

# U.S. Small Business Administration Office of Inspector General

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Semiannual Report to Congress  
Fall 2004



April 1, 2004 – September 30, 2004

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# Inspector General Act Statutory Reporting Requirements

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The specific reporting requirements prescribed in the Inspector General Act of 1978, as amended by the Inspector General Act Amendments of 1988, are listed below.

<i>Source</i>		<i>Page</i>
Section 4(a)(2 )	Review of Legislation and Regulations	19, 22 & 24
Section 5(a)(1)	Significant Problems, Abuses, and Deficiencies	3-21
Section 5(a)(2)	Recommendations with Respect to Significant Problems, Abuses and Deficiencies	37-41
Section 5(a)(3)	Prior Significant Recommendations Not Yet Implemented	34-36
Section 5(a)(4)	Matters Referred to Prosecutive Authorities	42-47
Section 5(a)(5) and 6(b)(2)	Summary of Instances Where Information Was Refused	None
Section 5(a)(6)	Listing of OIG Reports	26-27
Section 5(a)(7)	Summary of Significant Audits & Other Reports	3-21
Section 5(a)(8)	Audit Reports with Questioned Costs	28
Section 5(a)(9)	Audit Reports with Recommendations that Funds Be Put to Better Use	28
Section 5(a)(10)	Summary of Reports From Prior Semiannual Reports Where No Management Decision Was Made	30
Section 5(a)(11)	Significant Revised Management Decisions	None
Section 5(a)(12)	Significant Management Decisions with Which the OIG Disagreed	None

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## A Message From The Inspector General

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I am pleased to present the Small Business Administration (SBA), Office of Inspector General (OIG), Semiannual Report summarizing activities from April 1, 2004, through September 30, 2004.

As an independent, objective reviewer and evaluator of the operations and activities of the SBA, the OIG seeks to target potential financial vulnerabilities and fraud in SBA programs, promote effective program management, ensure sound Agency financial and management information, and improve information security management. During this reporting period, we issued 27 reports with significant recommendations for improving Agency operations, reducing fraud and unnecessary losses, and recovering funds. OIG investigations led to 58 indictments and 17 convictions of subjects who defrauded the Federal Government. In addition, the Office collectively reviewed 151 legislative, regulatory, policy, procedural, and other proposals concerning the SBA and Government-wide programs. With a staff of about 100, the OIG continues to produce substantial savings and important program improvements.

This reporting period has been one of continued transition for the Agency and the OIG. To improve our ability to address the rapid changes taking place in the Agency, the OIG responded to the recent centralization of the loan guaranty purchase and liquidation processes by assigning four of our audit staff to SBA's new National Guaranty Purchase Center (Center) in Herndon, Virginia. This move will enhance our ability to provide the Agency with timely information, observations, and recommendations on systemic issues. We have already published a key report addressing problems with the Agency's planning process for the Center.

Further, during this reporting period, our Investigations Division and subject matter experts in the Auditing Division have worked closely to identify significant fraud—especially in 9/11 disaster loans. We also made significant strides in addressing fraud by borrowers who falsely claim to be United States citizens. The OIG has also targeted loan agent fraud, and recently, a loan agent pled guilty to conspiracy and fraud in a scheme involving at least \$28 million in loans.

During the past 6 months, we issued reports focusing on a number of SBA's major management challenges, particularly in the areas of loan guaranty purchases, information security, financial management, and business development. While much remains to be done, SBA is making progress on a number of its challenges. Meanwhile, we continue to work closely with SBA to help resolve these issues.

I would like to thank Administrator Barreto for his support of the OIG's work. We will remain vigilant in protecting the interests of American taxpayers as we work with SBA and the Congress to achieve measurable results.

Harold Damelin  
Inspector General

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# Overview of the SBA and the OIG

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## The Small Business Administration

The Small Business Administration (SBA) was established in 1953 to assist small businesses from startup through the many stages of growth. The SBA's two major goals are to help small businesses succeed and to assist victims in recovering from disasters. The SBA offers many services to entrepreneurs through its Offices of Capital Access, Entrepreneurial Development, Government Contracting and Business Development, and Disaster Assistance. Services include providing (1) assistance with developing business plans through counseling services and resource partners, (2) financing through the Agency's various business and disaster lending programs, (3) marketing products and services, and (4) access to Federal procurement opportunities. The SBA's programs are delivered by a network of field offices in every state, the District of Columbia, the U.S. Virgin Islands, Guam, American Samoa, and Puerto Rico. The SBA had an FY 2004 appropriation of \$756 million, and, as of September 30, 2004, had 2,467 employees (this number includes Office of Inspector General (OIG) personnel but excludes disaster-funded employees).

## The Office of Inspector General

The SBA OIG was established by the Inspector General (IG) Act of 1978. Pursuant to this authority, through its four divisions, the OIG performs the following functions nationwide.

- **The Auditing Division** performs program performance reviews, internal control assessments, and financial, information technology and mandated audits, and oversees audits by contractors to promote the economical, efficient, and effective operation of SBA programs.
- **The Investigations Division** manages a program to prevent and detect illegal and/or improper activities involving SBA programs, operations, and personnel. The criminal investigative staff carries out a full range of traditional law enforcement functions. The security operations staff ensures that all Agency employees have the appropriate background investigations and security clearances for their duties and conducts the name check program, which provides SBA officials with character-eligibility information on loan applicants and other potential program participants.
- **The Counsel Division** provides legal and ethics advice to all OIG components, represents the OIG in litigation arising out of or affecting OIG operations, assists with the prosecution of civil enforcement matters, processes subpoenas and Freedom of Information and Privacy Act requests, and reviews and comments on proposed Agency policies, regulations, legislation, and procedures.
- **The Management and Policy Division** provides business support (e.g., budget/financial management, human resources, information technology, and procurement) for the various OIG functions, and coordinates legislative, regulatory, policy, and procedural review and analysis. It also prepares the Semiannual Report to Congress and the Report on SBA's Management Challenges and develops OIG strategic and performance plans.

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## Overview of the SBA and the OIG

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The OIG is headquartered in Washington, DC, and has field audit and investigation staff located in Atlanta, Chicago, Dallas, Denver, Houston, Kansas City, Los Angeles, Philadelphia, New York, and Seattle. An organization chart for the OIG is located in Appendix X.

As of September 30, 2004, the OIG had 96 staff on-board. The OIG's FY 2004 appropriation was \$13.358 million, including a \$495,000 transfer for disaster assistance oversight activities (net of rescissions).

The OIG's responsibility is to improve SBA programs by identifying key issues facing the Agency, ensuring that corrective actions are taken, and promoting a high level of integrity. We continue to focus on serving the needs of our customers and stakeholders and on safeguarding SBA resources from waste, fraud, and abuse. The five strategic goals we seek to achieve are to: (1) prevent fraud and unnecessary losses in SBA programs, (2) improve the security over and the accuracy of SBA accounting and management information, (3) assist SBA in improving its small business development and government contracting programs, (4) assist SBA management in identifying and resolving persistent and emerging management issues, and (5) strengthen our ability to identify and have maximum impact on the most significant SBA issues.

OIG efforts and accomplishments during the second half of Fiscal Year (FY) 2004 are summarized in the following pages. All audits and reports for this reporting period are listed in Appendix I. All investigative actions are summarized in Appendix IX.

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## Significant OIG Activities

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### **Goal: Prevent Fraud and Unnecessary Losses in SBA Programs**

The SBA has a wide range of programs designed to help small businesses gain access to capital, participate in the Federal procurement market, and better plan and manage their operations. The majority of SBA's resources are devoted to providing financial assistance to qualified small businesses. With more than 5,000 lenders authorized to make SBA loans, the Section 7(a) Guaranteed Loan Program is the SBA's largest lending program and the principal vehicle for providing small businesses with access to credit they cannot obtain elsewhere. This program is vulnerable to fraud and unnecessary losses because it relies on numerous parties (including borrowers, loan agents, lenders, and SBA) to complete loan transactions. Additionally, during the past 12 years, SBA has increasingly delegated more authority to its lenders. The number of loans originated under this delegated authority has grown from approximately 20 percent of SBA's loan volume in 1992 to over 75 percent today. As SBA has moved away from approving individual loans and placed more responsibility and independence on its lenders, the importance of OIG oversight has increased significantly.

The Disaster Loan Program is another key SBA lending program, which provides direct Federal assistance for non-farm private sector disaster losses. This highly visible program is particularly vulnerable to fraud and unnecessary losses because loan transactions are expedited in order to provide quick relief to disaster victims.

Because all SBA programs have some vulnerability, either because of insufficient internal controls or dishonest program participants who seek to take advantage of the program, the OIG devotes approximately half of its budget to prevent fraud and unnecessary losses in SBA programs.

### **SBA Centralizes 7(a) Business Loan Guaranty Purchases and Liquidations Without Adequate Planning**

One of SBA's management challenges is to strengthen the loan guaranty payment (referred to as purchase) process, which is the primary tool for assessing lender compliance on a loan-by-loan basis and protecting against improper (erroneous) guaranty purchase payments. Over the years, the OIG has conducted numerous audits of the guaranty purchase process and made recommendations for improvement, including centralization of this function. As part of its transformation effort, in January 2004, SBA established the National Guaranty Purchase Center (Center) in Herndon, Virginia, to centralize the 7(a) guaranty purchase process. In FY 2003, over \$700 million in loan guaranty and liquidation actions were processed by 266 employees located at 76 district offices. As a result of centralization, SBA reduced the number of loan officers assigned to process guaranty purchase requests and liquidation activities by 83 percent (from 266 to approximately 46 authorized staff as of May 2004).

