop a more robust debarment and suspension program.

As required by law, my office issues a report in October identifying key management challenges for SBA. Our most recent report had two new challenges. One challenge is based on significant projected improper payments in both the Disaster Loan Program and the 7(a) Loan Program. And the second challenge identified concerns with SBA's management of its largest current IT project to upgrade its loan monitoring and financial management systems, a project with an estimated cost of over $250 million.

Again, I want to thank you for the opportunity to comment on these issues, and look forward to your questions.

[The prepared statement of Ms. Gustafson is included in the appendix.]

Chairwoman VELÁZQUEZ. Thank you, Inspector General.

Administrator Mills, it has been a month since the IG delivered its report on acquisition personnel. And we would like to know, what changes has the SBA made to address the problems raised in that report? And what is your timeline to fix those issues?

Ms. MILLS. Madam Chair, earlier this week we announced a reorganization of our internal acquisition department. We are following the best practices of 10 other agencies—we are actually the tenth agency to reorganize under the Chief Financial Officer, so that the Internal Control Department will then be aligned with the Procurement Department, and those experts in internal control will provide better oversight to procurement.

We operate our procurement operation out of our Denver Finance Center, and we will be moving our procurement operation to be under that with new procedures.

Chairwoman VELÁZQUEZ. What about personnel?

Ms. MILLS. We have really important, terrific people in this area at the SBA. And change is very difficult, so—

Chairwoman VELÁZQUEZ. Well, the Inspector General's report particularly addressed the issue of the inadequacy of the SBA acquisition office in terms of failed to adequately staff the office that was doing procurement work for the Recovery Act.

Ms. MILLS. Yes. And this is one of the reasons for the move to Denver, where we have a pool of very strong personnel. We are going to offer all of our people in this area, the opportunity to move to Denver and support them. And if they don't move, I just want to reiterate that we are going to take care of them here.

Chairwoman VELÁZQUEZ. But my concern—if this is to implement those provisions of the Recovery Act, will require the expertise and the staff. And nine months ago you learned from the IG that you were not in compliance with the OMB requirements regarding the staff. But you are telling me that this week you are moving to do this.

Ms. MILLS. Yes. We have been working on this move for quite a long time. There has been extensive review of what the best practices are to get the right staff, whether that staffing would be available here, and how to change the procedures and the supervision, so that we have the quality of supervision. And this is the solution that we are pursuing.

Chairwoman VELÁZQUEZ. For more than a decade there have been inaccuracies in federal small business contracting data. And when you and I, we have a first meeting, that is one of the issues that I raised with you.

A recent IG report found that SBA's own data had an error rate of 92 percent for FY2008, 97 percent in 2009. In many cases, SBA was misreporting small business contracts that actually went to large businesses. Do these findings call into question the agency's credibility and ability to monitor government-wide reporting problems?

Ms. MILLS. Your point is exactly correct. This is extremely disturbing and is unacceptable. We have to be the standard for the rest of the agencies.

Chairwoman VELÁZQUEZ. So, Ms. Gustafson, has the agency implemented any of the IG's recommendations yet on this area?

Ms. GUSTAFSON. Representative Velázquez, they have committed to implementing those recommendations. In all candor, the audit is a couple months old. I am not certain that they have been finally implemented. I will get that answer back to you. I will check on that and get that answer back to you.

Chairwoman VELÁZQUEZ. Administrator Mills, can we get a timeline—

Ms. MILLS. Yes, Madam Chair.

Chairwoman VELÁZQUEZ. —when the agencies plan to implement those?

Ms. MILLS. Yes, Madam Chair.

Chairwoman VELÁZQUEZ. Okay. Last month this Committee was working to secure documents from the SBA's Office of Inspector General related to an active audit. During that process, the SBA General Counsel interjected herself in the matter, actually calling the House General Counsel. Was this done at your direction or at the direction of your staff?

Ms. MILLS. No.

Chairwoman VELÁZQUEZ. No, it wasn't—

Ms. MILLS. That was not done.

Chairwoman VELÁZQUEZ. It was at the direction of who?

Ms. MILLS. I don't have any direction about this effort.

Chairwoman VELÁZQUEZ. Do you think that was an appropriate action?

Ms. MILLS. My understanding of the situation is that we will try to be helpful in any case that we could.

Chairwoman VELÁZQUEZ. Ms. Gustafson, should it be a source of concern if the SBA's General Counsel has taken it upon herself to act as an intermediary between this Committee and the IG in matters pertaining to agency oversight?

Ms. GUSTAFSON. Madam Chairwoman, there is no question that the agency's General Counsel does not act for me. And being very involved in the IG Reform Act of 2008, one of the things that Act did was very specifically state that the IG is to have her own counsel, or his own counsel. And I have my own counsel.

And so to your exact question, which is, is it appropriate—would it be appropriate for an agency General Counsel to act on my behalf, I would say no, that is not appropriate, and I would—

Chairwoman VELÁZQUEZ. Administrator Mills, I hope that in the future your General Counsel will refrain from interjecting herself into matters that are related to the Inspector General and the work—the oversight work of this Committee.

This is to the IG. The findings of your report on the PCL program paint a picture of lax SBA oversight and deficient internal controls. Given what you have found in your report, if Congress were to undertake a major expansion of the CDC program, could the agency effectively administer the program?

Ms. GUSTAFSON. What I think the message of the report needs to be is not that the agency can't undertake effective oversight of the CDC program, but that we are concerned with how that oversight has been undertaken so far. SBA has the ability to set forth guidelines for the CDCs to eliminate or reduce the possibility of some of the underwriting concerns that we really had.

SBA does on-site reviews where they look at these types of issues. And one of the things that our report says is that there needs to be a tieback. The agency needs to look back and see if CDCs are doing better when they find these issues. We didn't really find that here.

So I wouldn't say that it is a question that it couldn't be done, but—

Chairwoman VELÁZQUEZ. Can they do it today?

Ms. GUSTAFSON. They would have to devote more resources than they are devoting now.

Chairwoman VELÁZQUEZ. Thank you. The PCL lender program was intended to reduce SBA costs by delegating authority for CDCs to process, close, service, and liquidate loans. In other words, PCLs were thought to be the most qualified to effectively administer this program with minimal SBA involvement. In light of your report on the program, does it appear the PCL program is meeting the intended goals?

Ms. GUSTAFSON. I really hesitate to paint a broad brush over the entire program based on this audit. We looked at three of the larger PCL lenders, and, again, I don't think that this audit should be taken to mean that they cannot do that. I just think that there is smaller oversight and there is lax oversight. And, again, I think the emphasis needs to be that there needs to be stronger oversight.

Chairwoman VELÁZQUEZ. Thank you. Mr. Graves.

Mr. GRAVES. Thank you, Madam Chair.

Thanks, Administrator, for being here. A couple of questions for both of you. The first one is, some of these lenders are not complying with some of the standards, but my question is, has the SBA ever revoked the status of any of its lending partners?

Ms. MILLS. Yes. Yes, we do revoke the status of the lending partners.

Mr. GRAVES. Recently or—

Ms. MILLS. Yes, we do on a continuous basis.

Mr. GRAVES. —regular basis?

Ms. MILLS. Yes.

Mr. GRAVES. And the second one is a completely different question, because we get some complaints from some folks when it comes to the standards review for certain industries. And some of them are very frustrated, because they think that the standard is so outdated it is making it very difficult for them to compete for federal programs.

My question is: can we modify the order in which the standards are reviewed, or change that priority for some industries, or speed it up, do something? Because we are getting a lot of complaints from different folks.

Ms. MILLS. Yes. Representative Graves, I understand that you might be talking about the size standards industry by industry.

Mr. GRAVES. Absolutely.

Ms. MILLS. —yes, we would be happy to focus on industries in which membership feels that a review needs to happen. And we would be happy to take a look.

Mr. GRAVES. In some cases, we need that review right away. But I will have the staff work with your staff.

And for you, Ms. Gustafson, my question is—and it is a real simple question—what are the risks to the taxpayer from the PCL program?

Ms. GUSTAFSON. Well, the PCL program obviously includes a portion that is guaranteed by the Federal Government.

Mr. GRAVES. Right.

Ms. GUSTAFSON. And there really isn't a lot, once these loans are due—once these loans are given, there is not a lot that the Federal Government can do to not pay a guarantee on that loan. And so that is really the biggest risk.

Again, this is a program where it was envisioned that there would be a lot of authority given to lenders, and the government was going to have to just kind of accept that, under the understanding that they were trusting the lenders to do the right decision. And so the risk comes in the—and I forget the hundreds of millions—the millions of dollars—I apologize, I forget the numbers—of outstanding loans that are out there that would probably have to be paid as a guarantee under the program.

Mr. GRAVES. Okay. Can we get that number?

Ms. GUSTAFSON. Oh, absolutely. Yes.

Mr. GRAVES. Thanks, Madam Chair.

Chairwoman VELÁZQUEZ. Ms. Dahlkemper.

Ms. DAHLKEMPER. Thank you, Madam Chair.

