LONG-TERM OBJECTIVE 4.3

Financial management systems will support both the SBA strategic management and financial accountability by providing financial information that is useful, relevant, timely and accurate and which assists the SBA in maximizing program performance and accountability.

4.3.1 By FY 2006, achieve a Status rating of Green for the Financial Management initiative of the PMA.

During FY 2005, SBA continued building on the significant improvements it has made in financial management over the past several years. The SBA received an unqualified opinion from its independent auditors for FY 2005 and one of the two material internal control weakness from the FY 2004 audit was eliminated—the designation of credit subsidy modeling. The SBA retained its Green rating for Progress for the Financial Management PMA and will retain the Red for Status because of the one remaining material weakness. For FY 2006, the SBA will be working on removing the remaining material internal control weakness—financial reporting. These results are a major achievement for the Agency and the Agency will build upon it to fulfill its mission effectively.

During the year, the Agency completed actions to address all of the issues raised by its independent auditor in the FY 2004 financial audit. SBA was able to complete these improvements while accelerating its financial reporting cycle to meet the November 15 financial statement deadline for the second year in a row. The OCFO continued the use of the internal teams established last year to address the audit findings and solve problems that required the involvement of subsidy, budget and accounting personnel. The team-based process has helped facilitate strong communication and accountability within the OCFO. In addition, several critical staff positions were filled with experienced individuals, bringing more leadership and expertise to the OCFO.

In FY 2005, the internal control processes over financial reporting and subsidy cost modeling were further enhanced. For example, a tool was created to ensure consistency across loan data extracts for accounting and subsidy purposes. This has resulted in expedited reconciliations and enhanced quality control over the loan program elements of the Agency's financial reports. Additional resources were added to the financial reporting team during the year, which allowed the team to complete more quality assurance testing throughout the reporting cycle and improve documentation of processes. The OCFO led an extensive effort to identify and deobligate any invalid obligations, which also improved the accuracy of the financial reports.

SBA's new director overseeing credit subsidy modeling continued to make significant progress in enhancing controls around the data, models and processes used in estimating the credit program costs. Also, for the first time ever, SBA completed subsidy reestimates for every program. For some of its smallest loan programs, the Agency had never before completed reestimates. This was accomplished under the new director's "no loan left behind" policy.

During the year, the OCFO led the SBA's effort to develop and begin the implementation of a plan for compliance with the new Appendix A requirements of OMB Circular A-123, Management's Responsibility for Internal Control, which becomes effective in FY 2006. The Agency established a Senior Assessment Team, which includes senior managers from all of the SBA's major offices, to participate in the A-123 implementation.

Beyond attaining and maintaining a clean audit opinion with no material internal control weaknesses, to be Green, the Agency must be continuously expanding the use of financial management data by program managers for decision-making. Although the SBA still has one material internal control weakness to eliminate, the SBA is pushing forward with respect to using financial data to manage its programs on a daily basis over the past year. For example, SBA began actively using its Loan/Lender Monitoring System, a state-of-the-art tool for risk-based management of lenders and the Agency's loan portfolio.

4.3.2 By FY 2005, achieve a rating of Green for the Budget and Performance Integration initiative of the PMA.

As a result of the SBA's accomplishments in integrating its budget processes and its performance, the Agency has maintained the rating of Green it received in FY 2004 on both Progress and Status on this President's Management Agenda item. This rating of Green was achieved a year and a half ahead of the Agency's plan.

The cornerstone of the Agency's integration of budget and performance is its five-year strategic plan. The plan was designed such that all Agency programs and administrative activities support SBA's four goals. Each goal has Long-Term Objectives with measurable outcomes and outputs. The main thrust behind the creation of the new SBA's Strategic Plan was to set outcomes that would allow the Agency to measure the impact that the Agency may have on the small business community compared to a similar group of small business.

A major achievement during FY 2005 was the elimination by the Office of Inspector General of the Management Challenge affecting budget and performance integration. This challenge read: Challenge 1. SBA needs to improve its managing for results processes and performance data.