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## Significant OIG Activities

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*...additional actions were needed to strengthen the process.*

While the OIG fully supports centralization of the 7(a) business loan guaranty purchase process as a way to improve the quality and consistency of purchase decisions, we concluded that additional actions were needed to strengthen the process. A recent OIG review which was conducted, in part, because of concerns that the Center was unable to meet the demand for purchase request and liquidation actions, found that a lack of planning led to several missteps in the transformation process. The Agency did not perform the necessary analysis to determine the appropriate staffing level needed to meet demand for purchase and liquidation actions, conduct a risk assessment to identify potential weaknesses, or adequately plan for the receipt and control of loan files. As a result, the Center was understaffed when it began operations in January 2004, and could not effectively process purchase requests and liquidation actions during the first months of operations.

*...a lack of planning led to several missteps in the transformation process.*

SBA projected that each loan officer would be able to perform an average of two purchase reviews per day. Although, as of September 2004, the Center reported that it was meeting current demand for purchase decisions, SBA was not able to assess the quality of the reviews to determine if material lender errors and noncompliances were being properly identified. Based on OIG audits, reviews, and investigations conducted over the past several years, we do not believe that the Center has sufficient staff to meet demand while maintaining the quality level necessary to protect the Agency from making improper payments.

*...we do not believe that the Center has sufficient staff to meet demand while maintaining the quality level necessary...*

The OIG recommended that SBA determine the appropriate number of employees needed to perform guaranty purchase reviews and liquidation actions by (1) establishing the quality elements for purchase and liquidation actions, (2) determining the amount of time needed to complete a quality purchase and liquidation action, and (3) computing the staff levels needed to complete the estimated annual purchase and liquidation actions at an acceptable level of quality.

### **Citizenship Fraud Remains a Persistent Problem**

Investigations by the OIG and other law enforcement agencies continue to find a pattern of borrowers falsely claiming to be U.S. citizens in order to obtain SBA-guaranteed loans. (Under certain circumstances, non-citizens can legitimately obtain SBA financing.) Millions of dollars are at risk, with some individual loans at least \$1 million in size. Investigations have disclosed that borrowers and loan agents are participating in well-organized, multi-loan schemes in which misrepresentations of citizenship are made and loans default quickly. As more loans are guaranteed by SBA using expedited processing, this problem is expected to increase significantly.



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## Significant OIG Activities

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For example, during this reporting period, 12 SBA loan recipients in just one part of Texas were indicted for making false claims of U.S. citizenship in connection with loans totaling over \$7.1 million. The investigation leading to these indictments was conducted jointly with the Department of Homeland Security, a county-level organized crime task force, the Social Security Administration, and the Texas Alcoholic Beverage Commission. It was part of an ongoing effort among local, state, and Federal agencies to (1) disrupt organized criminal enterprises that coordinate similar financial violations across the U.S., and (2) identify the final destinations of monetary proceeds. Another 16 individuals were indicted or pled guilty to crimes related to citizenship fraud during this semi-annual period.

*...during this reporting period, 12 SBA loan recipients in just one part of Texas were indicted for making false claims of U.S. citizenship in connection with loans totaling over \$7.1 million.*

### Joint Effort Detects Fraud in Wake of 9/11 Tragedy

SBA's disaster assistance program provides the victims of disasters with low-interest loans. In response to the September 11, 2001, terrorist attacks on the United States, the program approved over 11,000 loans valued at over \$1 billion. As of August 2004, more than 10 percent (1,446) of these 9/11 loans, totaling over \$200 million, had defaulted. Defaulted loans are loans that are more than 60 days past due, have been charged off, or are in liquidation. Inevitably, some of these loans involved fraud because, in disaster relief, there is seldom enough time to exercise sufficient due diligence.

*As of August 2004, more than 10 percent (1,446) of these 9/11 loans had defaulted—totaling over \$200 million.*

To identify and prosecute those individuals who have taken advantage of this national tragedy, the OIG Auditing and Investigations Divisions are working together to identify indicators of fraud in a sample of defaulted 9/11 loans. These loans are then examined further by investigators and may ultimately result in criminal prosecutions and fraud convictions. A secondary purpose of this effort is to identify loan origination and servicing problems, which are referred to appropriate SBA program offices for action. Thus far, out of a judgmental sample of 125 defaulted loans, 23 of the loans (with a total value of \$11.6 million) contained possible fraud indicators and have been referred to the Investigations Division.

*...the OIG Auditing and Investigations Divisions are working together to identify indicators of fraud in a sample of defaulted 9/11 loans.*

In a case resulting from a SBA field office referral, the president and the managing partner of a business were sentenced to incarceration and ordered to pay a combined total of \$618,000 in restitution. After the terrorist attacks, they had received an SBA disaster assistance loan by falsely claiming that their company had been located at the World Trade Center. In fact, their business was not located at the World Trade Center on September 11, 2001, and the individuals were salaried employees of another company at the time.

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## Significant OIG Activities

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### Loan Agent Fraud is Likely to Increase

A loan agent is employed and compensated by an applicant or lender to prepare an SBA loan application and/or refer the applicant to a lender (or vice versa). Although honest loan agents can help small businesses gain access to capital, some have perpetrated fraudulent schemes involving hundreds of millions of dollars in loans. These fraudulent loans often default for non-payment, and SBA is forced to purchase the guaranteed portions of the loans. Because SBA currently has a limited ability to prevent and detect loan agent fraud, this is an Agency management challenge.

Three aspects of the loan agent issue are particularly troubling. First, it takes only a handful of dishonest loan agents to be involved with a large dollar amount of loans. In a multi-state area covered by just one OIG field office, from 1996 to the present, seven dishonest loan agents were involved with 260 loans totaling over \$205 million. During this reporting period, in one scheme involving at least \$28 million in loans, a loan agent pled guilty to conspiracy and fraud. He had caused prospective borrowers to sign false application documents and made it appear that the borrowers had provided the required capital injections or down payments.

*...it takes only a handful of dishonest loan agents to be involved with a large dollar amount of loans.*

*...no one knows how many loan agents are involved with SBA loans.*

A second problem is that no one knows how many loan agents are involved with SBA loans. Until the Agency fully implements a reliable electronic database containing information on loan agents, the universe of loan agents will remain unknown.

Finally, as SBA continues to centralize loan processing and liquidation, general oversight of these loans is being shifted to the lenders. As a result, the quality of oversight is likely to vary significantly, and loan agent fraud schemes are likely to increase.

### Early Defaults of 7(a) Program Loans Result in Unnecessary Losses

Prior OIG audits of early defaulted Section 7(a) business loans have shown a high incidence of noncompliance and abuse by lenders and borrowers. For example, audits have uncovered early defaults resulting from borrower misrepresentation of material facts in applying for a loan, lenders allowing loan proceeds and business assets to be used for unauthorized purposes, and lenders not properly evaluating borrower creditworthiness or repayment ability.

During this reporting period, the OIG issued 10 audit reports pertaining to early defaulted loans that were originated by four lenders. The reports identified borrowers with questionable character and delinquent Federal debt, as well as one borrower who could not legally remain in the country long enough to repay the loan. Lenders further allowed loan proceeds to be used for inappropriate purposes, such as refinancing of ineligible debts, and did not account for the use of the loan proceeds as required by SBA rules. Lenders also did not properly evaluate equity injections or verify the borrower's creditworthiness

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## Significant OIG Activities

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or repayment ability. These 10 audits of 7(a) loans that defaulted early identified improper payments of over \$2.9 million due to noncompliance with SBA requirements. The OIG recommended recovery from the lenders of \$2,934,692 in guaranty purchases that had previously been paid by SBA. For two of the reports, SBA has agreed with the recommendations to recover the funds. For the other eight reports, SBA either partially agreed with the recommendations to recover the funds, or was still reviewing the circumstances.

*...audits of 7(a) loans that defaulted early identified improper payments of over \$2.9 million due to non-compliance with SBA requirements.*

### Analysis of Industry Code Loan Data Can Assist SBA in Managing Risk of Section 7(a) Loan Program

The Office of Lender Oversight (OLO) has responsibility for monitoring Section 7(a) business loans to identify and analyze risk through lender reviews and analysis of lender and loan data. The SBA uses industry codes to classify each loan and maintains this information in its loan accounting database. Prior to March 2003, SBA did not include routine analysis of the loan portfolio by industry codes in its risk assessments. The OIG reviewed, by industry code, all loans guaranteed during the period October 1996 to June 2003 to demonstrate the value of this method of risk analysis. For example, we found that one district office and one lender were responsible for most of the charge-offs and liquidations for two industry codes, and that early defaulted loans comprised more than 45 percent of the dollars charged off for the two industry codes.

loans comprised more than 45 percent of the dollars charged off for the two industry codes. The finding demonstrates that this type of analysis can identify risk not only at the industry code level, but also at the regional, district office, and lender levels. In addition, SBA could combine the industry code analysis with other data elements to identify risk levels in specific types of loans or borrowers. Subsequent to our review, industry code analysis was incorporated in SBA's oversight activities and is now an integral part of the new loan monitoring system.