Administrator Mills, as you know, I have introduced some legislation for the 7(a) Express Loan Program to increase the size of the loans, as well as the guarantees. I really see this legislation as just one of the important tools we need to give our struggling small businesses. I have talked to many businesses. I have talked to my small banks in my region about this piece of legislation, and they believe it is another tool to get access to our small businesses for that working capital that they need.

I introduced this legislation, and many of my colleagues have actually joined me in co-sponsoring this legislation. But as I am, you know, listening to this I just want to ask you, the 7(a) Express Loan Program, do you think that it should be discontinued? Or do you think that we can move that forward in a way that we won't see some of the abuses going on that we have seen?

Ms. MILLS. The 7(a) Express Program is an extremely powerful program, particularly in this time when many people have had their lines of credit pulled. In the last year in the Recovery Act we did 20,000 loans, so we helped 20,000 businesses with $1.5 billion.

We believe that people like this program quite a bit, because it allows banks to use their own paperwork. It does have a limit of $350,000. If that limit were higher, the statistics say that the larger loans perform better, so it actually would reduce the risk of the overall pool as well.

We feel that all of these oversight issues that are brought up are serious and need attention across the board, and we are committed to increasing our oversight, not only of the programs raised today but in all of our programs.

Ms. DAHLKEMPER. Well, just as a follow-up to that, I know that there is also a proposal by the administration to allow the 504 loans to be refinanced. And how does the 504 loan refinancing plan proposed by the administration support our small businesses in the current economic climate?

Ms. MILLS. We have analyzed all of the gaps in creating the small business jobs package proposed by the President. One of these gaps is in refinancing owner-occupied real estate. We know that there are enormous numbers of small businesses— such as a dentist who owns the office or a manufacturer who owns the warehouse--who took out a bullet mortgage that will become due in 2010, 2011, 2012.

We have proposed using the 504 program in a non-delegated manner, so it would not go to the lenders that the Inspector General reviewed for delegated authority. We would review all of these loans, and we believe that we would only take loans that were in good standing, and for refinancing, and that the risk in this matter has been assessed and modeled as being lower than the current 504 risk pool, because that is for an expansion. And when a small business owner has an expansion, he or she doesn't actually know what the next year's cashflow coverage will be, because they are growing.

So we are looking to meet this market gap, and we believe that this is a lower risk way of reaching probably seven to ten billion small businesses who will really potentially be out of business if they can't refinance these bullet mortgages.

Ms. DAHLKEMPER. Thank you. Ms. Gustafson, can I just ask you about the 7(a) Express Loan Program? Particularly with my legislation that I brought forward, do you see any issues with that program?

Ms. GUSTAFSON. Well, in the interest of full disclosure, we haven't done an audit very recently—I have been there not very long—on SBA Express, so I don't want to go too far out on a limb, except to say that any time—one of the things that SBA Express does, again, when you have delegated authority, there is always an increased risk due to that, which isn't to say that it would necessarily mean that your legislation would not be a good idea.

I don't feel like I have the—it is just all of these programs with delegated authority always give auditors a little bit of pause, just because there is a risk when you are having the lenders do some of this process. But it is not a question of being unmanageable. Again, the key is that SBA is doing effective oversight on the programs that they are administering. And with that, if that is in place, and with that commitment from the SBA, there is no reason to think that it would be unwise.

Ms. DAHLKEMPER. Thank you. I know my businesses are very interested in this. It is a crucial time to get this type of legislation passed. So thank you very much. My time is up.

Chairwoman VELÁZQUEZ. Time is expired. Mr. Thompson.

Mr. THOMPSON. Thank you, Madam Chair. Thank you to both of you for coming today, testifying, and for—you know, for the efforts that you are putting in to assure and really safeguard the resources that we use for strengthening small businesses, working to eliminate the waste and fraud and abuse.

Administrator Mills, one of my questions is, since our last hearing, what further actions has the Small Business Administration taken to remove and to eliminate firms that do not qualify under HUBZone or the service-disabled programs?

Ms. MILLS. Thank you. We found the last hearing, particularly on service-disabled veterans, extremely helpful, and have put in a three-part action plan to address many of the issues that came up. The first action is that we are working on the front end on identification of service-disabled veterans, and there the VA holds the database.

I have met with General Shinseki, and with Department of Veteran Affairs Deputy. The SBA has their cooperation on improving that database, so we can find out who is a service-disabled veteran.

The second thing is that we have enhanced our bid protest process, and we are now doing about double the bid protests. If a service-disabled firm is found to be ineligible, we require them to delist themselves from the contract register, the CCR, within 30 days. If they don't do it, we do it. So an ineligible firm can't stay in the register, which was something that we found was a problem.

And the third is that we have investigated the 10 fraudulent examples in the last GAO report. We have referred all 10 to the Inspector General, and will pursue anybody who is proven to be acting inappropriately to the Department of Justice.

Mr. THOMPSON. In follow-up, given the GAO report, one of the problems with HUBZone service-disabled veteran contracting, it sounds like—and I throw this out there for you to respond to—has the agency become more aggressive in suspending and preparing debarment proceedings against federal contractors, if found to be ineligible?

Ms. MILLS. Yes.

Mr. THOMPSON. Okay.

Ms. MILLS. We call that going after the bad actors.

Mr. THOMPSON. Okay. Very good. I read that the White House sent out kind of—a little different question, sent out postcards to millions of small businesses concerning tax credit and the recent health bill. And what actions has SBA taken to inform small businesses of the potential impacts of the health care bill, you know, such as mandate to provide insurance to the employees, you know, the details that businesses need to know proactively to prepare their business plans?

Ms. MILLS. Right now, on our website, a small business can find a very clear description of how to determine eligibility for tax credits. We have estimated that about four million of the six million employer-owned employee small businesses could potentially be eligible. But it is hard for them to know, so it is our role to walk them through it.

We are also committed to training and educating all of our 900 small business development centers, our women's business centers, and our SCORE representatives, so that they also could walk a small business through it. And I don't know about you, but I personally have actually walked a number of small businesses through this question, because this is money in their pocket in 2010, and they need to have it.

Mr. THOMPSON. Okay. Thank you. Inspector General, I just want to pursue kind of a previous follow-up on premier certified lenders. You know, what additional oversight do you believe the SBA should take with respect to the PCLs?

Ms. GUSTAFSON. Well, first and foremost, I think they need to reconsider some of their responses to our audit. I would really like to see them tighten up some of the standards that the PCLs are using, as far as underwriting. I do think that that's a problem.

Again, I think it is crucial that these onsite reviews be done regularly. I think they are probably being done pretty regularly, but there has to be follow-up and there has to be consequences. And I don't really—we didn't really see that happening.

And they don't always have to be just bad consequences, but I do think that they need to be encouraged and told to be more prudent in some of the practices. I really think that that was the main—

Chairwoman VELÁZQUEZ. Would the gentleman yield?

Mr. THOMPSON. Sure. Please.

Chairwoman VELÁZQUEZ. IG, and one of those areas that really raised concern could be the exorbitant salaries that some of the CDC executives are getting. And the IRS reported that some of the executives make more than $500,000 a year, with some earning close to $1 million annually. Isn't that contradicting the mission of the CDCs?

Ms. GUSTAFSON. With the exception of a very few CDCs, which were not part of our sample on salary, these are nonprofits, and so these are eye-popping salaries. And, again, the crucial thing for us is all of the money that is being paid to salaries is necessarily not available for either reserve or for economic development in that community. And that is really what those CDCs are expected and really charged with doing. So it is a concern.

And so I hope that they do follow through with their agreement to look at maybe some requirements on reserves, how much needs to be there, use—

Chairwoman VELÁZQUEZ. Is that an area for SBA to—

Ms. GUSTAFSON. Absolutely. Yes.

Chairwoman VELÁZQUEZ. Thank you for yielding. Did you have another—

Mr. THOMPSON. No. My time had well expired beyond at that point when I yielded. Thanks.

Chairwoman VELÁZQUEZ. Mr. Schrader.

Mr. SCHRADER. Thank you, Madam Chair. Following up on that last line of questioning, I guess I would ask the Administrator, who, frankly, is new to the position, within a year, so a lot of this has happened on other people's watch, and she is working hard I think to correct that, is what I am hearing.

But with regard to the salaries, that has been a big issue in the financial debate. So how are you anticipating dealing with that with some of the CDC programs?

Ms. MILLS. These excessive salaries are deeply disturbing, and for exactly the reasons that the Inspector General just described. These are nonprofits, and any excesses are supposed to be reinvested in community development. And if they are not, this is inappropriate and has to change.

We are responsible for oversight of these CDCs, and we are now preparing new guidelines on corporate governance to address exactly this issue.

Mr. SCHRADER. To follow it, I guess I would ask the IG, you have talked a little bit about the HUBZone issue with the courts interpreting it one way versus another. I guess I would be interested in what you would—what direction you are looking for from the Congress. And, frankly, I would be interested in Ms. Mills' response to that also.

Ms. GUSTAFSON. Well, in all candor, that was actually Administrator Mills who talked about that—

Mr. SCHRADER. Oh, sorry about that.

Ms. GUSTAFSON. —talked about the HUBZone. But while—

Mr. SCHRADER. Chat away.