The OIG concluded that the Agency's progress in this area was such that the existence of the Challenge was no longer warranted.

In FY 2005, the SBA began the implementation of an independent evaluation of many of its programs, to be conducted by an outside contractor. This was a direct result of OMB recommendations in the PART process. SBA conducted discussions with all major program offices developing the scope and methodology for the program evaluation study. This phase of the study will be finalized in FY 2006. Once study instruments are approved by OMB, the SBA will begin its research. The Agency also continues its three-year impact study, spearheaded by the Office of Entrepreneurial Development, on the technical assistance programs for which they are responsible. Additionally, the HUBZone program evaluated for the first time its impact on small businesses.

This year, all planning and budget processes were conducted in the context of the Agency's strategic goals. Management was informed about performance data (output goals, accomplishments, and efficiency measures) when making budget decisions. This was true of all major budget processes, including the annual operating budget, mid-year reviews, and planning for FY 2007.

For a number of years, the Agency has used an activity-based costing model, which identifies the full cost of each of its programs. This model is based on a survey conducted each year. To further refine the survey, OCFO staff met with all program offices to review in detail how the survey is conducted, how costs are determined, and how indirect and overhead costs are allocated. Through these meetings and subsequent discussions with program offices, the activities to which staff attribute their time and the manner in which program costs are determined by activities were refined in order to improve the survey. The results of the activity-based costing model allow SBA to identify the full cost of its programs.

That information led, in part, to the Agency's discontinuing a program that was deemed too expensive to the taxpayer and to the decision to centralize certain administrative activities. The decision to centralize the 7(a) loan liquidation function has led to significantly greater savings than projected. The cost of this activity was $32 million in FY 2003. The SBA had estimated that cost to drop to an estimated $16 million in FY 2006 (a 50% reduction in cost). However, in FY 2005 the cost had already fallen to $7.4 million, a reduction of 77% in nominal terms.

The Agency has established annual performance indicators for all programs. These indicators appear in the Performance and Accountability Report and in all performance and budget documents. The Agency also maintains an Executive Scorecard. This scorecard is used by senior management to periodically review the accomplishments of Agency managers in achieving their goals.

A factor in the process of budget and performance integration has been the training of program offices. This year the training has focused on data validation and source documentation. One result of this training is that the Office of Entrepreneurial Development has revised the manner in which the number of people trained is counted, to avoid double counting, and to ensure comparability among technical assistance programs.

In order to ensure Agency-wide participation in the strategic plan, annual performance appraisals for all managers have included an element rating them on how well they contributed to the Agency's achievement of its goals. Appraisals for non-supervisory staff also include such an element. These appraisals are referred to at SBA as "personal business commitments."

Intermediate Outcome Measure: No SBA programs are rated by OMB's Program Assessment Rating Tool as "Results Not Demonstrated"

To date, 10 of the Agency's programs have been evaluated by OMB using the Program Assessment Rating Tool (PART). This year this assessment focused on the HUBZone, 8(a), and Surety Bond Guarantees programs. The OCFO aided the process by providing hands-on training to program offices and helping them through the process. The objectives of the training were the analytical PART process, linkage of PART questions with Agency's Strategic Plan, and identification and research of internal and external sources of supporting documentation. The results of the PART evaluation of the Agency's programs are also a cornerstone of the SBA's Green in performance and budget integration. For an agency to receive a Green in this PMA initiative, no program may be rated as Results Not Demonstrated for two or more years. Although SBA received a Results Not Demonstrated in its Business Information Centers program, the Agency received Green in FY 2005 because the program has been discontinued.

4.3.3 Each year, SBA financial systems will meet the standard as prescribed in the Federal Financial Management Improvement Act (FFMIA).