*Subsequent to our review, industry code analysis was incorporated in SBA's oversight activities and is now an integral part of the new loan monitoring system.*

### OIG Continues to Provide Substantial Resources to Counter Business Loan Fraud

*Approximately half of the OIG's FY 2005 budget request is allocated to preventing fraud and unnecessary losses in SBA programs, with business loan fraud mitigation accounting for a major portion.*

Approximately half of the OIG's FY 2005 budget request is allocated to preventing fraud and unnecessary losses in SBA programs, with business loan fraud mitigation accounting for a major portion. The workload in this area is substantial and complex, as criminals use a variety of schemes to defraud SBA loan programs. Perpetrators typically submit false and fraudulent documents such as phony invoices, claim assets that do not exist, fail to disclose other SBA loans for the same business, or misuse loan proceeds.

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## Significant OIG Activities

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As a result of a joint investigation with the FBI, four Texas men were recently indicted in connection with falsely obtaining nine SBA-guaranteed convenience store loans totaling \$9.5 million. SBA's guaranteed portion was nearly \$6.6 million. Among other things, the men allegedly recruited individuals to apply for the loans, submitted false and fraudulent documents, artificially inflated checking account deposits, and concealed the fact that down payments were funded by loan proceeds. In addition, one of the men allegedly used his position of trust as a commercial real estate escrow agent to facilitate the scheme and defraud a bank.

In California, 16 individuals and two corporations were among those recently indicted in connection with a complex scheme to falsely obtain SBA loans. Two of the individuals controlled 60 convenience stores. They used fraudulent borrowers to obtain the loans, concealed their financial interests in the businesses and the source of cash injection, and laundered each loan's proceeds. They applied for approximately \$20 million in loans, with \$8 million having been approved and disbursed. The SBA OIG continues to conduct this investigation jointly with the FBI, IRS, Immigration and Customs Enforcement, Department of Agriculture, and California's Alcohol and Beverage Control.

### Character Screening Reduces the Likelihood of Program Abuse

The SBA requires applicants for assistance to meet certain character standards before participating in programs involving business loans, disaster assistance loans, Section 8(a) certifications, surety bond guarantees, small business investment companies, and certified development companies. The OIG's Office of Security Operations ensures that program participants meet these standards by processing name checks and, where appropriate, fingerprint checks on applicants. During this semiannual period, the OIG processed a total of 1,565 external name check requests for the above programs.

The OIG also assists the Agency in making character eligibility determinations through its on-line connection with the FBI's Machine Readable Data system. The OIG refers applicants who appear to be ineligible to program officials for adjudication. During the last 6 months, OIG referrals resulted in SBA business loan program managers declining 56 applications, and disaster loan program officials declining eight applications, totaling \$19,139,000 and \$673,150, respectively. Denials of loans based on character eligibility determinations make credit available to other applicants who have no such issues. Nearly \$263 million in loans have been declined during the last 10 years due to character eligibility issues.

*Denials of loans based on character eligibility determinations make credit available to other applicants who have no such issues.*

In addition, based on OIG character eligibility information, the Section 8(a) program declined seven applications for admission to the program and the Surety Bond Guarantee Program declined two applications. The OIG also coordinates background investigations for Agency employees and certain contractor personnel. During this reporting period, the OIG initiated 79 background investigations and issued 23 security clearances. The OIG also adjudicated 76 background investigative reports and ensured that SBA's Office of Disaster Assistance adjudicated 20 derogatory background investigative reports that were forwarded to it for action. Finally, the OIG processed 3,051 internal name check requests for various Agency activities such as success stories, Small Business Person of the Year nominees, and disaster assistance new hires.

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## Significant OIG Activities

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### Fraud Awareness Briefings

As part of its mission to heighten awareness of waste, fraud, and abuse, during this reporting period, the OIG conducted six briefings for 91 SBA employees.

### OIG Emphasizes Debarments

Historically, SBA has undertaken few debarment actions. The OIG believes that it is in the public interest to debar parties from conducting business with the Federal Government that have a history of fraud or otherwise lack business integrity. In the past 6 months, the OIG has intensified its efforts in making debarment recommendations to the SBA, as well as to other Federal agencies with respect to debarments of parties participating in SBA programs. In an effort to facilitate the Agency's review of OIG-proposed debarments, the OIG prepares a detailed proposal describing why a party should be debarred, supplies pertinent evidence and documentation supporting the debarment, and prepares drafts of the initial Notices of Proposed Debarments for transmission to the party in the event the Agency agrees that debarment is appropriate.

*...it is in the public interest to debar parties from conducting business with the Federal Government that have a history of fraud or otherwise lack business integrity.*

For example, in May 2004, the OIG proposed the debarment of a previously convicted employee of a lender participating in the 7(a) loan program. In seeking to induce SBA to pay the 80 percent loan guaranty on a defaulted 7(a) loan, the employee submitted a forged authorization document purporting to have been issued by an SBA official. In response to the OIG recommendation that the employee be debarred for three years, the Agency issued a notice of proposed debarment, and is considering the party's response. A summary of OIG debarment referrals and Agency debarment actions over the past 6 months is located in the Statistical Highlights.

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## Significant OIG Activities

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### **Goal: Improve the Security Over and the Accuracy of SBA Accounting and Management Information**

The SBA depends on a complex information technology (IT) environment, which includes 38 mission critical systems running on a mix of legacy mainframe, client-server, and minicomputers. The SBA had difficulty producing reliable and timely financial and management information to support its operations, primarily because of reliance on outdated IT systems that are not integrated. The SBA is developing a new Disaster Credit Management system to modernize and improve its disaster loan-making activities. The SBA is also implementing a Lender and Loan Monitoring System to monitor its business loan portfolio. These efforts are critical to the SBA's successful future operations. However, these efforts do not impact SBA's Loan Accounting System, which is sorely outdated and in need of replacement.

The Chief Financial Officers Act of 1990 requires each Federal agency to have annual audited financial statements. A key Office of Management and Budget (OMB) initiative is to have agencies improve their financial management activities, including providing financial statements and financial performance information in a timelier manner. For the past few years, SBA's external auditor has been critical of the Agency's reporting process and its ability to provide accurate, complete, and reliable financial data. Approximately 20 percent of the OIG budget is devoted to information security and financial management work.

### **Progress Being Made but Vulnerabilities and Risks Exist in SBA's Information Systems Security Program**

The SBA has identified 38 major systems that it is dependent on in carrying out its day-to-day operations, and is implementing changes and new systems as it moves to satisfy the expectations of the President's e-gov initiative. One of SBA's most significant challenges is to improve its financial management and performance, which are affected by the Loan Accounting System (LAS). LAS, which has been in use since the 1970s, comprises approximately nine subsystems and is programmed in COmmon Business Oriented Language (COBOL) computer language. The SBA relies on LAS to account for, and report on, different aspects of its loan portfolio. The Agency incurs substantial risk relating to the continued use of LAS because the system is close to the end of its useful life and SBA faces the loss of contractor support for LAS within the next few years.

*One of SBA's most significant challenges is to improve its financial management and performance, which are affected by the Loan Accounting System...*

While SBA continues to make progress in implementing its computer security program, additional improvements are needed to achieve compliance with evolving Federal laws, regulations and related standards. Specifically, SBA needs to (1) increase emphasis on the follow-up and resolution of weaknesses and vulnerabilities identified in audits and risk assessments, (2) strengthen its control environment so managers make security of information systems, which are the cornerstone of support for their day-to-day operations, a priority, and (3) establish standard configurations for its general support computer operating systems and infrastructure components to ensure secure operations.

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## Significant OIG Activities

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*Improvements are needed in general and application controls related to financial information general support systems.*

Improvements are needed in general and application controls related to financial information general support systems. Our independent auditor's FY 2003 review of general and application controls related to SBA's financial information systems was issued during this reporting period. This audit followed guidance provided in the Government Accountability Office's (GAO) Federal Information System Controls Audit Manual (FISCAM) and concluded, as it did for FY 2002, that SBA needs to improve (1) entity-wide security program controls, (2) access controls, (3) application software development and program change controls, (4) system software controls, (5) segregation of duty controls, and (6) service continuity controls.

Audits issued during this reporting period relating to the security of general support systems for e-mail found that SBA did not follow a standard system configuration when the e-mail system was implemented. Changes to system configurations were also not made in a controlled manner. Moreover, SBA's e-mail system is vulnerable to possible security exploits that could lead to SBA's e-mail being compromised or becoming unavailable. The SBA also needs to identify the types of data that could be transmitted via e-mail, and identify the safeguards needed to more securely transmit sensitive e-mail. Due to the technical nature of the findings, these reports were issued under limited distribution.