Ms. GUSTAFSON. While I am here, the one thing I do want to point out, without getting into a policy debate on preferential—on priorities of these programs, we have longstanding concerns about the ability to really enforce the HUBZone, just to put it out there. HUBZone is a difficult animal to get hold of, because it is hard to figure out where these companies—the majority of the employees live and whether they are really attempting to maintain the statistics that they have to as far as how many employees live in an economically disadvantaged area.

So this would be preferential treatment for the program that we think is hardest to really enforce, and very hard—Administrator Mills talked about an enhanced bid protest procedure. A lot of times these things are kind of dependent on the person who loses the bid to protest, and it is really hard for a losing bidder to know exactly where these companies are, especially in the really limited amount of time they have to do the protest.

And so those are the concerns that I personally—that I have as IG on this, but—

Mr. SCHRADER. Ms. Mills, would you comment, then, please?

Ms. MILLS. Yes. The SBA and the White House support the congressional intent of parity, or equal treatment, among the contracting programs, which is 8(a), HUBZone, service-disabled veterans, and the women-owned small business. The concern is that there was a recent court decision that potentially undermines the policy, because it interpreted the Small Business Act to provide for a HUBZone preference.

The administration supports the legislative efforts, which would confirm Congress's original intent to provide for parity.

Mr. SCHRADER. All right. Very good. A little different strain—we have tried it before, Administrator Mills, about some of the existing small business programs. And there has been interest, both in Congress and the administration, to increase some of the levels of opportunity within the 7(a) and 504 programs.

And we have had a conversation about larger small businesses and smaller small businesses, and talked a little bit about making sure that some of the smaller small businesses had enough in the pot that they could compete for, because some of the larger small businesses could eat up a lot of the increases that we both, you know, could argue about the number, but I think are important. Could you address that? How do you see us addressing that going forward?

Ms. MILLS. The President and the administration have asked Congress to consider raising the loan limits on 7(a) and 504 to $5 million. Currently, there are $2 million loan limits. The reason for this is that there is a gap in the marketplace. Many of the institutions that did do these larger loans for warehouses, and for financing some of these business development companies, are not in the market anymore. And so there is enormous pressure from everyone, from car dealerships and franchisees to manufacturers, who have capped out at the $2 million limit.

The concern was raised by you and also by the Chairwoman from the start that this would crowd out the smaller loans. The smaller loans are really extraordinarily important at the SBA, and these are the main street small businesses which we serve as the core of what we do.

So one of the things that has been suggested is that we cap the number of these jumbo loans that would be allowed, so that we serve that market, and do not allow them to crowd out the smaller loans. The concern is that these large loans are more profitable, larger, easier to do, and that the banks might not pay attention to the smaller loans. We cannot let that happen.

Mr. SCHRADER. I appreciate that. I yield back.

Chairwoman VELÁZQUEZ. Mr. Luetkemeyer.

Mr. LUETKEMEYER. Thank you, Madam Chair. Ms. Gustafson, very quickly, in your testimony you talk about a lot of things that are wrong or things to be changed or doing differently. Have you seen improvement over the last year or two in the way things have been done?

Ms. GUSTAFSON. Well, I have been here six months, but I will try to speak—

Mr. LUETKEMEYER. Okay.

Ms. GUSTAFSON. —on behalf of the office in general. I think—

Mr. LUETKEMEYER. You qualified your answer already. Okay.

Ms. GUSTAFSON. I think that, you know, I came into the job kind of at the tail end of the preliminary work that SBA had done on the Recovery Act, and big increase in those programs. And I know from speaking to my auditors, and working on it when I got there in October, we were really heartened by the amount of thought and work that went into trying to implement these programs and institute a risk management plan on these types of things, as opposed to doing it very quickly and dealing with the aftermath afterwards.

I am very heartened by Administrator Mills' statement that she is very serious about suspension, debarment, and enforcement. I do think that that's something that SBA has been lacking in. And because of a lack of resources, or just kind of in their more traditional role as an advocacy organization almost, I do think that that is somewhere that they have been lacking.

I am hopeful that we continue to work together and we do get a stronger suspension and debarment program in SBA. We are not there yet. I hope we see some suspensions and debarments. Traditionally, it has been very hard to get anybody debarred from an SBA program, unless there has been a conviction. And that is really not what the law is, and I think it is important to start really kicking people out of the program before they are going to jail.

And, you know, I have a commitment from the Administrator that she is going to work with us on that, and, you know, I think it is going to be very telling in the next several months whether we can really get that done. Suspension and debarment is a lengthy process, but the proof will be in the pudding pretty soon on these.

Mr. LUETKEMEYER. Okay. Great. You mentioned something a while ago about loan agent fraud. Can you explain that just a little bit for me, please?

Ms. GUSTAFSON. Yes. Our criminal investigators in the last several years have seen a really kind of distressing trend of very complex fraud schemes out there, not the traditional business owner who might be falsifying an equity injection to get a loan for his own personal benefit, or just because he can't quite make it.

We are seeing active conspiracies among people like loan agents, where they are packaging loans and taking part and falsifying documents, and it is not just one SBA loan, and it is certainly not just one government loan, and—

Mr. LUETKEMEYER. So the loan originator himself is a part—or herself is a part of the scheme to defraud the government or get people monies who don't really have—or shouldn't be eligible for them.

Ms. GUSTAFSON. Exactly. As I mentioned in my testimony, in the last 10 years, just talking about cases where we have been able to pursue criminal action, we are talking about loans of $250 million, where one of the bad actors is a loan agent who is actively involved in perpetuating the fraud.

And that is why one of the management challenges for the agency has been—it is very hard to track these loan agents, and it would be fantastic to be able to go to the database and start when you can see a trend, you can stop this stuff a lot sooner. And right now we don't have that capability, and so, again, in our agency management challenges, tracking loan agents and really monitoring that and trying to figure out both where the bad actors are and where just the bad loan agents who are doing bad loans are is crucial. It is really crucial, so—

Mr. LUETKEMEYER. Very good. Administrator Mills, what do you see as the environment out there right now? Do you see the continued increased demand for SBA loans? Is it tapering off? Do you see the economy—how is your office interacting with everybody? What do you see? You are on the front line.

Ms. MILLS. Yes. We are now operating at a very high level. We have put about $26 billion into the hands of small business through the Recovery Act due to the 90 percent guarantees and the fee reductions. So we are at above our 2007/2008 levels. We have completely come back at the SBA.

But the total environment out there is not back. There is still a problem with access to capital for small businesses, and it comes in a series of pockets. There are all kinds of underserved markets that are being left behind in the recovery. There are larger loans that aren't being made. There are lines of working capital being cut. There are commercial real estate issues. What we have done is identify those gaps, and then design our small business jobs bill request before Congress to meet each of these gaps.

Chairwoman VELÁZQUEZ. Time is expired.

Mr. LUETKEMEYER. Thank you, Madam Chair.

Mr. GRAVES. Madam Chair, can I interject real quick? To dovetail on what Representative Luetkemeyer said, and what I was talking about, too, as far as the status revoked of some of these firms, could we get a list from the last five years of the firms, your lending partners, whose status you have revoked?

Ms. MILLS. Yes.

Mr. GRAVES. Please.

Ms. MILLS. Yes.

Chairwoman VELÁZQUEZ. Mr. Nye.

Mr. NYE. Thank you, Madam Chairman. Inspector General Gustafson, I noted in your testimony—and we have talked a little bit today about the fraud that was uncovered in the service-disabled veteran program—you mentioned that your office is working with the Department of Justice to prosecute companies that were found to have defrauded the program. Can you give us a little detail on exactly what you are doing with Department of Justice and how far along you have gotten?

Ms. GUSTAFSON. As they are active criminal investigations, I can't. I will tell you that we pursued—we opened a case on every instance that GAO found, and we are still—some of these cases, many of these cases, are still active, and we really do anticipate getting some movement and getting some actions, getting some indictments. And when that happens, I can fill you in. But until then, in an open hearing, I really can't. I am sorry.

Mr. NYE. Okay. Can you talk a little bit about—you mentioned talking with Administrator Mills on an action plan and getting some input from her on some of the steps that can be taken to strengthen the enforcement, particularly on debarment and suspension. Can you talk a little bit about some of the specific steps you would like to see, and going back to the bid protest phase?

And you mentioned that one of the challenges—and I hear this from a lot of constituent companies at home—that they feel like the burden has been on them sometimes to point out the problem rather than having that happen as a matter of automatic course. Can you talk about what you would like to see?

Ms. GUSTAFSON. Right. That's exactly right on the bid protest. I mean, it is good to have a robust bid protest process, in case a losing bidder happens to have the information where they can pursue it. But the timelines are short, and the burden is really tough.

What I would like to see is multi-step. First, again, it is important that Administrator Mills has said that she will make sure the SBA is kicking people out of the program that don't belong there. But it really is going to be a big change for the agency to see themselves as a strong enforcement authority.

There needs to be some very strong training on what these programs are, when suspension is appropriate, when debarment is appropriate. We are always worried about programs where it is a self-certification program where you don't have to do a lot on the front end to prove that you should be in there. And service-disabled veteran is one of those where there is a lot of leeway to just get yourself on the list, and we are concerned about that.