SBA has continued to make progress in this area. However, SBA has still not fully met the standards prescribed in the Federal Financial Management Improvement Act (FFMIA) because of lingering information technology constraints and limited resources. The Agency has developed compensating procedural controls for some items where it could not correct the problem technologically, but the financial system has still been deemed not in compliance by the independent auditor. The status is a reportable condition, however, not a material weakness. While SBA will make resolving this a high priority in FY 2006, it may take several years to fully comply with the standards prescribed in FFMIA because of the cost and level of effort required.

4.3.4 Each year, SBA will receive an unqualified opinion on its financial statement audit.

The mission of the SBA OCFO is to use its personnel, processes, and systems to achieve sound financial management and to produce accurate, timely, and useful information to support operating, budget, and policy decisions. SBA's top ongoing financial management objective has been to obtain and maintain a clean audit opinion, as that is the primary measure of quality financial management. SBA's clean audit opinion this year marks the Agency's achievement of a significant objective and puts the Agency in a strong position to move forward in accomplishing many new things in financial management. Achieving and maintaining Green in the PMA for financial management and eliminating improper payments are also high priorities for the Agency.

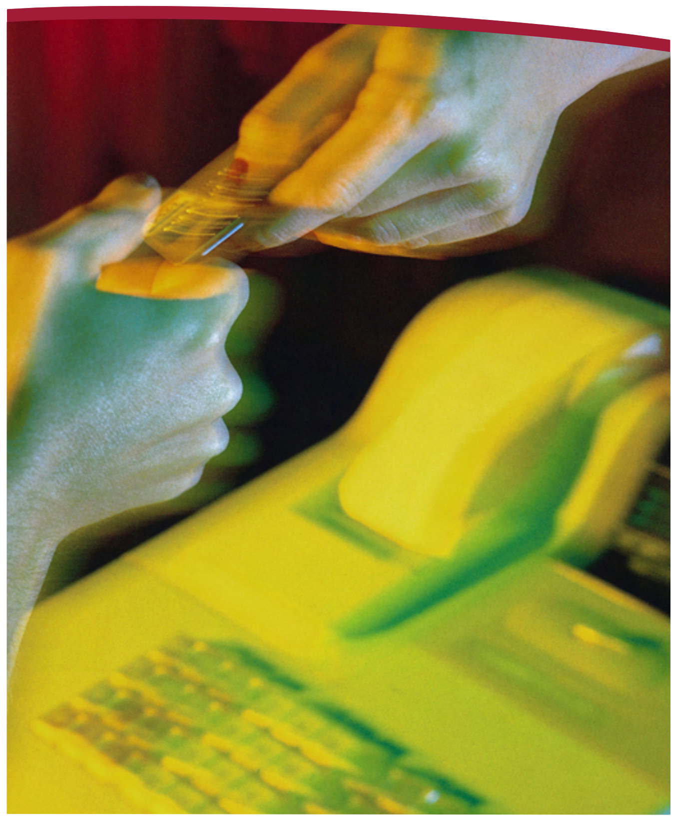
SBA's plan for maintaining a clean audit opinion is based on a commitment to continuous improvement. The Agency will continue striving to reduce the time required to produce financial data while improving the quality of the data. This will ensure the Agency continues to meet the accelerated financial statement reporting schedule. More accessible data will also create more opportunities to analyze the information and identify issues and trends that may be of interest to management. SBA will have a new independent auditor in FY 2006, so SBA anticipates it will be an interesting and challenging year as the new auditor will undoubtedly bring new perspectives and ideas for SBA's financial management.

A second critical element of SBA's financial management plan is to maintain Green on the President's Management Agenda for Financial Management. In addition to maintaining a clean audit opinion, to be Green the Agency must continuously expand the use of financial data for operational decision-making. SBA's plan for expanding managers' use of financial management data is focused on two key areas – improving the Agency's debt collection information and processes, and reducing interest paid under the Prompt Pay Act. Another key area in SBA's financial management plan is the implementation of OMB Circular A-123. The Agency will be working in all of these areas in the coming year.