*...SBA's e-mail system is vulnerable to possible security exploits that could lead to SBA's e-mail being compromised or becoming unavailable.*

*A recent review of SBA's Loan Application Tracking System (LATS) found problems.*

LATS is a subsystem of SBA's LAS. LATS was internally designed over 20 years ago using COBOL. LATS supports LAS by providing a data entry system for SBA's loan application tracking process. The audit of LATS identified that (1) computer desktop access to the LATS transaction screens is not secure, and (2) the Chief Financial Officer was incorrectly designated as the sole owner of the LATS. As a result, there is a risk that SBA loan data could be changed or corrupted without detection. Additionally, guarantor information protected under the Privacy Act could be viewed or disclosed without permission.

The OIG recommended establishment of a "Configuration Control Board" representing all the offices that have partial ownership of LAS to ensure that the needs of SBA's different offices are fully represented. The SBA generally agreed with this recommendation and has taken aggressive action to address some findings. As the IT front is fraught with continuing threats, continued vigilance is needed to fulfill the requirement for a secure computer environment with reduced risks to operations.

### Financial Management is a Major Challenge for SBA

Various laws and regulations place significant responsibilities on Federal financial managers to assess whether they are effectively and efficiently managing public resources. In recent years the OIG, GAO, and SBA's external auditor noted significant internal control weaknesses that resulted in the Agency being unable to produce reliable, timely, and accurate financial information, including its annual financial statements and the results of past loan asset sales. As a result, the external auditor has been unable to

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## Significant OIG Activities

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render an opinion on SBA's financial statements since FY 2000. For FY 2004, SBA has the added challenge of addressing financial management issues while accelerating their financial reporting process by 2½ months and preparing new special purpose financial statements to support the financial report of the United States.

The OIG has identified financial management as one of the Agency's top management challenges and has devoted substantial resources to SBA's annual financial statement audit to ensure a timely and thorough review of SBA's actions. This has included additional resources to provide subcontractor support to the external auditor's review of SBA's new subsidy models and subsidy cost estimates, as well as increased funding to enable the external auditor to perform additional work needed to meet accelerated reporting dates and new audit requirements.

*SBA's Administrator has made improving financial management one of the Agency's top priorities.*

SBA's Administrator has made improving financial management one of the Agency's top priorities. Steps to improve Agency financial management and reporting have focused primarily on improving the Agency's models for estimating subsidy costs, improving controls over financial statement preparation, and correcting accounting errors related to loan sales and subsidy cost allowances. FY 2004 is the first full reporting cycle with these improvements in place. While preliminary reviews indicate that significant progress has been made, SBA's actions have yet to be fully placed into operation and evaluated.

In response to the external auditor's FY 2002 finding that SBA's assurance statement on the Agency's internal controls was not consistent with the external auditor's internal control findings, in this reporting period the OIG issued an audit report on the process that SBA developed to comply with Federal Managers' Financial Integrity Act (FMFIA) requirements. Although we did not audit SBA's internal controls, we determined that SBA has not established and maintained an effective process for ensuring compliance with FMFIA's annual internal control assessment and reporting requirements. SBA management partially agreed with our findings and is taking steps to improve the critical process of evaluating and reporting on internal controls.

*...SBA has not established and maintained an effective process for ensuring compliance with FMFIA's annual internal control assessment and reporting requirements.*



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## Significant OIG Activities

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### Goal: Assist SBA in Improving its Small Business Development and Government Contracting Programs

The SBA provides assistance to existing and prospective small businesses through a variety of counseling and training services offered by Agency partner organizations. Among these are Small Business Development Centers (SBDCs), the Service Corps of Retired Executives (SCORE), and Women's Business Centers (WBCs). Through its broader Government contracting program, the SBA works with Federal agencies to establish and implement procurement goals for contracting with small, small-disadvantaged, women-owned, service-disabled veteran-owned, and historically underutilized business zone (HUBZone) small businesses. The SBA also manages the Section 8(a) Business Development program (8(a) program), which was established to provide business development assistance to small businesses owned by socially and economically disadvantaged individuals and to help them access the \$277 billion Federal procurement market. These programs demand effective and efficient management, outreach, and service delivery. Determining whether business development and Government contracting programs meet these demands depends on reliable internal and external data for effective monitoring and oversight.

#### 8(a) Program Lacks a Systematic Approach to Providing Business Development Assistance

For years the GAO and the OIG have expressed concerns about several aspects of the 8(a) program. The program has been one of the Agency's top management challenges since the inception of the OIG challenges report. The OIG is concerned that the program does not (1) place adequate emphasis on business development to enhance 8(a) firms' ability to compete, (2) adequately ensure that only 8(a) firms with economically disadvantaged owners in need of business development remain in the program, (3) promote the equitable distribution of contracting opportunities among 8(a) participants, and (4) have a database that contains the information needed to successfully manage the program.

During this reporting period, the OIG completed an audit survey that determined SBA has not established criteria for delivering and tracking 8(a) business development services. Due to the lack of guidance, individual district offices developed and delivered varying types of assistance. This unstructured strategy may have resulted in program participants not receiving the full benefits the program is intended to offer. Participants also may not have been treated equally in obtaining business development services. Because business development activities are not tracked, SBA is unable to determine whether it is fulfilling its mission as outlined in the Small Business Act, or if it is efficiently and effectively utilizing Government resources to deliver services. The SBA has now committed to issuing in-depth guidance on business development activities by June 1, 2005. Further, a new electronic annual review process—planned to debut in 2005—will implement procedures for collecting the required data.

*...SBA has not established criteria for delivering and tracking 8(a) business development services.*

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## Significant OIG Activities

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### Illegal Schemes Continue in 8(a) Program

Over the years, the 8(a) program has been subject to fraudulent—and sometimes elaborate—schemes designed to misrepresent the true status of a business. During this reporting period, the president of a

*Over the years, the 8(a) program has been subject to fraudulent—and sometimes elaborate—schemes designed to misrepresent the true status of a business.*

defunct construction company was sentenced to seven years in jail, ordered to pay nearly \$6.5 million in restitution, and assessed other penalties for defrauding the 8(a) program. The subject had improperly transferred \$495,000 from his construction business account to his personal offshore account in the Bahamas to hide money from creditors, while closing the business and abandoning its contracts and subcontractors. He also falsely represented that he had relocated his personal residence to Pennsylvania (the location of

his Section 8(a) certified business) and that he controlled the firm's day-to-day operations. Moreover, he and another individual submitted false financial statements to obtain bonding for the construction firm's bids and contracts. The president also falsely certified to the Department of Veterans Affairs (VA) that he was paying and intended to pay his subcontractors on a timely basis from the proceeds of a VA Medical Center contract. We conducted this investigation jointly with the Naval Criminal Investigative Service, VA OIG, and the Defense Criminal Investigative Service.

### Improvements Needed in Oversight of SBA-Sponsored and Co-Sponsored Activities

In order to promote and better fulfill the Agency's mission to help small businesses succeed, over time SBA has shifted the focus of the district offices—involving them more in outreach activities with public and private entities. The Small Business Act gives SBA statutory authority to sponsor solely, or in conjunction with other entities, a wide variety of training and counseling programs to assist small businesses. Events planned and conducted solely by SBA are considered SBA-sponsored events. Events planned or conducted jointly with public or private entities are considered co-sponsored events. SBA has statutory authority to accept cash and other types of gifts for use in conducting events that provide technical and managerial assistance to small businesses and for other uses in carrying out the purpose of the Small Business Act.

In September 2004, the OIG issued a summary audit report of SBA-sponsored and co-sponsored events conducted by district offices. The report summarized the results of audits done in FYs 2002 and 2003 of SBA-sponsored and co-sponsored activities of three district offices. It also included information gathered about the same type of activities of six other district offices. We found that, between May 1999 and November 2002, nine district offices conducted 49 SBA-sponsored and co-sponsored events that were not in compliance with Federal laws or SBA's policies and procedures.

*...between May 1999 and November 2002, nine district offices conducted 49 SBA-sponsored and co-sponsored events that were not in compliance with Federal laws or SBA's policies and procedures.*

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## Significant OIG Activities

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We summarized noncompliances into 19 categories. There were three especially common areas of noncompliance. First, in eight district offices, gift funds to the Federal Government were not deposited into SBA's Business Assistance Trust (BAT) Fund as required by law. Second, eight district offices collected registration and vendor fees during SBA-sponsored and not-for-profit co-sponsored events without having the appropriate authorization. Third, seven district offices solicited and accepted gift funds from parties having a business relationship with SBA without conducting conflict of interest determinations. Some of the donors were participants in SBA's lending programs who had actions pending with the district offices shortly before or after the donations.

*Some of the donors were participants in SBA's lending programs who had actions pending with the district offices shortly before or after the donations.*

Our efforts resulted in SBA (1) issuing more detailed guidance concerning outreach activities, (2) revising existing and developing new standard operating procedures for SBA-sponsored and co-sponsored activities, (3) providing training for SBA personnel, and (4) establishing the Office of Strategic Alliances to oversee all outreach activities.