Again, this is something we need to work with the VA on as well, but it concerns us. There needs to be—one of the things SBA is doing, for example, in the women owned small business programs, which is a new program that they have announced some regulations for, is requiring documents to be there, so that people can see. You know, it is just not enough to just say, "Yes, I qualify because I am this, this, and this and this." You have to submit some documents to show that.

I think that that is—that is crucial. It is too much—too much emphasis on the tail end which will never be completely effective. You have to have people hesitate before they decide to try to get in these programs, and I am not sure that that is happening right now.

Mr. NYE. Okay. Administrator Mills, can you just comment on your thoughts on steps that you will be taking to try to enhance that? And also, can you talk a little bit about your approach towards perhaps using suspension as maybe an intermediary step that might be easier to pursue than debarment?

Ms. MILLS. We see, in all our procurement programs, three phases of going after fraud, waste, and abuse. The first is on the front end, whether it is certification, or, in the cases of self-certification, we actually send a letter requiring people, under penalty of perjury, to re-self-certify, and we make sure that they know that we are serious and that they have to be eligible.

The second is site visits--ongoing and monitoring actual businesses. So once someone is in a program, we need to visit them. And as I said earlier, we are up to more than 1,000 site visits in HUBZone, for instance, in order to make sure that people who are supposed to be in the program stay.

And the third is we are committed to going after the bad actors. We are very grateful for the partnership with the IG. We think the suggestions the IG has made for training and other changes in order to be more effective in going after bad actors are very valuable, and we are going to pursue them aggressively.

This is a very high priority.

Mr. NYE. And just one last question. Do you intend to make greater use of unannounced site visits, the kind that really I think have a little bit more effect, since they don't know you are coming?

Ms. MILLS. Yes.

Mr. NYE. Thank you. I yield back.

Chairwoman VELÁZQUEZ. Mr. Bartlett.

Mr. BARTLETT. Thank you. I first want to apologize for being late. We just completed a markup in Armed Services.

I want to make a couple of comments about HUBZones, and then to ask a question about HUBZones. Most of our programs are meant to help disabled veterans or women, specific groups. The HUBZone program really helps whole communities.

As an example of that, I have a HUBZone contractor who has a facility, both in Howard County near NSA, and out in Garrett County. His facility in Garrett County pays his people there probably three times the mean annual salary in Garrett County. So it is a hugely important economic engine there.

He recently had an employee that qualified for a job in Howard County or one in Garrett County. He told the employee that if he went to work in Howard County, he would get $100,000; if he went to work to do the same kind of thing in Garrett County, he would get $70,000. The worker very wisely chose to go to work in Garrett County for $70,000, because he will live better in Garrett County on $70,000 than he would live with $100,000 in Howard County.

So this is a win-win program, both for the community because now we have people working in Garrett County at roughly three times the mean annual salary there, and now NSA can hire three people in Garrett County, where they could only hire two people in Howard County. So it is a win-win for both the government agencies and for the communities.

But, as you know, this program has been fraught with fraud, and that is partly our fault, because if you look at the 8(a) program and this program, we gave you, until very recently, enormously relatively more money to monitor the 8(a) program than we did the HUBZone program.

We were counting on something which runs contrary to good business practice, and that is we were relying on peers to say, "Joe over there is cheating. He really doesn't have enough of his people in the District, and that is—the office in the District is only a fraud. His main office is somewhere else."

Now we have given you more money, which we should have given you earlier, and I was pleased that you—how many site visits you said you had made. How are we doing it, making sure that this really worthwhile program is effectively monitored, so that people aren't able to cheat so easily?

Ms. MILLS. As I said, we have a three-prong—we are very committed to going after this fraud, waste, and abuse, and it has—this is an issue where we have done a lot of work. We still have more work to do.

In the front end, we have changed the certification and increased our requirements substantially. In the middle part, we have done the increased site visits, which went from I think seven in the six months before I came to now more than 1,000 in this year. And we have trained, so now we are doing unannounced site visits, and really much more robust, you know, activity in that, and people know we are serious. We are going after the bad actors.

So we are committed to executing this program at another whole level, because we have had lots of issues to address. We have addressed some of them. We have more work to do.

Mr. BARTLETT. I know that GSA has looked at this previously. Is GSA now following—I am sorry, GAO—GAO now following the progress that the administration is pursuing?

Ms. MILLS. GAO gave us several audits. We actually accepted I think 11 of the 12 recommendations, and really it is 12 of the 12, because we don't have any issue with the last one. So we are working with GAO. They have given us a very good road map in our contracting operations, and we are working to implement all of those recommendations.

We also have $2 million in the FY11 budget for increased oversight in our contracting programs.

Mr. BARTLETT. Are they happy with your progress?

Ms. MILLS. The GAO?

Mr. BARTLETT. Yes.

Ms. MILLS. Well, as I said, we accept all of their recommendations. So I hope they are happy.

Mr. BARTLETT. Well, but have you implemented them? You may accept them—

Ms. MILLS. Yes, we are implementing them.

Mr. BARTLETT. —but implementing something else.

Ms. MILLS. Yes, we are implementing all of them.

Mr. BARTLETT. And they are happy with the extent to which you have implemented them?

Ms. MILLS. You know, they are—

Mr. BARTLETT. Is there something in writing saying that, or have they not yet had an opportunity to do that specifically?

Ms. MILLS. I don't think that they have come back, but we hope that they will be very happy. We are working very much in good partnership with them, and we believe, as I said, there is more to do. But we are making progress.

Mr. BARTLETT. Thank you very much.

Chairwoman VELÁZQUEZ. Mr. Altmire.

Mr. ALTMIRE. Thank you, Madam Chair. Administrator Mills, we have talked extensively about the salaries issues, and I just had more point I wanted to ask about that, just for clarification. And as context, as you know, the IRS prohibits nonprofit entities from engaging in certain activities in order to maintain their status.

Specifically, nonprofits must ensure that earnings do not benefit any private shareholder or individual. And, as we have discussed, the CDCs at the heart of this report were paying an average of 25 percent of their earning in executive compensation, which, as most people would agree, is well above what you see generally in the nonprofit world. And you have said that you identify that as a problem and something you want to see corrected through the administration level.

But my question is: would the SBA—would you support legislation that moved forward that strips CDCs of their nonprofit status when executive compensation is deemed to be excessive?

Ms. MILLS. As we said, this is deeply disturbing, because the money that is—that goes into excessive salaries is really taken right out of the benefit of the community. And these CDCs are subject to our oversight, and we are going to issue corporate governance guidelines to this effect.

Mr. ALTMIRE. Good. But what—

Chairwoman VELÁZQUEZ. Would you yield, the gentleman yield?

Mr. ALTMIRE. I would, Madam Chair.

Chairwoman VELÁZQUEZ. Also, I would like to bring to the attention of the Committee and the Administrator that recent IRS records show that a number of CDCs have luxury cars for company use, including a CDC with Lexuses, another CDC driving a Mercedes, and yet another one with a high brand Acura.

So do you think that these type of amenities are consistent with the goals of the program? And when you say that you are working on corporate and governance, give us a timeline as to when those will be implemented.

Ms. MILLS. Well, this is increasingly disturbing information, and thank you for bringing that to our attention. We will give you a timeline, but this is for immediate attention.

Chairwoman VELÁZQUEZ. Thank you for yielding.

Mr. ALTMIRE. Certainly. So the question was about legislation moving forward. Do you feel, given your answer, that it wouldn't be appropriate, that you have identified this as a problem, and you think you can correct it administratively? Or if we did decide to move forward legislation, is it something that we would have your support on?

Ms. MILLS. Well, we certainly will move forward immediately on this, and we—I think we share the concern amongst us, so we are probably all in the same—of the same mind on this.

Mr. ALTMIRE. Great. Thank you.

Inspector General Gustafson, approximately 80 percent of loans guaranteed annually by the SBA are made by lenders to whom SBA has delegated the loan-making authority, as you know. And the SBA has centralized many loan functions and reduced the number of staff performing these functions.

So the SBA has given more responsibility and independence to its lenders, but the need for effective oversight would seem to be more important than ever, given that fact. So has the OIG identified any systemic deficiencies in the SBA's lender oversight and risk management efforts?

Ms. GUSTAFSON. We have been concerned with lender oversight as well. I know that there has been a very recent GAO report on lender oversight. We were actually intending to begin an audit of just the lender oversight process. And given the very extensive GAO report, which I thought, quite frankly, was very useful, we have held off on that, because it seems kind of duplicative to come in at a time when SBA has made attestations that they are going to work on the issues that GAO has identified.

We have concerns with lender oversight. We, of course, have had instances of lenders with delegated authority really doing some kind of bad things, and having delegated authority a lot longer than they really should have, based on some prior cases. And, obviously, that is a big concern for us.

So I would just echo what GAO has found. Sorry.

We have in the past reiterated that we do understand that SBA has a limited amount of resources, but still has a very important oversight role. We would like to see things like their onsite reviews timed more appropriately, so you have an onsite review at a time when you may be looking at a lender's delegated authority and their risk rating, and having the two kind of marry, so that it becomes a useful tool and a timely tool.