Overall, the SBA will continue using a team-based approach for resolving audit findings and identifying and solving new issues. The Agency was able to fill several critical positions within OCFO last year with strong new team members. The SBA anticipates continuing to build its team both with a few new additions and by providing training and cross-training opportunities. Finally, imperative to the success of the Agency is its ability to facilitate strong, constructive communication, both within the OCFO and between the OCFO and the IG, independent auditor, and OMB.

SBA's financial management plans also include achieving and maintaining a Green status rating for the Improper Payment component of the President's Management Agenda by the first quarter of FY 2006. The Agency is committed to carrying out the required improper-payment assessments and analysis and taking steps to implement any identified remediation actions.

As required by the Improper Payments Information Act (IPIA) the SBA reviewed its payment programs during FY 2005. From this analysis, the SBA identified the 7(a) guaranty purchase program as high risk under IPIA guidelines issued by the OMB in its memorandum M-03-13 dated May 21, 2003. The SBA has also included three other major credit programs in this report in accordance with OMB guidance in OMB Circular A-136, as these programs were previously identified by OMB in the former Section 57 of OMB Circular A-11 as subject to Improper Payment reporting. The four SBA credit programs included in this report are the 7(a) Business Loan Program, the Section 504 Certified Development Company (CDC) Debenture Program, the Small Business Investment Company (SBIC) Program and the Disaster Assistance Loan Program. The following report is formatted to include the content as specified in OMB Guidance in Circular A-136.



I. Describe your agency's risk assessment(s), performed subsequent to compiling your full program inventory. List the risk-susceptible programs (i.e., programs that have a significant risk of improper payments based on OMB guidance thresholds) identified through your risk assessments. Be sure to include the programs previously identified in the former Section 57 of OMB Circular A-11.

Response: Risk assessments have been performed for the SBA's credit programs previously identified under Section 57 of OMB Circular A-11 reporting requirements. The credit programs are: 7(a) business loan guaranty purchase, Certified Development Company Program, Small Business Investment Company Program, and Disaster Loan program.

The 7(a) guaranty purchase program utilized a new Quality Assurance Program in FY 2005. The 7(a) guaranty purchase program includes the National Guaranty Purchase Center in Herndon, VA, which purchases defaulted 7(a) guaranties, as well as centers in Fresno, CA, and Little Rock, AR, which purchase defaulted SBAExpress guaranties. Based on the initial results of the 7(a) quality assessment program, this process has been designated as high risk under IPIA guidelines. The delegation of responsibility for 7(a) guaranty issuance, servicing and liquidation to SBA's participating lenders around the U.S. creates a high risk of improper payment that is subject to SBA oversight, monitoring and attention to identified discrepancies.

The risk of improper payments in the CDC program is deemed by SBA to be practically non-existent due to extensive control over guaranty processing and purchase operations that includes review by program and legal professionals prior to issuance of the guaranty and the purchase of defaulted guaranties. SBIC program improper payment risk is minimal, again due to extensive operational controls, including legal review over guaranty issuance and default purchase activities. Disaster program risk of improper payment is minimal because of operational controls over the Disaster application, damage verification, credit review and loan closing activities.

II. Describe the statistical sampling process conducted to estimate the improper payment rate for each program identified..

Response: 7(a) guaranty purchase statistical sampling utilized OMB memorandum M-03-13 dated May 21, 2003. A sample of 120 for the NGPC and 36 each for Fresno and Little Rock was used. Each of the 192 purchases sampled was subjected to an independent review that thoroughly examined the guaranty issuance, lender SOP compliance and purchase procedures. The 504 program statistical sampling was not completed because each and every guaranty issued is subject to thorough review by SBA program and legal professionals, and due to the non-existence of improper payment in this program. The SBA has petitioned the OMB for an exception to IPIA reporting requirements.