Another recent co-sponsorship-related audit identified problems with the collection of program income and a procurement action by the Silicon Valley Small Business Development Center (SVSBDC). The co-sponsorship agreement executed in the San Francisco District Office documented a relationship in which SBA, in conjunction with other entities, would provide training and counseling programs to assist small businesses. Through the Entrepreneur Center (E-Center), the SVSBDC offered small businesses and entrepreneurs one facility where they could obtain assistance with their business needs. The audit concluded that (1) \$57,645 of program income for the SVSBDC was inappropriately collected, commingled with unrelated funds, and disbursed by the San Jose Service Corps of Retired Executives (SCORE) office, and (2) \$225,000 was paid for contractor services that were not acquired in accordance with established guidelines. These conditions occurred because the district office improperly implemented procedures for handling funds of the E-Center and its co-sponsors that were contrary to the SBDC Cooperative and Co-sponsorship Agreement, and influenced the sole source selection of the SVSBDC-Technical Assistance Program Director in possible violation of ethics and employee standards of conduct rules. As a result, the SVSBDC was unable to collect and use \$57,645 in program income, and authorized \$225,000 for contracted services that did not comply with the competitive procurement requirements of the co-sponsorship agreement.

*Another recent co-sponsorship-related audit identified problems with the collection program income and a procurement action by the Silicon Valley Small Business Development Center...*

### OIG Responds to Complaint Regarding a Small Business Set-Aside Contract

Under the Small Business Act, Federal agencies can enter into procurements by using "small business set-asides" (i.e., procurements reserved exclusively for small businesses). In addition, to promote an equitable Federal procurement policy, the Federal Government has established Government-wide small business goals. Currently, the goal is to provide 23 percent of the Federal Government's procurement expenditures to small businesses. SBA, as the proponent of small business, should make every effort to ensure that only eligible small businesses receive these set-asides. Further, in order to effectively

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## Significant OIG Activities

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evaluate the support the Federal Government provides to small businesses, the percentage of Government procurements going to small businesses must be accurately recorded.

The OIG conducted a review based on a complaint we received concerning the award of a small business set-aside. Prior to the audit, SBA's Office of Government Contracting reviewed a protest to this award

*...the small business recipient was ineligible to receive the set-aside because it actually supplied the product of a large business.*

and issued a size determination that, in essence, stated that the company was a small business. The OIG determined that the small business recipient was ineligible to receive the set-aside because it actually supplied the product of a large business. The product manufacturer was considered large based on its affiliation with a large business. The Agency implemented our recommendations to (1) advise the procuring agency that the contract should not be counted as a small business contract, and (2) provide guidance to SBA size determination officials to increase awareness of the need to consider affiliation issues.

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## Significant OIG Activities

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### **Goal: Assist SBA Management in Identifying and Resolving Persistent and Emerging Management Issues**

A key objective of OIG work has been to identify emerging and persistent programmatic and operational problems that may hamper SBA's ability to effectively support small business. Many of these problems have been designated as major management challenges.

#### **Top Management Challenges**

In May 1997, OIG issued a report on "Critical Management Issues Facing SBA." Since then we have responded to congressional requests and the Reports Consolidation Act of 2000 by refining these issues into reports on the most serious management challenges confronting the Agency each fiscal year. The list of challenges represents areas identified as being particularly vulnerable to fraud, waste, abuse, or mismanagement, or that otherwise pose significant risk. The challenges generally have been the subject of one or more OIG or GAO reports, have been confirmed by OIG investigations of fraud or abuse, and/or have resulted from our general knowledge of Agency management issues.

The most serious Management Challenges that faced SBA at the beginning of FY 2004 were as follows:

- SBA needs to improve its managing for results processes and performance data.
- SBA faces significant challenges in financial management and reporting which affects its ability to provide reliable, timely and accurate financial information.
- Information systems security needs improvement.
- Maximizing program performance requires that SBA fully develop, communicate, and implement a human capital management/transformation strategy.
- SBA needs better controls over the business loan purchase process.
- SBA needs to continue improving lender/participant oversight.
- The Section 8(a) Business Development program needs to be modified so that more participating companies receive access to business development and standards for determining economic disadvantage are clear and objective, so that more eligible companies receive 8(a) contracts.
- SBA needs to clarify its rules intended to deter Section 8(a) Business Development participants from passing through procurement activity to non-Section 8(a) Business Development firms.
- Preventing loan agent fraud requires additional measures.
- SBA needs to update its system of directives to provide proper guidance and control over its operations.

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## Significant OIG Activities

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For each management challenge, we provide the Agency with recommended remedial actions together with our assessment of Agency progress on each item during the preceding fiscal year. During this reporting period, at the Administrator's direction, the Agency focused more attention on the challenges by, among other things, placing them on the Management Board agenda and assigning responsibility for overseeing the Agency response to the management challenges to the Chief Operating Officer. As a result, SBA has made progress on many of the challenges, especially on the managing for results challenge. While this is encouraging, much more remains to be done. By their nature, these challenges require continued long-term commitment and effort by the Agency.

*During this reporting period, at the Administrator's direction, the Agency focused more attention on the challenges...*

For more information on the OIG's assessment of the SBA's FY 2004 Management Challenges, please review the report at <http://www.sba.gov/ig/challenges.html>.

### **Small Business Investment Company (SBIC) Program Poses Significant Risk to Taxpayer Money**

As a result of a 2003 OIG audit of the Agency's oversight of the SBIC program and the conclusions of the FY 2003 financial statement audit, in May 2004 the OIG issued a new management challenge on the SBIC program. One of the most important challenges facing SBA today is that the current structure and oversight practices of the SBIC program place too much risk on taxpayer money.

SBIC program officials have estimated that, given the rapidly mounting losses in the portfolio, the cumulative cost of the SBIC program to the Federal Government is projected to be almost \$2 billion on an outstanding portfolio of \$5 billion. The problem areas relating to program structure and oversight that we identified included (1) SBA's "profits" were not proportional to the investment that the Agency makes in SBICs, (2) insufficient incentives exist to encourage SBICs to pay back principal debt to SBA as quickly as possible, (3) SBA's policy of allowing extensive time for financially troubled SBICs to attempt rehabilitation has allowed SBIC assets to decrease, thereby reducing the potential for recovery, and (4) the vast majority of capitally impaired participating securities SBICs that have been transferred to liquidation were not being liquidated or were not being liquidated in compliance with Agency procedures. In addition, the subsidy model had underestimated the cost of the program, with the technical assumptions more optimistic than actual performance. Program officials are taking actions, including pursuing new legislation that will strengthen the assessment and management of financial and regulatory risks inherent in the SBIC program.

*...given the rapidly mounting losses in the portfolio, the cumulative cost of the SBIC program to the Federal Government is projected to be almost \$2 billion on an outstanding portfolio of \$5 billion.*

In accordance with the Reports Consolidation Act of 2000, this challenge is being incorporated with other Agency challenges in our Report on the Most Serious Management Challenges Facing the Small Business Administration in FY 2005. The complete FY 2005 report will be included in SBA's annual Performance and Accountability Report this fall.

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## Significant OIG Activities

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### Other Significant Management Issues

#### OIG Promotes Improved Management Through Reviews of Agency Proposals

The OIG plays an important role in assisting SBA in identifying and resolving emerging management issues through reviews of proposed legislation and regulations affecting SBA, as well as internal standard operating procedures (SOPs), agency procedural and policy notices, and other internal agency documents. From March 1, 2004, through September 30, 2004, the OIG reviewed approximately 95 proposed legislative and regulatory changes and approximately 56 internal SBA SOPs, notices, and other documents. The OIG provided comments and was able to obtain changes on many of these items, thereby improving the Agency's ability to deter waste, fraud, and abuse in its programs.

For example, both the GAO and the OIG have expressed concerns in the past about the lack of independence of the Office of Lender Oversight (OLO) from the Office of Capital Access (OCA). Due to the fact that OCA's mission, in part, is to promote SBA business loans, the GAO and OIG believed that OCA may have a conflict of interest that could prevent OLO from effectively performing its lender oversight functions. The OIG raised a number of concerns in response to an Agency proposal to restructure OLO's responsibilities. As a result, the OIG was able to obtain agreement from the Agency to make several fundamental revisions in the proposed restructuring of OLO functions to promote independence, including giving greater authority to an Agency committee to oversee OLO.

*The OIG was able to obtain agreement from the Agency to make several fundamental revisions in the proposed restructuring of OLO functions...*

#### Decrease in Reports with Overdue Management Decisions

Management decisions on OIG recommendations take several forms. Program officials may agree to a recommendation as presented by the OIG, seek to negotiate a compromise agreement with the OIG, or disagree with the recommendation. The IG Act requires that Federal agencies make management decisions on all findings and recommendations within a maximum of 6 months of report issuance. As of September 30, 2004, management decisions on 18 OIG reports were overdue (See Appendix V). This is a decrease from the 21 reports with overdue management decisions mentioned in the previous semiannual period. We are optimistic that this trend will continue as we work with the Agency to resolve these issues.

*As of September 30, 2004, management decisions on 18 OIG reports were overdue...*

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## Significant OIG Activities

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### **Goal: Strengthen our ability to identify and have maximum impact on the most significant SBA issues**

To successfully implement our strategic goals, the OIG must ensure the efficiency and effectiveness of our internal operations. The OIG must manage its human capital, and other resource allocation processes to maximize the impact of our efforts to improve Agency programs and operations. Moreover, we must be quick to respond to the changes currently taking place in SBA.