That is something that I think GAO echoed in their audit, and I think that would go a long way. When you have limited resources, directing the resources at the right time is crucial. I am going to read my post-it note for a second.

So we have found in our oversight of Recovery Act loans that we are concerned about the quality of purchase reviews. That is something that, again, needs to be really emphasized by SBA, and we come in and we have concerns about those. And, again, we are concerned about the quality of onsite reviews and the timing of onsite reviews. That is something that is on our radar and that we will be looking at as well.

Mr. ALTMIRE. Thank you, both.

Chairwoman VELÁZQUEZ. Mr. Buchanan

Mr. BUCHANAN. Hi. Administrator, I appreciate the opportunity. You called me at my office. We had a good discussion, so I appreciate the opportunity to be here today.

I read a little bit—I want to talk about health care. It is a little maybe off the subject, but I want to touch base on the White House had sent out a bunch of mailers of small businesses in terms of talking about tax credits and other things. What is the SBA doing to work with small businesses about the new health care bill in terms of compliance or in terms of tax credits that they might receive? Do you have an aggressive effort? Maybe you covered that, I don't know, I got here a little late.

But I just wanted to touch base on that, because that—I am hearing of that in the business community. I was back home this weekend, and we had an actual hearing in our area. But health care is a big issue for small businesses, and they are trying to make sense of where we are at in that process.

Ms. MILLS. Yes. We do have an aggressive effort in the area of making sure that small businesses that might be eligible for the new 2010 health care tax credits know that they might be. We immediately posted on our website the IRS guidance along with plain, common sense examples, so that a small business can walk themselves through what they might be able to apply for as a tax credit.

And I was saying that we are also going to train our personnel, and resource partners, to help a small business get the money that they need, because this is cash in their pocket in 2010. We believe that four million of the six million small businesses that have employees may in fact be eligible, so that is a pretty big number.

Mr. BUCHANAN. The other thing, on a little different note maybe, but we just had a conference that I spoke at where we had Panama and a lot of our people in our area, small business people primarily, looking to do more business in Central and South America and Florida. Has the SBA had discussions with the Export-Import Bank or the United States Trade Representatives on ways to increase exports by small businesses?

As you recall, the President made that part of his State of the Union as to he thought that was a great opportunity to create jobs, and I agree. And then, I don't know if you want to touch on the other thing, the free trade agreement that came up a lot about Panama and the U.S. and why we can't get that done.

Ms. MILLS. We are part of the President's National Export Initiative in which we are working to double exports over the next five years. Thirty percent of exports are done by small business under indexes, so there is a lot of opportunity. Only 250,000 small businesses export.

We at the SBA provide the leadership in the Small Business Export Trade Coordinating Committee, which includes Department of Commerce, Department of State, and the Export-Import Bank. So Gary Locke and Fred Hochberg and myself go on the road, and we have a big effort around small business exporting that is very much an interagency effort. We will be implementing a lot of new programs. We right now train 17,000 small businesses a year in exporting, but we are going to do more.

Mr. BUCHANAN. And my last question is just—we did a congressional hearing with a fellow member of the panel—he is actually chairman of the Finance and Tax; I am the ranking member—Congressman Schrader, in my district, I think Monday—Monday I guess it was, and we talked about access to capital. There still appears to be all the banks in our area—maybe it is different in different areas, especially all the community banks, but even the bigger banks, have—they are not in the business of lending money, but that is their primary source.

Is there any way that the SBA in this environment, because it is so tough for small businesses to get access to credit, that they could do any kind of direct lending of qualified small businesses? Because I have got to tell you, we had one guy as a witness that does consulting for the region, and he says he is, you know—credit that was very easy to get or they have had more than enough collateral, they can't get—there is no credit, absolutely zero, or very little available, because they are looking at past earnings in our region, and a lot of businesses haven't done very well the last year or two. Is there any thought about that at all?

Ms. MILLS. Well, we know you were kind enough to invite one of our capital access folks down there with you, and you have a particularly—

Mr. BUCHANAN. And he did a good job, by the way.

Ms. MILLS. —tough—thank you. We have a great team. But you have a particularly tough geography, and your banks have been hit hard and are recovering more slowly.

We have brought our SBA lending back above the 2007/2008 levels, but the rest of the market is not recovering as fast. So what we have done is go through where the gaps of the markets are. And we have proposed specific parts of the jobs plan, whether it is something for commercial real estate, owner-occupied commercial real estate, whether it is something for working capital lines of credit, or just continuing this really successful 90 percent guarantee and fee reductions.

That is only continued now through I believe the end of May. We very much hope that Congress might consider continuing it further, at least for the fiscal year end.

Mr. BUCHANAN. Thank you, and I yield back.

Chairwoman VELÁZQUEZ. Time is expired. Ms. Kirkpatrick.

Ms. KIRKPATRICK. I want to thank both of you for the good job that you have done in a relatively short time, and, you know, I have seen an improvement in my district. And, Administrator Mills, I especially want to thank you for your attention to rural Arizona, and for coming to Arizona, and the time that you have spent on the phone with me talking about this.

You know, it is still that balance between adequate documentation for small businesses and making sure they get the money they need. I am still seeing that problem in rural Arizona where even in good times small businesses struggle. And so when the criteria is really tightened, they don't look good compared to the urban businesses, and we are still struggling with that.

And I just wondered—I wanted to follow up a little bit with Mr. Buchanan's line that, you know, I hear it from a lot of my small businesses, they would prefer to apply directly to the SBA and not to have to go through a bank, because the major banks who are carrying the SBA loans have good relationships with metropolitan businesses, but they are not informed about how small businesses in rural areas work.

And so maybe—I would like your thoughts about the SBA, you know, lending directly. Also, you know, is there any criteria with the major banks that they fund a certain portion of small business loans in rural America?

Ms. MILLS. On the question about rural loans, you know, we are working very hard on that, and I am actually pleased that I have recently seen some data that actually in Arizona things are lightening, because that was one of the areas that had lagged.

On the issue of direct lending, I think the Chairwoman has also raised that issue, you know, from the beginning. We looked at it very hard. We had a whole task force around it. The issue of actually executing and operationalizing that has some unintended consequences and some costs related to it.

And so we have gone in the direction of looking at the specific gaps and driving the program that we have to reach the areas that are not getting reached, you know, particularly the underserved markets, some of the smaller loans, which are still highly problematic.

Ms. KIRKPATRICK. Would part of that effort be requiring the banks who receive SBA funds to fund a certain number of—or a certain percentage of small business rural businesses?

Ms. MILLS. We have not yet considered that.

Ms. KIRKPATRICK. Okay. All right. And then, Inspector General Gustafson, you talked—I am a former prosecutor, so I know a little bit about how hard it is to prosecute white collar crime. What kind of resources do you need to be able to do a better job?

Ms. GUSTAFSON. Well, everybody could use more resources. I have a tremendous staff of criminal investigators, but I appreciate your discussion about prosecutors. I was a former prosecutor, too, and I remember white collar cases, and I hated them because they are hard and they are complex. I would rather take a drug case any day, in all candor.

I think what would really be helpful for us to get more bang for our buck would be, quite frankly, some change in the laws. Right now, not only are these cases tough and complex, but a lot of them, especially those in the contracting area, are no loss cases, which is to say the government got a contract, the government got services, and especially under federal sentencing guidelines it becomes very unappealing to go to an Assistant U.S. Attorney and say, "I need you to devote six months to this case," and the guy is probably going to get probation.

And that is something that in my understanding, there had been an approach to the Federal Sentencing Commission, and some resistance to that. A lot of times that kind of movement takes a statutory change. And if these people who really are defrauding the government, and taking money that is not meant for them, are going to prison, some of this—a lot of this would stop. And so that is something that would be incredibly helpful.

On these complex cases, we have suggested longer statutes of limitation, because they are very complex. And, you know, I have a good staff, but I have under 50 investigators and billions of dollars out there that I am trying to oversee. And so it is tough.

Chairwoman VELÁZQUEZ. Would you—

Ms. GUSTAFSON. Yes, I am sorry.

Chairwoman VELÁZQUEZ. I am sorry.

Ms. GUSTAFSON. Yes, I will yield. Go ahead.

Chairwoman VELÁZQUEZ. I am sorry I interrupted you.

Ms. GUSTAFSON. That is okay.

Chairwoman VELÁZQUEZ. Just finish your line of thought.

Ms. GUSTAFSON. I have lost it.

[Laughter]

Chairwoman VELÁZQUEZ. I am sorry. I am sorry. Would you yield? I know you are talking about how difficult it is to prosecute this type of white collar cases. But if we have proper oversight by the agency, and then it will make your job much easier.

Ms. GUSTAFSON. Actually, the best way to deter these people is to hit them in the pocketbook, and that can be done with stronger enforcement. If they think on the front end that they are not going to get to where they are getting the money, that is a really strong deterrent, as opposed to maybe getting restitution at the end. It is a lot harder to get it back once it is out the door, so I agree with you wholeheartedly.

Chairwoman VELÁZQUEZ. Thank you for yielding.

Ms. KIRKPATRICK. Thank you. Thank you, Madam Chairman.

Chairwoman VELÁZQUEZ. Who else? Do you have any other questions?