The SBIC improper payment rate was determined using its examination program in FY 2005, which conducted approximately 250 examinations of leveraged SBICs, or almost 74% of all leveraged SBICs. Although this was not a statistical sample, it provided more reliable results than a smaller sample would have. Improper payments arise when an examination finds a participating security funded investment has a variance from SBIC program regulations, or when an instance of fraud is reported or when a discrepancy is noted in SBA's leverage funding process. Results were compiled for the Participating Security program in this report because government expenditure is required for the advances made to the holders of participating securities.

The Disaster loan improper payment rate was determined by the Office of Disaster Assistance (ODA) Quality Assurance Review process (QAR). The QAR process consists of a review of 120 loan files in each of the Disaster Area Offices, or a total sample size of 480 files. The scope of ODA's review covers three primary compliance areas: basic eligibility; adherence to relevant laws, rules, regulations and standard operating procedures; and credit worthiness. The QAR sample size far exceeds that required by OMB guidance in its memorandum M-03-13 dated May 21, 2003.

III. Describe the Corrective Action Plans for:

A. Reducing the estimate rate of improper payments. Include in this discussion what is seen as the cause(s) of errors and the corresponding steps necessary to prevent future occurrences. If efforts are already underway, and/or have been ongoing for some length of time, it is appropriate to include that information in this section.

B. Grant-making agencies with risk susceptible grant programs, discuss what your agency has accomplished in the area of funds stewardship past the primary recipient. Include the status of projects and such results of any reviews.

A. Response: The 7(a) guaranty purchase program plan is to identify and track the reasons for any improper payments discovered in the QAP, and then make appropriate changes in the QAP to reduce the purchase error rate. This will be accomplished by focusing on purchase policy and procedures that may require revision, and by developing additional training materials based upon policy or procedural changes put into effect. In this regard, in April 2005, SBA issued a major update to the SOP that will ensure greater accuracy and uniformity in the guaranty purchase process.

The CDC program risk of improper payment is practically non-existent. The SBA has submitted a request to the OMB for exception to the requirements of the IPIA for the CDC program.

The SBIC guaranty program includes mandatory training for program participants in program regulations, and participants must demonstrate adequate resources to comply with regulations. Also, credit checks are performed on potential program participants to assure only fiscal prudent managers are admitted. A financial incentive is provided to program participants having "clean" reports and examinations will focus on participants having the greatest risk to the government. Finally, SBA will review the "out-funding" process and make any improvements necessary to avoid improper payments.

The error rate on Disaster loans is consistently well below the IPIA 2.5% and $10,000,000 thresholds. The ODA will continue to update its QAR program over Disaster field offices and continue the automation of its operations. The SBA has requested that the OMB provide an exception to IPIA reporting requirements for the Disaster Program.

B. Response: Not Applicable–SBA is not a grant making agency.

IV. Improper Payment Reduction Outlook FY 2004 – FY 2007.

Response: The SBA's planned reduction of Improper Payments is shown as required in the following table.

Improper Payment Reduction Outlook

($ in millions)

Program	PY[a] $ Outlays	PY IP %	PY IP $	CY[a] $ Outlays	CY IP %	CY IP $	CY[a]+1 Est. $ Outlays	CY+1 IP %	CY+1 IP $	CY[a] +2 Est. $ Outlays	CY+2 IP %	CY+2 IP $	CY[a]+3 Est. $ Outlays	CY+3 IP %	CY+3 IP $
7(a) Guaranty Purchase	707.4	NA	NA	605.1	5.20	31.4	600.0	5.00	30.0	600.0	4.90	29.4	600.0	4.80	28.8
CDC Debentures[b]	141.3	NA	NA	117.6	NA	NA	110.0	NA	NA	110.0	NA	NA	110.0	NA	NA
SBIC Part. Securities[c]	2,786.60	4.65	129	1,568.20	0.67	10.5	1,500.0	2.25	33.7	1,200.0	2.00	24.0	1,000.0	2.00	20.0
Disaster Loan Program	806.4	0.13	1.1	2,230.50	0.07	1.6	4,000.0	0.50	20.0	1,300.0	0.33	4.3	1,300.0	0.25	3.3

a. Outlays in this report represent the "base amount" of the program activity related to SBA Improper Payments; and this amount will differ from the amount reported as outlays in SBA's PB 06 submission because PB 06 outlays include reestimates of subsidy cost, reimbursements to SBA administrative funds and other costs

b. The SBA has petitioned OMB for an exception to IPIA reporting requirements for the CDC Debentures program.