### **OIG Auditors Are Assigned to National Guaranty Purchase Center**

In January 2004, SBA centralized the Section 7(a) business loan guaranty purchase and liquidation processes at the National Guaranty Purchase Center (Center). The purpose of this action was to improve the quality and consistency of guaranty purchase decisions and liquidation actions and reduce the number of employees that perform these tasks. The action to centralize this function responds to the OIG management challenge on guaranty purchases. In May 2004, four auditors from the OIG Credit Programs Group were assigned to the Center to perform audits of the guaranteed loan program and provide oversight.

The OIG has conducted numerous audits of the 7(a) loan program throughout the years and made many recommendations to improve the process, including centralization. Before the Center was established, the auditors had to either travel to the district offices to review the loan files or arrange to have the files sent to the auditors' location. This not only delayed the audit process but, in some cases, placed a burden on the district offices when active loan files were requested for audit. With the centralization of the purchase process and the assignment of several OIG auditors to the Center, access to loan files should be easier, quicker, and less disruptive to the Agency.

*With the centralization of the purchase process and the assignment of several OIG auditors to the Center, access to loan files should be easier, quicker, and less disruptive to the Agency.*

During the last 6 months, the OIG completed a major review of the transfer of operations from the district offices to the Center and initiated a follow up audit on the guaranty purchase process. For a discussion of the audit, see the first goal in this Semiannual Report.

### **OIG Issues SOP on Telework Policy**

Section 359 of the FY 2001 Department of Transportation and Related Agencies Appropriations Act, Public Law 106-346, states, "Each executive agency shall establish a policy under which eligible employees of the agency may participate in telecommuting to the maximum extent possible without diminishing employee performance." Although SBA has a Telecommuting SOP in place, the OIG believed it was important to issue its own telework policy.



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## Significant OIG Activities

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There are many beneficial aspects to the OIG's Teleworking policy—both direct and indirect. Direct benefits to the OIG include: a reduction in payments for commuter benefits; a built-in incentive for recruitment and retention of high-caliber candidates; flexibilities to provide for employees with short-term or long-term health conditions; and improved work quality, productivity, and effectiveness. Important indirect benefits to the OIG include improved employee morale and communication between employee and supervisor. The benefits to employees are equally important—less cost and time commuting.

*Important indirect benefits to the OIG include improved employee morale and communication between employee and supervisor.*

# Statistical Highlights

## FY 2004 6-Month Productivity Statistics April 1, 2004, through September 30, 2004

<b>Office-wide Dollar Accomplishments</b>	<b>Totals</b>
A. Potential Investigative Recoveries and Fines.....	\$11,751,411
B. Loans Not Made as Result of Investigations and Name Checks.....	\$21,831,550
C. Disallowed Costs Agreed to by Management .....	\$2,244,110
D. Recommendations that Funds Be Put to Better Use Agreed to by Management.....	<u>\$300,069</u>
<b>Total .....</b>	<b><u>\$36,127,140</u></b>
 <b>Efficiency and Effectiveness Activities</b>	
A. Reports Issued .....	27
B. Recommendations Issued.....	140
C. Dollar Value of Costs Questioned.....	\$3,114,730
D. Dollar Value of Recommendations that Funds Be Put to Better Use.....	\$671,380
E. Collections as a Result of Questioned Costs .....	\$24,000*
 <b>Follow-up Activities</b>	
A. Recommendations Closed.....	151
B. Disallowed Costs Agreed to by Management .....	\$2, 244,110
C. Dollar Value of Recommendations that Funds Be Put to Better Use Agreed to by Management.....	\$300,069
D. Unresolved Recommendations.....	173
 <b>Legislation/Regulations/Standard Operating Procedures (SOPs)/Other Reviews</b>	
A. Legislation Reviewed.....	89
B. Regulations Reviewed.....	6
C. Standard Operating Procedures Reviewed .....	11
D. Other Issuances Reviewed** .....	45

\*To be collected in installments.

\*\*This category includes policy notices, procedural notices, Administrator's action memoranda, and other communications, which frequently involve the implementation of new programs and policies.

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## Statistical Highlights

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### Summary of Indictments, Convictions, and Case Activity

A. Indictments from OIG Cases.....	58*
B. Convictions from OIG Cases .....	17
C. Cases Opened .....	59
D. Cases Closed .....	65

\*Includes eight indictments that occurred in the last Semiannual reporting period but were not reported.

### Summary of Recoveries and Management Avoidances

A. Potential Recoveries and Fines as a Result of OIG Investigations.....	\$11,751,411
B. Loans/Contracts Not Approved as a Result of OIG Investigations.....	\$2,019,400
C. Loans/Contracts Not Approved as a Result of the Name Check Program .....	<u>\$19,812,150</u>
<b>Total .....</b>	<b><u>\$33,582,961</u></b>

### SBA Personnel Actions Taken as a Result of Investigations

A. Dismissals .....	0
B. Resignations/Retirements .....	2
C. Suspensions .....	1
D. Reprimands .....	0
E. Other .....	1

### Program Actions Taken as a Result of Investigations

A. Debarments Recommended to the Agency .....	4
B. Debarments pending at the Agency.....	4
C. Proposed Debarments issued by the Agency .....	1
D. Final Debarments issued by the Agency .....	0

### Summary of OIG Hotline Operation

A. Total Fraud Line Calls/Letters .....	112
B. Total Calls/Letters Referred to Investigations Division .....	26
C. Total Calls/Letters Referred to SBA or Other Federal Agencies .....	72
D. Total Calls/Letters Needing No Action.....	14

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# Statistical Highlights

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## FY 2004 Full Year Productivity Statistics October 1, 2003, through September 30, 2004

### Office-wide Dollar Accomplishments

A. Potential Investigative Recoveries and Fines.....	\$17,887,395
B. Loans Not Made as Result of Investigations and Name Checks.....	\$35,367,934
C. Disallowed Costs Agreed to by Management .....	\$3,255,810
D. Recommendations that Funds Be Put to Better Use Agreed to by Management.....	<u>\$835,539</u>
<b>Total .....</b>	<u><b>\$57,346,678</b></u>

### Efficiency and Effectiveness Activities

A. Reports Issued .....	45
B. Recommendations Issued.....	261
C. Dollar Value of Costs Questioned.....	\$7,724,603
D. Dollar Value of Recommendations that Funds Be Put to Better Use.....	\$678,380
E. Collections as a Result of Questioned Costs .....	\$1,422,692

### Follow-up Activities

A. Recommendations Closed.....	201
B. Disallowed Costs Agreed to by Management .....	\$3,255,810
C. Dollar Value of Recommendations that Funds Be Put to Better Use Agreed to by Management.....	\$835,539
D. Unresolved Recommendations.....	366

### Legislation/Regulations/Standard Operating Procedures (SOPs)/Other Reviews

A. Legislation Reviewed.....	131
B. Regulations Reviewed.....	17
C. Standard Operating Procedures Reviewed .....	21
D. Other Issuances Reviewed* .....	54

\*This category includes policy notices, procedural notices, Administrator's action memoranda, and other communications, which frequently involve the implementation of new programs and policies.

# Statistical Highlights

## Summary of Indictments, Convictions, and Case Activity

A. Indictments from OIG Cases.....	75
B. Convictions from OIG Cases .....	30
C. Cases opened .....	109
D. Cases closed .....	127

## Summary of Recoveries and Management Avoidances

A. Potential Recoveries and Fines as a Result of OIG Investigations .....	\$17,887,395
B. Loans/Contracts Not Approved as a Result of OIG Investigations.....	\$5,031,292
C. Loans/Contracts Not Approved as a Result of the Name Check Program .....	<u>\$30,336,642</u>
<b>Total .....</b>	<b><u>\$53,255,329</u></b>

## SBA Personnel Actions Taken as a Result of Investigations

A. Dismissals .....	0
B. Resignations/Retirements.....	3
C. Suspensions .....	1
D. Reprimands .....	0
E. Other .....	1

## Program Actions Taken as a Result of Investigations

A. Debarments Recommended to the Agency .....	4
B. Debarments pending at the Agency.....	4
C. Proposed Debarments issued by the Agency .....	1
D. Final Debarments issued by the Agency.....	0

## Summary of OIG Hotline Operation

A. Total Fraud Line Calls/Letters .....	308*
B. Total Calls/Letters Referred to Investigations Division.....	45
C. Total Calls/Letters Referred to SBA or Other Federal Agencies .....	135
D. Total Calls/Letters Needing No Action.....	128

\*Total no longer includes hang-ups.