[No response.]

I do have more questions. I would like to talk about SBA lender oversight. And, Ms. Mills, or, no, Ms. Gustafson, in May 2003, an IG audit of the microloan program identified deficiencies in the SBA's oversight of lenders. Six years later, in April 2009, the IG reported that SBA still had not taken final action to develop a comprehensive microloan program standard operating procedures.

It also has not set program goals or moved to require outcome-oriented data from all program participants. Why are we seeing this failure to take appropriate corrective actions?

Ms. GUSTAFSON. That is a question that would be hard for me to answer. You are right, I think the microloan program is woefully understaffed. I think that they definitely need to have this oversight in place. I can't explain why it hasn't happened. I would note that lender oversight in general has been a management challenge for the agency for years, and last year, just looking at a report, we haven't seen a change, we haven't seen an improvement yet on some of these. So it is a problem.

Chairwoman VELÁZQUEZ. Administrator Mills, particularly at a time when small businesses are struggling in getting capital, microloan lending has been an important element that really helped some of those who have not been able to access capital. So we need to make sure that microloan lenders are complying with the law. And for that, we need proper oversight.

Ms. MILLS. Madam Chair, you are exactly right. And this is now on us, and we are addressing it. We are working with the IG, increasing the staff, and writing the SOP. We need more clarity and more simplification. We actually have a program for automation. The place had no automated systems, all paper.

Chairwoman VELÁZQUEZ. Timeline?

Ms. MILLS. That is unacceptable.

Chairwoman VELÁZQUEZ. Ms. Mills?

Ms. MILLS. Pardon?

Chairwoman VELÁZQUEZ. Timeline?

Ms. MILLS. Timeline?

Chairwoman VELÁZQUEZ. Yes.

Ms. MILLS. Well, this is immediate. We are in process. We just—

Chairwoman VELÁZQUEZ. Okay.

Ms. MILLS. —hired a new branch chief last week, and the SOP is being written. And we can give you a timeline.

Chairwoman VELÁZQUEZ. Okay. Administrator Mills, SBA recently put out a request for quotation worth up to $5 million for a task order consulting contract. This potential award has now been limited to four companies, including McKinsey and Company. This contract expands on work done under a previous contract performed by McKinsey.

Given that a number of senior officials, including yourself, worked for McKinsey, does the agency have any officials outside reviewing these contracts?

Ms. MILLS. We have a very robust competitive contract system.

Chairwoman VELÁZQUEZ. I am asking about a truly independent third party. I am not—does the Board have outside people who do not—are not working for the agency or have worked for McKinsey?

Ms. MILLS. The contracting process is an independent competitive process. I don't personally get involved with any individual contracts. It is very important that that process be complied within an orderly process, because, as you said earlier, we are the standard.

Chairwoman VELÁZQUEZ. Okay. My question is: does SBA have officials outside the SBA reviewing these contracts?

Ms. MILLS. I am not familiar with the individual contract, and we would be happy to get back with you and answer your question.

Chairwoman VELÁZQUEZ. Okay. In addition to the problems identified in the recent CDC PCL audit, the IG also conducted a review of the 7(a) loans disbursed pursuant to ARRA. The IG found numerous deficiencies in this program. The SBA has an outstanding request for over half a billion dollars to fund the 7(a) and 504 programs through the end of the fiscal year. What is the SBA doing to address the problems identified by the IG? And how is the agency working to ensure taxpayers' money is being used responsibly?

Ms. MILLS. This review of the IG actually turned out to be extremely helpful in giving us guidance of how to solve a problem which was unacceptable, and that was that the guidelines that we had given, according to the Recovery Act, required additional documentation, but it turned out the loans didn't have that documentation, because it wasn't clear to the lenders and the borrowers that they had to have these certifications. I think it was an additional immigration certification or a workforce certification.

But now, thanks to the IG for pointing it out in this early audit, we were able to simplify and clarify what the requirements were and get it on track in an efficient way. And to us it is an example of how to work productively with the IG.

Chairwoman VELÁZQUEZ. In exercising our oversight role, this Committee could request contract file of the agency whenever we are in that process. We did so, and the SBA General Counsel indicated that they lost materials associated with an award. Is that a common occurrence, or is this the first time that such a thing happened?

Ms. MILLS. Well, whether it is common or the first time, it is deeply disturbing. And we are getting—I am aware—that this file went missing. We are able to reconstruct the file. I think we have sent half of it to you, and the rest of it will come to you, and we will get it to you. And we are doing an investigation.

Chairwoman VELÁZQUEZ. I take the responsibility, the oversight responsibility, of this Committee very seriously, whether it be a Democratic administration or a Republican administration in the White House. And I want to make that clear. So it is nothing personal. It is our duty to do that. And I expect that when documents are requested, they are made available to us.

Ms. MILLS. Absolutely.

Chairwoman VELÁZQUEZ. Thank you. Any other member has any question?

[No response.]

So with that, I ask unanimous consent that members will have five days to submit a statement and supporting materials for the record. Without objection, so ordered.

This hearing is now adjourned.

[Whereupon, at 11:30 a.m., the Committee was adjourned.]

NYDIA M. VELAZQUEZ, NEW YORK
CHAIRWOMAN

SAM GRAVES, MISSOURI
RANKING MEMBER

Congress of the United States
U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-6315

STATEMENT
Of the Honorable Nydia M. Velázquez, Chairwoman
United States House of Representatives, Committee on Small Business
Committee Hearing: *"Oversight of the Small Business Administration and its Programs"*
Wednesday, April 21, 2009

In January of last year, the House adopted Rule 11, requiring regular hearings on waste, fraud and mismanagement of programs under the committee's jurisdiction. Since then, we've held no fewer than 18 oversight hearings, spanning a broad range of issues from federal contracting to SBA disaster loans. Today's discussion is in that vein. It will allow us to build on past oversight hearings, providing a much-needed opportunity to examine some of the agency's most critical programs. And it could not come at a more pressing time.

Over the last two years, our economy has endured a seemingly endless parade of challenges. While these setbacks have differed in scope and industry, they have managed to have the same impact on small firms. Even today, as we steadily climb back towards recovery, entrepreneurs face obstacles. Now, more than ever, they need the resources necessary to not only overcome those roadblocks, but to keep our recovery strong.

Historically, the SBA has helped deliver that support. It has served as a vital source of stability for small companies, particularly during periods of economic decline. But, as this committee is well aware, the agency has also struggled in areas ranging from lending to procurement. After years of underfunding, SBA continues to wrestle with a legacy of neglect—one that has eroded its oversight mechanisms and left many of its programs in disarray. With an emphasis on accountability and a strong commitment from the Inspector General, we can tackle those issues directly.

As Judge Brandeis famously said, sunshine is the best possible disinfectant. And make no mistake—there is no better tool for scrubbing out waste than transparency. When it comes to holding agencies accountable, the Inspector General has a critical role to play, and I am pleased the IG is with us today. It is my hope that our conversation will serve as a frank and open forum for examining SBA's problem areas. Because until we've identified those concerns, we can neither move forward with solutions nor expect to see improvements.

When SBA programs are running at full capacity, they are true economic catalysts. Just look at Small Business Development Centers. In 2008 alone, they helped generate 58,000 new jobs at a cost of $3,000 a piece. Or, consider the Recovery Act's SBA loan provisions. They have allowed the agency to support more than $23 billion in lending. At a time of historic declines in the small business capital markets, that particular effort has been nothing less than a lifeline. But, unfortunately, not all of SBA's initiatives have been quite so successful.

Later this morning, we will look at a number of IG reports, all of which point to problems within SBA programs. In some instances, core initiatives have been wracked by fraud. In other cases, they have been undermined by questionable practices. It is imperative that these troubled programs be restored to reflect their original mission—strengthening and supporting small businesses. Because at the end of the day, small firms aren't just the "backbone" of our economy—they are our greatest source of job growth.

According to a recent study by the Kauffman Foundation, virtually all net new jobs created between 1980 and 2005 came from startup companies. With unemployment at 9.7%, it only makes sense to focus on these firms—the small and startup businesses that have always provided job security. With a portfolio of strong, well-managed SBA programs, we can do that very thing. I know I speak for all members of the committee when I say we are dedicated to upholding the integrity of the agency's programs, and to ensuring small firms have the tools and resources they need to thrive.

U.S. HOUSE OF REPRESENTATIVES

SMALL BUSINESS COMMITTEE REPUBLICANS

REPRESENTATIVE SAM GRAVES, RANKING MEMBER

Contact: Alexandra Haynes
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Opening Statement for Hearing:
"Oversight of the Small Business Administration and its Programs"
Sam Graves
Ranking Member
House Committee on Small Business
United States House of Representatives
Washington, D.C.
April 21, 2010

I would like to thank the Chairwoman for holding this important hearing today on oversight of the Small Business Administration and its programs. I look forward to hearing from the Administrator and Inspector General on some very critical issues concerning the management of the Agency's lending programs.

The SBA lending programs operate in coordination with the private sector by guaranteeing loans made by banks and certified development companies. Due to the possibility that taxpayers could have to pay on the guarantee, the programs should be overseen with the utmost care and transparency.