c. SBIC Participating Security program guaranties are reported in FY 2005 because government expenditure is required for the advances made to the holders of participating securities. FY 2004 reporting included SBIC debentures and Participating Securities.

d. A five-year historical average of Disaster activity was used to project CY +1, 2 and 3 Est. $ Outlays figures. The Disaster CY outlay figure will depend on the magnitude of Gulf Coast loans.

V. Discuss your agency's recovery auditing effort, if applicable, including any contract types excluded from review and the justification for doing so; actions taken to recoup improper payments, and the business process changes and internal controls instituted and/or strengthened to prevent further occurrences. In addition complete the table below:

Agency component (if applicable)	Amount subject to Review for CY Reporting	Actual Amount Reviewed and Reported	Amounts Identified for Recovery	Amounts Identified/ Actual Amount Reviewed	Amounts Recovered CY	Amounts recovered PY(s)
NA	NA	NA	NA	NA	NA	NA

The SBA's credit programs reported under IPIA requirements are not subject to recovery auditing activities. SBA's programs, however, do include activities to recover improper payments if appropriate.

Response: The target for recovery of 7(a) improper payments made in connection with guaranty purchase disbursements has been set at 80%. These recoveries will be obtained through negotiating with SBA participating lenders or through enforced collection procedures if negotiation proves to be unsuccessful in reaching a settlement. The CDC program does not have any improper payments and recovery activities are not required. Improper payments made in the SBIC program are rectified through changes in funding arrangements or Agency liquidation activities in the SBIC program, and a recovery rate target is not required. Disaster program improper payments are recovered through its servicing and liquidation of loans that may be made improperly. The SBA has determined that it is not appropriate to demand the immediate repayment of a loan made improperly to a disaster victim, and recovery rate targets are not appropriate.

VI. Describe the steps the agency has taken and plans to take (including time line) to ensure that agency managers (including the agency head) are held accountable for reducing and recovering improper payments.

Response: The Improper Payment initiative is included in the President's Management Agenda along with the Administration's other management initiatives. The SBA's Strategic Goal Four is to assure the SBA programs operate efficiently and effectively, including compliance with PMA initiatives. The SBA's Strategic Goals are included in annual performance plans for all of its programs as business objectives, and these business objectives are included in employee performance plans. SBA management monitors accomplishment of its business objectives in its performance plan using its Execution Scorecard, and action is taken when progress is not on target. Executive and management bonuses are based on the accomplishment of business objectives included in employee annual performance plans.

VII. A. Describe whether the agency has the information systems and other infrastructure it needs to reduce improper payments to the levels the agency has targeted.

Response: The newly-developed Guaranty Purchase Tracking System supports the 7(a) guaranty purchase process very well, and it will be continually updated to enhance the overall integrity of the purchase process. The SBA's information systems adequately support the CDC program and this program does not have any improper payments. The SBIC program has a program data system that adequately tracks examinations, examination findings and their resolution, and its improper payment rate is very low. Also, all individuals are empowered to refer any SBIC case of suspected fraud to the Inspector General. The Disaster loan program historically has the information systems and other infrastructure needed to minimize improper payments. An integrated loan processing system has been implemented to streamline and enhance the Disaster loan-making process. It replaced multiple systems that adequately supported disaster operations. The new system will support workflow management, electronic file management and document generation functions. An objective of the system is to improve the Quality Assurance process in order to minimize future improper payments.

B. If the agency does not have such systems and infrastructure, describe the resources the agency requested in its FY 2005 budget submission to Congress to obtain the necessary information systems and infrastructure.

Response: Not applicable.