# Appendix

## Appendix I OIG Reports Issued April 1, 2004, through September 30, 2004

Title	Report Number	Issue Date	Questioned Costs	Funds for Better Use
<i><b>Capital Access</b></i>				
The SBIC Program: At Significant Risk for Losses	4-21	5/24/2004		
Audit of SBA Guarantied Loan	4-25	6/22/2004	\$177,166.00	
Audit of an Early Defaulted Loan	4-26	6/22/2004		\$235,008.00
Audit of SBA Guarantied Loan	4-28	7/9/2004		\$142,549.00
Audit of an Early Defaulted Loan	4-29	7/12/2004	\$373,760.00	
Audit of SBA Guarantied Loan	4-32	7/29/2004	\$542,663.00	
Audit of SBA Guarantied Loan	4-33	7/30/2004	\$362,207.00	
Audit of an Early Defaulted Loan	4-36	8/10/2004	\$740,000.00	
Memorandum Report – Survey of Risk Management by Industry Code	4-37	8/11/2004		
Audit of SBA Guarantied Loan	4-38	8/24/2004	\$83,576.00	
Management Advisory Report on the Transfer of Operations to the National Guaranty Purchase Center	4-39	8/31/2004		
Audit of SBA Guarantied Loan	4-40	9/13/2004	\$246,460.00	
Audit of an Early Defaulted Loan	4-43	9/17/2004		\$293,823.00
<b>Program Subtotal</b>	13 Reports		\$2,525,832.00	\$671,380.00
<i><b>Agency Management</b></i>				
Audit of SBA's Loan Application Tracking System	4-18	4/5/2004		
Audit of SBA's Information Systems Controls Fiscal Year 2003	4-19	4/29/2004		
Single Audit of Federal Financial Assistance Programs Service Corps of Retired Executives (SCORE)	4-30	7/13/2004		
Audit of SBA's Process for Complying with the Federal Managers' Financial Integrity Act Reporting Requirements	4-34	7/29/2004		
Single Audit of Federal Financial Assistance Programs Bronx Museum of the Arts	4-35	8/3/2004	\$256,407.00	
Audit of Selected SBA computer General Support Systems	4-41	9/10/2004		
Audit of SBA's Email System	4-42	9/10/2004		
Single Audit of the University of the Virgin Islands	4-23	6/15/2004		
Single Audit of Federal Financial Assistance Programs Greenpoint Manufacturing and Design Center	4-24	6/15/2004	\$331,489.00	
<b>Program Subtotal</b>	9 Reports		\$587,896.00	
<i><b>Government Contracting and Business Development</b></i>				
Audit Report of Small Business Set-Aside Contract to Measurement Instruments	4-20	5/18/2004		
Business Development provided by SBA's 8(a) Development Program	4-22	6/2/2004		
Audit of San Francisco District Office Administrative Activities Related to the Silicon Valley Small Business Development Center	4-27	6/29/2004		

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# Appendix

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**Appendix I (cont.)  
OIG Reports Issued  
April 1, 2004, through September 30, 2004**

<b>Title</b>	<b>Report Number</b>	<b>Issue Date</b>	<b>Questioned Costs</b>	<b>Funds for Better Use</b>
Audit of Expenses for Meals and Refreshments Incurred by the Latino Coalition Foundation on SBA 7(j) Cooperative Agreement	4-31	7/19/2004	\$1,001.80	
Audit Report – Summary Audit of SBA-Sponsored and Cosponsored Events Conducted by District Offices	4-44	9/24/2004		
<b>Program Subtotal</b>	5 Reports		\$1,001.80	\$0
<b>TOTALS (all programs)</b>	<b>27 Reports</b>		<b>\$3,114,729.80</b>	<b>\$671,380.00</b>

# Appendix

## Appendix II OIG Reports with Questioned Costs

		Reports	Recs*	Questioned Costs**	Unsupported Costs**
A.	For which no management decision had been made by March 31, 2004	8	17	\$6,339,311.10	\$2,557,231.00
B.	Which were issued during the period	10	11	\$3,114,729.80	\$0
	<b>Subtotals (A + B)</b>	18	28	\$9,454,040.90	\$2,557,231.00
C.	For which a management decision was made during the reporting period	6	6	\$3,368,410.00	\$376,106.00
	(i) Disallowed costs	3	3	\$2,244,110.00	\$376,106.00
	(ii) Costs not disallowed	3	3	\$1,124,300.00	\$0
D.	For which no management decision had been made by September 30, 2004	12	22	\$6,085,630.90	\$2,181,125.00

\* Recommendations: reports may have more than one recommendation.

\*\* Questioned costs are those which are found to be improper, whereas unsupported costs may be proper but lack documentation.

## Appendix III OIG Reports with Recommendations that Funds Be Put to Better Use

		Reports	Recs*	Recommended Funds For Better Use
A.	For which no management decision had been made by March 31, 2004	4	4	\$833,250.00
B.	Which were issued during the period	3	3	\$671,380.00
	<b>Subtotals (A + B)</b>	7	7	\$1,504,630.00
C.	For which a management decision was made during the reporting period	2	2	\$300,069.00
	(i) Recommendations agreed to by SBA management	0	0	\$0
	(ii) Recommendations not agreed to by SBA management	2	2	\$300,069.00
D.	For which no management decision had been made by September 30, 2004	5	5	\$1,204,561.00

\* Recommendations; reports may have more than one recommendation.



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# Appendix

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## Appendix IV OIG Reports with Non-Monetary Recommendations

		Reports	Recommendations
A.	For which no management decision had been made by March 31, 2004	27	163
B.	Which were issued during the period	14	126
	<b>Subtotals (A + B)</b>	41	289
C.	For which a management decision was made (for at least one recommendation in the report) during the reporting period	24	143
D.	For which no management decision (for at least one recommendation in the report) had been made by September 30, 2004	31*	146

\*Adding the number of reports for C&D will not result in the subtotal of A&B because any single report may have recommendations that fall under both C&D.

# Appendix

## Appendix V OIG Reports From Prior Semiannual Periods with Overdue Management Decisions as of September 30, 2004

<b>Title</b>	<b>Number</b>	<b>Issued</b>	<b>Status</b>
Georgia District Office Sponsorship Activities	2-25	8/26/02	Awaiting final action by management for recommendation 1.A.
Impact of Loan Splitting on Borrowers and SBA	2-31	9/30/02	Awaiting management decision on two recommendations.
Eligibility of 15 HUBZone Companies and a Review of the HUBZone Empowerment Contracting Program's Internal Controls	3-05	1/22/03	Awaiting management decision on outstanding recommendation; expected by 10/31/04.
Guaranty Purchase Process	3-15	3/17/03	Awaiting management decision on recommendation 1.A.
Asset Sales Program	3-19	3/31/03	Recommendations are in management resolution process.
SBA's Information System Controls for FY 2002	3-20	3/31/03	Awaiting management decisions on one outstanding recommendation; expected by 11/30/04.
Equity Injection in the SBA 7(a) Loan Guaranty Program	3-21	3/31/03	Three recommendations are in management resolution.
The Microloan Program: Moving Toward Performance Management (Inspection)	3-26	5/13/03	Two recommendations are in management resolution.
Early Defaulted Loan to 2B Systems, Inc.	3-30	6/19/03	One recommendation in management resolution.
SBA's Acquisition, Development and Implementation of the Joint Accounting and Administrative Management System	3-32	6/20/03	Awaiting management decision on two outstanding recommendations; expected by 11/30/04.
SBIC Oversight	3-33	7/1/03	One recommendation in management resolution.
Audit of the National Women's Advisory Council	3-35	7/28/03	Awaiting management decision on one outstanding recommendation; eight recommendations are in management resolution.
Insufficient Proof of Citizenship Status for SBA Loans (Inspection)	3-43	9/30/03	Awaiting management decision on one outstanding recommendation.
SBA's Federal and State Technology Partnership (FAST) Program	4-05	12/30/03	Awaiting management decision on outstanding recommendations; expected by 10/31/04.
Puerto Rico & US Virgin Island DO Cosponsorship and SBA-Sponsored Activities	4-07	1/20/04	Awaiting management decision.
Enforcement of SBA's IT Enterprise Architecture During the Development of the Disaster Credit Management System	4-14	3/2/04	Awaiting management decision on one outstanding recommendation.
SBA's Administration of the Procurement Activities of Asset Sale Due Diligence Contracts and Task Orders	4-16	3/17/04	Awaiting management decision on outstanding recommendations; expected by 10/31/04.
SBA's FY 2003 Financial Statements – Management Letter	4-17	3/23/04	One recommendation in management resolution.