SBA regulations and procedures are supposed to be designed to protect the federal government. However, the Inspector General's recent report indicates that lenders have been failing to comply with SBA requirements. This should raise a red flag at the Agency, but it appears that little has been done to correct this problem.

Additionally, the Inspector General's report raises significant concerns about SBA program management. Poor oversight increases the risk to the taxpayer. While I am generally supportive of programs designed to assist small businesses in obtaining scarce credit and capital, I cannot and will not maintain that support when the programs are not properly monitored to protect taxpayers from unnecessary risk.

Ultimately, the issue of today's hearing is whether SBA lending programs operate primarily for the benefit of the lenders or for the small business borrower. I believe that Congress wants these programs to assist small business borrowers. If this is, in fact, the case, the Agency must take aggressive action to ensure that only the most responsible lenders are involved in these programs. Anything less would be unacceptable to Congress and the taxpaying public.

Again, I thank the Chairwoman for holding this important hearing. I am looking forward to hearing witnesses' recommendations on how we can increase the availability of capital to small businesses without placing the taxpayers in jeopardy for the poor business management decisions of the SBA's lending partners.

U.S SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

TESTIMONY OF KAREN G. MILLS

ADMINISTRATOR

U.S. SMALL BUSINESS ADMINISTRATION

BEFORE THE

U.S. HOUSE OF REPRESENTATIVES COMMITTEE ON SMALL BUSINESS

ACCOUNTABILITY UPDATE

APRIL 21, 2010

Chairwoman Velazquez, Ranking Member Graves and members of the Committee, it's an honor to again be with you today. In working with you over the past year, these meetings have been important and helpful. It's truly a shared endeavor to improve oversight and risk management, while removing waste, fraud and abuse.

I'm pleased to say that we're making good progress. One tangible metric is that we've cut the number of overdue IG audit findings by more than half – from 97 last June to 48 this March. We also have less than 50 open recommendations from the GAO, having closed 6 full audits since 2008 due to satisfaction of recommendations.

We also just received our fourth consecutive Certificate of Excellence in Accountability Reporting[1] for our Agency Financial Report and our Summary of Performance and Financial Information.

But we know there's more work to do. It's now part of SBA's Strategic Priorities to build on this progress in two particular areas.

The first area is our government contracting and business development programs, where we have efforts aimed at all three steps of the process:

- At the front-end, it means more upfront certification and eligibility.
- For small businesses already in the program, it means more efforts with compliance and site visits.
- And if they're found to be out of compliance, it means pursuing and removing bad actors.

Already, we made dramatic increases in the number of site visits to HUBZone firms – from less than 100 in 2008 to over 900 in 2009. We're on track to do more than

[1] From the Association of Government Accountants

1,000 this year. We're working to ensure that only legitimate and eligible firms are benefiting from HUBZone.

In our 8(a) program, we agree with nearly all of GAO's recent recommendations. Already, we're training our field staff to more quickly identify ineligible firms. And when it's clear that fraud exists, we're taking steps to debar and/or work with the Department of Justice to prosecute.

We also did the first comprehensive review of 8(a) in a decade and proposed regulatory changes. We went to 10 cities, held two tribal consultations, and received extensive public comments. GAO has given us positive feedback on how we've handled this process.

As a result, we'll clarify what it means to be "economically disadvantaged" and we'll help small businesses get the maximum benefit from joint ventures and mentor-protégé relationships.

The President's FY11 budget requests $2 million for strengthening efforts to prevent fraud, waste and abuse in our contracting programs.

The second area is lender oversight, where we're working to instill best practices that will ensure compliance and manage risk more effectively as we work with our lending partners.

In fact, the FY11 budget requests $2 million more for lender oversight and on-site reviews, as well as $1 million for stronger program assessments. This will include efforts with our Certified Development Companies in the 504 program, including Premier Certified Lenders.

Overall, the entire SBA team is focused on continued vigilance in identifying, tracking and reducing risk. Through our partnership with this Committee – and with insights from the GAO and our Inspector General – I know we moved in the right direction this past year, and we'll continue to take even bigger steps in the future.

Separately, an important issue has come up in the past few days that I'd like to bring to the Committee's attention. The SBA and the White House support the Congressional intent of parity – or equal treatment – among our contracting programs: 8(a), HUBZone, service-disabled veteran and, soon, women-owned small businesses. However, in light of a recent court decision, it would be useful to clarify and reiterate Congress's original intent that there be parity among the programs. The Administration supports legislative efforts to confirm Congress's original intent to provide for parity.

I welcome any questions, concerns, and comments about our efforts in any of the areas I've mentioned today.

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STATEMENT OF PEGGY E. GUSTAFSON
INSPECTOR GENERAL
U.S. SMALL BUSINESS ADMINISTRATION

BEFORE THE SMALL BUSINESS COMMITTEE,
UNITED STATES HOUSE OF REPRESENTATIVES

APRIL 21, 2010

Introduction:

Chair Velazquez, Ranking Member Graves, and distinguished members of the Committee, thank you for giving the Small Business Administration (SBA) Office of Inspector General (OIG) the opportunity to discuss some of our current activities.

As you know, I am the head of an independent office established within SBA by statute to deter and detect waste, fraud, abuse and inefficiencies in SBA programs and operations. Every year, our staff of approximately 110 employees, which includes criminal investigators, auditors, and program analysts, conducts numerous criminal investigations to identify fraud and other wrongdoing throughout the country, and issues dozens of audit reports identifying weaknesses and deficiencies in SBA programs and operations. We also issue an annual report identifying what the OIG believes to be the most significant management challenges for the Agency. Since it would be impossible to discuss all of our current efforts in the time allotted, my testimony today will focus on several recent audits and reviews we have completed, several important indictments and convictions we have obtained through criminal investigations, and two new management challenges that the OIG introduced in October of 2009. To review our reports and learn more about my office's activities, I invite you to visit our website at www.sba.gov/ig.

Audits:

During the first 7 months of Fiscal Year (FY) 2010, the OIG issued 24 reports of audits and other reviews, containing 97 recommendations to SBA to promote efficiency and reduce waste. A number of these reports focused on the early identification of problem loans and Agency controls over programs financed by the American Recovery and Reinvestment Act (Recovery Act).

PCL/CDC Executive Compensation Report. In March of this year, the OIG issued a report on an audit of the underwriting practices and compliance of three of the largest Premier Certified Lenders (PCLs) in the CDC/504 Loan Program. This program is administered through cooperative agreements with non-profit organizations, called Certified Development Companies (CDCs), who work with private sector lenders to provide financing for real estate construction and other capital projects to eligible for-profit businesses. CDCs typically originate CDC/504 loans and forward them to SBA for approval; however, lenders granted PCL status are authorized to approve, close and service CDC/504 loans, with SBA reviewing the loan requests only for eligibility.

The OIG found that PCLs may not have used prudent practices in approving and disbursing 68 percent of the sampled loans, totaling nearly $8.9 million, due to (1) poor loan underwriting and (2) eligibility or loan closing issues. Projecting the sample results to the universe of CDC/504 loans disbursed in FY 2008 by the three PCLs, we estimated that at least 572 loans, totaling nearly $254.9 million in CDC/504 loan proceeds, had weaknesses in the underwriting process, eligibility determinations, or loan closing practices. The OIG estimated that a minimum of 183 of these loans, totaling $56.4 million or more, were made to borrowers based on faulty analyses of whether they could repay the loans. We also estimated that loans totaling $209 million involved problems in determining borrower eligibility and/or loan closing issues.

Further, our examination of CDC expenditures for executive compensation disclosed that eight CDCs paid more than 20 percent of their gross receipts towards executive compensation, one of which paid almost 44 percent. SBA regulations require that any excess funds remaining after payment of staff and overhead expenses be retained by the CDC as a reserve for future operations or for investment in other local economic activity; therefore, high compensation expenditures reduce the amount of funds for the reserve or for economic development activity.

The OIG recommended that SBA revise its procedures to clarify the analysis that CDCs should use to determine borrower repayment ability and borrower eligibility, and that SBA develop a process to ensure that corrective actions are taken in response to the Agency's onsite reviews if errors are identified with CDC underwriting and loan origination practices. The OIG also recommended that SBA consider establishing guidelines on the level of excess funds that CDCs should retain as a reserve or invest in other local economic and development activities.

Oversight of Recovery Act Programs. The Recovery Act, which was signed into law on February 17, 2009, contains a number of provisions intended to help SBA promote economic recovery for the nation's small businesses. These include reduced loan fees, higher guaranties, new SBA credit programs, secondary market incentives, and enhancements to current SBA programs. In order to provide enhanced levels of transparency and accountability, the Recovery Act and implementation guidance from the Office of Management and Budget require increased reporting and oversight to deter and detect fraud, waste, and abuse and ensure that program goals are met. Since the passage of the Recovery Act, the OIG has developed a Recovery Oversight Plan; created a separate group within the Auditing Division to oversee SBA Recovery Act Programs staffed with several temporary auditors, program analysts, and contractors; and issued 14 Recovery Oversight reports, identifying programmatic and other deficiencies.