VIII. A description of any statutory or regulatory barriers which may limit the agencies' corrective actions in reducing improper payments.

Response: Not applicable. The SBA does not have any statutory or regulatory barriers limiting improvement to its performance on the Improper Payments initiative

IX. Additional comments, if any, on overall agency efforts, specific programs, best practices, or common challenges identified, as a result of IPIA implementation.

Response: The SBA has applied to OMB for an exemption to the requirements of the IPIA for its CDC and Disaster programs because improper payments are non-existent or very minimal. The SBA's risk assessment of improper payment in these programs, as well as the SBIC program, indicate a low level of risk below the IPIA threshold. The OMB has not yet issued this requested exemption, and the SBA has therefore continued to report these credit programs according to IPIA requirements in OMB Circular A-136. In addition, the SBA will apply for an exemption in FY 2006 for the reporting of its SBIC program under IPIA because of the low risk of improper payment in this program that falls below the IPIA threshold.

4.3.5 By FY 2008, budgeting and performance measurement will be fully integrated at SBA.

SBA is well on its way to meeting this outcome measure. Continuing to improve and utilize the cost model, completing program performance evaluations for all major programs, and basing budget decisions on the results of program performance have been incorporated as part of SBA's regular business processes. These practices will continue to build on themselves and SBA will remain a leader in this area in the Federal Government.

4.3.6. By FY 2008, 75% of non-financial managers will agree with the statement that financial performance information is being used in SBA budget formulation and strategic planning and that they understand how such uses have been relevant to their own areas of responsibility.

Now that the SBA has improved its core financial management processes, attained a clean audit opinion, and met the accelerated financial reporting schedule for two years in a row, the Agency is prepared to begin devoting significant resources to this outcome measure. As described in 4.3.4 above, the Agency must demonstrate that it is continuously expanding the use of financial data for operational decision-making under the PMA. The OCFO will lead the Agency's efforts in working with program managers to expand their use of financial data for budget formulation, strategic planning and operations.

Office of Lender Oversight

In FY 2005, the Portfolio Analysis Committee (PAC) meetings became a part of the Office of Lender Oversight's (OLO) operations, where management review and discuss analysis of useful, relevant, timely and accurate performance data to maximize the 7(a) and 504 program performance. In FY 2005, OLO set up the Lender Oversight Committee (LOC) meetings, where senior management utilize relevant, timely and accurate performance data to maximize accountability as it relates to the supervision of lenders and taking action as necessary to address issues associated with high-risk lenders. In FY 2005, OLO developed the Lender Risk Ratings, which are currently being tested, and which will be implemented once the OLO regulations are issued in FY 2006. The risk ratings use both past performance and expected future performance, and are a key component in efficiently and objectively evaluating and monitoring every 7(a) and 504 lender on a quarterly basis. Earlier, OLO had developed the Loan and Lender Monitoring System (L/LMS) by which program and lender performance data are analyzed and monitored; and in FY 2005 L/LMS was acknowledged as a promising practice in the Federal Credit Management Programs publication, sponsored by IBM. In addition, in FY 2005, OLO conducted 75 on-site reviews of some of SBA's largest lenders.

During FY 2005, SBA published the Administrator's delegations of authority to OLO and the two committees: PAC and LOC. Subsequently, OLO drafted a major rewrite of the SBA's lender oversight activities regulations, which will shortly go into clearance. OLO also drafted standard policies and procedures governing the conduct of on-site lender reviews, which has been cleared internally by all but two offices. OLO is also drafting a proposed notice on the Lender Risk Ratings developed in FY 2005.

Finally, in FY 2005 OLO developed the Lender Portal for L/LMS, which allows SBA lenders, district offices, and other SBA offices to access risk ratings and other performance metrics on any individual SBA 7(a) or 504 lender. A proposed notice on the Lender Portal will be drafted shortly. All of these actions strengthen SBA's strategic management and financial accountability, which will improve portfolio performance for the 7(a) and 504 small business loan programs.