Recently, the OIG completed an audit of loans made by lenders under the 7(a) program subject to SBA guaranties. Our review examined loans disbursed under the authority of the Act to determine whether they were originated and closed in compliance with SBA policies and procedures and to identify any evidence of suspicious activity. We reviewed a statistical sample of 30 Recovery Act loans that had been reviewed and approved by SBA and 30 loans that had been approved by lenders without SBA review. Our review identified deficiencies in 23 percent of the SBA-approved loans and 53 percent of the lender-approved loans. These problems included deficiencies in change of ownership transactions; the absence of borrower certifications as to whether they were engaged in a pattern or practice of hiring or recruiting illegal aliens for employment in the United States; and miscellaneous origination, closing and eligibility deficiencies. The inappropriate approval of these loans both increased the risk of loss to SBA should the loans default and reduced the availability of SBA loans to other eligible borrowers.

The OIG recommended that SBA improve lending program procedures and processes and provide additional training for lenders and Agency personnel involved in approving loans.

Procurement audits. We also recently completed several audits that raised concerns with SBA's procurement of goods and services. In February, we issued a report on an audit of SBA's annual certification regarding the quality of the Agency's acquisition data in the Federal Procurement Data System (FPDS). Data in FPDS must be accurate because it is used to report on government contracting actions, procurement trends, achievement of small business goals, and contract activity under the Recovery Act.

The OIG found that SBA certified to the accuracy of its FY 2008 contracting data, even though 92 percent of a random sample of contract actions reviewed by the OIG contained one or more inaccurate or incomplete data elements in FPDS. Most of the problems noted involved inaccurate data entries involving the size of the business, the North American Industrial Classification System code used to determine the size standard, type of award, the contractor's Data Universal Number System (DUNS) number, and location of contract performance. While SBA had developed a data quality plan for FY 2008, it did not fully implement the plan, which contributed to the errors identified by the OIG. Further, due to the volume of errors identified in FPDS, it appears that contracting personnel did not review FPDS data inputs to ensure they reflected accurate information, as required by the Federal Acquisition Regulations.

Our review of the accuracy of SBA's data from FY 2009 showed a higher rate of error in that approximately 97 percent of the contract actions sampled contained one or more inaccurate or incomplete data elements, indicating continued problems with reviews by SBA contracting personnel of data accuracy. However, overall, fewer problems were noted with each data element.

The OIG recommended that SBA either update its FY 2008 data quality plan or revise applicable procedures to include explicit steps to be taken to ensure data is reviewed for accuracy and completeness; conduct an independent review to ensure that the data quality plan or procedural requirements have been fully implemented; and ensure that contracting personnel are held accountable for the accuracy of FPDS data. In response to these recommendations, SBA stated that it would revise the data quality plan to include specific steps that must be taken to ensure data is properly reviewed for accuracy and completeness, and would provide training to contracting specialists/officers to reinforce this effort. In addition, the Agency awarded a contract to conduct an independent review of the FPDS data, and stated that it would revise annual performance plans for contracting specialists/officers to include a critical element associated with the accuracy and completeness of FPDS data.

In April, the OIG issued two additional reports raising concerns about SBA's procurement function. One report found that the current workforce involved in procurement actions is insufficient to effectively award, administer, and oversee Recovery Act contracts as well as other SBA contracts. Without adequate staff to perform contract execution and administration functions, and to oversee the contractors, the Agency is exposed to an increased risk of mismanagement, improper payments, fraud, waste, and abuse. In response to the OIG's recommendation, SBA agreed to implement a staffing solution.

In the second April report, we found that SBA did not report all non-competitive contract actions to Recovery.gov and mischaracterized some of the actions it did report. SBA agreed to take all of the recommended actions.

Criminal Investigations:

During the first six months of this fiscal year, OIG criminal investigations resulted in 51 indictments and 14 convictions. Potential recoveries and fines from these investigations totaled approximately $16 million. Most of our investigations involve false statements by white collar criminals who seek to manipulate SBA programs for their personal gain. These cases involve: (1) fraud by borrowers who seek to obtain SBA-guaranteed loans or disaster loans; (2) fraud by company executives who seek to use programs set-aside for small, disadvantaged, or other minority-owned businesses to obtain government contracts; and (3) fraud by loan agents and/or lender employees who seek financial gain by orchestrating origination of multiple SBA-guaranteed loans based on falsified information.

Fraud by loan agents and other consultants involved in packaging or brokering 7(a) loans remains a significant problem. For many 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. Although loan agents often serve a useful purpose by helping to connect borrowers with guaranteed lenders, unscrupulous agents have pursued multi-million dollar fraudulent schemes involving numerous loans. In the last decade, the OIG has obtained convictions and guilty pleas on numerous cases involving loan agent fraud, totaling in excess of $260 million. In the last six months alone, fraudulent schemes involving loan agents have been identified in more than $60 million of SBA loans.

For example, in February of this year, as a result of a joint investigation between the OIG and the Federal Bureau of Investigation (FBI), a 185-count indictment was unsealed charging eleven individuals in Missouri with various federal crimes for their involvement in a scheme involving at least 31 fraudulent business loans, totaling more than $10 million. Among those charged were a former executive vice president and chief lending officer of a bank, a former SBA branch manager, and two business consultants that assisted in putting the loans together.

Also in February, as a result of a joint investigation between the OIG and the FBI, the former owner of an Illinois finance company was sentenced to 135 months imprisonment, five years supervised release, and ordered to pay restitution of $7.4 million. He previously pled guilty to providing false bank entries, reports, and transactions. The investigation revealed his involvement in a scheme to provide fraudulent information to a lender and SBA to approve a $1.35 million SBA-guaranteed loan to one of his companies. In addition to obtaining an SBA loan for himself, he brokered 46 SBA-guaranteed loans—totaling more than $44 million—for others which he admitted involved the submission of false information to lenders.

The OIG also remains concerned about fraud in the 8(a) and HUBZone Programs and other contract preference programs for small and socio-economically disadvantaged businesses. Recent OIG audits and investigations, and recent reports from the Government Accountability Office show that ineligible companies continue to obtain set aside contracts and that non-disadvantaged individuals are exploiting these programs. Recently, an investigation by OIG working with other agencies led to the U.S. Air Force issuing indefinite suspensions to 19 companies and 4 individuals affiliated with a subsidiary of an Alaskan Native Corporation. The suspension actions stemmed from a multi-agency investigation of a conspiracy by the principals of the subsidiary and its numerous business entities to defraud the SBA and the U.S. Defense Department by failing to divulge business and ownership agreements in order to remain in the 8(a) program.

The OIG is also working with the Department of Justice to pursue criminal and civil False Claims Act prosecution against companies that the GAO identified as fraudulently obtaining contracts under the HUBZone and Service Disabled Veteran contracting programs. Additionally, we are working with SBA so the Agency can develop a more robust debarment and suspension program. The OIG believes the Agency needs to be more aggressive in pursuing debarments and other enforcement activity against companies that wrongfully obtain preferential contracting benefits.

Management Challenges:

As required by law, the OIG issues a report in October of every year identifying key management challenges for SBA. Our most recent report contained ten management challenges, including two new challenges dealing with: (1) improper payments in the Disaster and 7(a) Loan Programs, and (2) SBA's management of a major project to integrate its loan monitoring and financial management systems and move them to a new operating platform, known as the Loan Management and Accounting System (LMAS).

Improper Payments. Recent OIG audits of SBA's Disaster and 7(a) Loan Programs determined that the improper payment rates that SBA had 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. However, the OIG reported that improper payments should be based on loan disbursements, not loan approvals, and estimated that the improper payment rate was at least 46 percent of $3.4 billion in loans disbursed in 2007, or approximately $1.5 billion. SBA also reported that the improper payment rate for the 7(a) Program was 0.53 percent for FY 2008. Of $869 million in total outlays during that fiscal year, this would represent improper payments of $4.6 million. However, the OIG estimated the rate to be 27 percent, or approximately $234 million. We concluded that 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 SBA Office of Financial Assistance inappropriately overturned improper payments identified by reviewers. As a result, we added this as a management challenge for SBA, and identified recommended actions to improve SBA's reporting of improper payments, reduce the rate of improper payments, and increase recovery of improper payments.

Loan Management and Accounting System (LMAS) Project. In November 2005, SBA initiated the 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 SBA's mainframe. With an estimated cost of over $250 million, LMAS is currently SBA's largest IT project. When completed, it will increase functionality, reduce data entry redundancies, and allow real-time updates and inquiries of loan data. Previous OIG reports have stressed the urgency of replacing the current loan accounting system, which presents substantial risk to SBA because it 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. 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 found that SBA had not established either an enterprise-wide or project-level Quality Assurance 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 met Agency standards.

Due to the importance of this project, the OIG added this as a management challenge for SBA, and provided recommended actions to improve SBA's acquisition process for the LMAS project. Although SBA has taken steps to address the OIG's concerns, more needs to be done.

Conclusion:

In conclusion, the OIG will continue to aggressively investigate fraud in SBA programs, and will continue to seek creative and effective ways to improve internal controls within SBA to limit waste and inefficiency within agency programs and operations.

Thank you for the opportunity to comment. I look forward to answering any questions that you may have.