# Appendix

## Appendix VI OIG Reports Without Final Action as of September 30, 2004

Report Number	Title	Date Issued	Date of Management Decision	Final Action Target
43H006021	8(a) Continuing Eligibility Reviews	9/30/94	10/30/94	10/30/02
87H002017	NOAA Computer Workstation Contracts	6/18/98	3/01/99	3/31/02
9-23	Survey of Electronic Records Management	9/15/99	11/30/99	9/30/05
0-14	7(a) Service Fee Collections	3/30/00	8/22/00	9/30/03
0-19	SDB Certification Program Obligations and Expenditures	6/30/00	3/30/01	9/30/02
0-30	SBA's Administration of MBELEDF Cosponsorship	9/30/00	3/26/01	**
0-31	Boscart Construction, Inc.	9/30/00	2/26/01	10/22/04
1-09	PDD 63	3/26/01	9/27/01	9/15/03
1-11	GPRA for the MSB&COD Program	3/27/01	9/28/01	7/31/03
1-12	SBA's Information Systems Controls – FY 2000	3/27/01	***	**
1-16	SBA's Follow-up on SBLC Examinations	8/17/01	9/25/01	12/31/03
1-19	PLP Oversight Process	9/27/01	8/27/02	12/31/03
A1-06	Evaluation of SBA's Computer Security Program	9/28/01	1/9/02	**
1-20	Agreed-Upon Procedures Report on Sensitive Payments	9/28/01	12/18/01	11/30/03
2-12	Improvements in the SBLC Oversight Process	3/20/02	8/27/02	**
2-17	SBA's FY 2001 Financial Statements – Management Letter	4/12/02	***	**
2-18	SBA's Information Systems Controls FY 2001	5/6/02	***	**
2-22	Travel of SBA's Former Region VI Regional Administrator	8/7/02	9/26/02	**
2-27	SBA's Experience with Defaulted Franchise Loans	9/16/02	12/19/02	6/30/03
2-29	Internal Control Over Colson Services Corporation's Contract as Central Servicing Agent for SBA's CDC Program	9/16/02	12/12/02	6/30/05
2-31	Impact of Loan Splitting on Borrowers and SBA	9/30/02	7/12/04	10/9/04
2-34	SBA's Controls over the Access, Disclosure and Use of Social Security Numbers by Third Parties	9/30/02	7/23/03	9/15/03
3-02	Performance Measurement in the Federal and State Technology (FAST) Program	1/3/003	9/30/03	12/1/03
3-05	Eligibility of 15 HUBZone Companies and a Review of the HUBZone Empowerment Program's Internal Controls	1/22/03	7/10/03	7/21/03
3-08	SBA's Oversight of the Fiscal Transfer Agent for the 7(a) Loan Program	1/30/03	***	**
3-10	504 Loan Program Oversight	2/6/03	10/1/03	12/31/03
3-13	Economic Injury Disaster Loans	3/14/03	***	**
3-14	TEP Consulting, Inc.	3/14/03	4/10/03	12/31/03

# Appendix

## Appendix VI (cont.) OIG Reports Without Final Action as of September 30, 2004

Report Number	Title	Date Issued	Date of Management Decision	Final Action Target
3-18	Grants to the Texas Center for Women's Business Enterprise	3/20/03	6/04/03	10/15/03
3-20	SBA's Information System Controls for FY 2002	3/31/03	***	**
3-21	Equity Injection in the SBA 7(a) Loan Guaranty Program	3/31/03	5/27/04	12/30/04
3-23	Service Corps of Retired Executives Program	4/11/03	9/30/03	6/30/04
3-24	SBA's FY 2002 Financial Statements – Management Letter	4/14/03	***	**
3-26	Microloan Program: Moving Toward Performance Management	5/13/03	8/28/03	**
3-32	SBA's Acquisition, Development and Implementation of the Joint Accounting and Administrative Management System	6/30/03	***	**
3-33	SBIC Oversight	7/1/03	10/6/03	**
3-34	SBA's Compliance with JFMIP Property Management System Requirements	7/23/03	9/11/03	**
3-35	National Women's Business Council	7/28/03	9/11/03	**
3-36	Audit of an Early Defaulted Loan	8/19/03	10/1/03	9/30/04
3-39	Monitoring of SBA's Implementation of the Disaster Credit Management System	9/24/03	12/11/03	**
3-41	SBA Guaranteed Loan to Concrete Transport, Inc.	9/29/03	4/22/04	8/31/04
3-42	Travel Card and Purchase Card Controls	9/29/03	6/17/04	12/30/04
4-02	Early Defaulted Loan to Flower Mound Conoco	11/24/03	8/10/04	11/30/04
4-09	Review of SBA Purchase Cards	1/26/04	8/24/04	12/31/04
4-10	SBA's FY 2003 Financial Statements	1/30/04	7/16/04	**
4-13	Early Defaulted Loan to Ocumed Group, Inc.	3/2/04	4/6/04	10/31/04
4-14	Enforcement of SBA's IT Enterprise Architecture During the Development of the Disaster Credit Management System	3/2/04	7/12/04	8/31/04
4-15	SACS/MEDCOR: Ineffective and Inefficient	3/9/04	5/11/04	9/30/05
4-16	SBA's Administration of the Procurement Activities of Asset Sale Due Diligence Contracts and Task Orders	3/17/04	5/12/04	**
4-17	SBA's FY 2003 Financial Statements – Management Letter	3/23/04	5/14/04	**
4-18	SBA's Loan Application Tracking System	4/5/04	***	**
4-19	SBA's Information Systems Controls FY 2003	4/29/04	***	**
4-22	Business Development Provided by the 8(a) Business Development Program	6/2/04	7/14/04	**

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# Appendix

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## Appendix VI (cont.) OIG Reports Without Final Action as of September 30, 2004

<b>Report Number</b>	<b>Title</b>	<b>Date Issued</b>	<b>Date of Management Decision</b>	<b>Final Action Target</b>
4-25	SBA Guarantied Loan	6/22/04	7/1/04	12/31/04
4-26	Early Defaulted to Northwest Conoco	6/22/04	7/1/04	12/31/04
4-34	SBA's Process for Complying with the FMFIA Reporting Requirements	7/29/04	9/9/04	**

\*\* Target dates vary with different recommendations.

\*\*\* Management decision dates vary with different recommendations

# Appendix

## Appendix VII Significant Recommendations From Prior Semiannual Reporting Periods Without Final Action as of September 30, 2004\*

Report Number	Date Issued	Recommendation	Management Decision Date	Final Action Target
43H006021	9/30/94	Establish procedures for determining whether Section 8(a) participants should no longer be considered economically disadvantaged based on their ownership interest in their 8(a) firm, the equity and market value of their primary residence, and the net worth of their spouses.	12/21/01	10/30/02
98-03-01	3/31/98	Establish a loan agent monitoring system.	7/21/98	9/30/99
87H002017	6/18/98	Provide definitive guidance and definitions to evaluate the manufacturing criteria shown in regulations.	11/19/01	3/31/03
1-11	3/27/01	Ensure that performance plans include indicators for determining how effectively and efficiently the Section 8(a) program is operating.	9/28/01	7/31/03
1-19	9/27/01	Revise the scoring for the annual review process to ensure the volume and weighting of point values of other questions does not offset low scores for eligibility and credit quality.	3/27/02	12/31/03
2-12	3/20/02	Develop a formal policy regarding effective supervisory and enforcement actions.	8/27/02	12/31/03
2-18	5/6/02	Develop an Agency-wide security plan to establish and implement the policies, procedures and practices for the following: (1) full integration of the information security approach and implementation process; (2) coordination among program offices to support their security needs; (3) guidance to the program office to implement information system security controls; and (4) methods to monitor the effectiveness of each part of information technology security.	6/28/02	11/17/03
3-08	1/30/03	Initiate a new procurement action for fiscal and transfer agent (FTA) activities and terminate the existing contract with the FTA when a new contract can be enacted.	12/10/03	3/31/06
3-08	1/30/03	Review FTA activities and identify contract costs for fees and services. Report these contract costs in proposed Master Reserve Fund (MRF) financial statements so future FTA contracts will have historical cost data for comparison purposes.	10/15/03	11/17/03
3-10	2/6/03	Design a review guide to incorporate performance aspects to address financial risk, address the specific requirements of the Section 504 loan program, and incorporate a performance-driven scoring system.	10/01/03	12/31/03
3-26	5/13/03	Develop a comprehensive Microloan Program SOP and a systematic approach to disseminate guidance.	8/28/03	12/31/04

\*These are a subset of the universe of recommendations without final actions.

## Appendix

### Appendix VII (cont.) Significant Recommendations From Prior Semiannual Reporting Periods Without Final Action as of March 31, 2004\*

Report Number	Date Issued	Recommendation	Management Decision Date	Final Action Target
3-33	7/1/03	Revise SOP on Small Business Investment Companies (SBICs) to ensure it includes requirements to perform quarterly risk assessments for capitally impaired SBICs, include an analysis of potential for repayment of outstanding leverage, and determine what criteria should be used to recommend an SBIC be transferred to liquidation.	10/6/03	12/28/03
3-35	7/28/03	That NWBC Executive Director require FEW to provide justification for receiving \$579,368 from the Silicon Valley I and II, New England, New York and Mid-West Forums base on estimated expenses incurred. After reviewing the justification, determine whether any income in excess of expenses should be recovered. If a determination to seek recovery is made, ensure that the CFO recovers the funds from the responsible party or parties.	9/3/03	6/30/04
3-36	8/19/03	Seek recovery of \$282,447 from First International Bank, less any subsequent recoveries, for loan number 343 767 4004.	10/1/03	9/30/04
3-39	9/24/03	That the Chief Information Officer formulate a strategy to provide for more proactive project oversight and system planning efforts to ensure that the SDM is followed by SBA sponsoring offices for large-scale systems development projects.	12/11/03	12/31/04
3-41	9/29/03	Require the lender to repay SBA \$273,675 for loan number 153-313-4007.	4/22/04	8/31/04
4-02	11/24/03	Seek recovery of \$376,106 plus interest and fees from the lender for loan number 375-199-4004.	8/10/04	11/30/04
4-10	1/30/04	That the Chief Financial Officer develop a comprehensive SOP detailing the subsidy reestimate process, including related internal controls, that reflects SBA's current reestimate preparation processes and any proposed improvements. The new SOP should be updated at least annually to capture significant changes such that it reflects the current operating process.	7/16/04	3/31/05
4-10	1/30/04	That the Administrator, in conjunction with the CFO, assess whether SBA has developed sufficient and qualified resources to adequately address its current financial reporting shortcomings and determine if the current process is in need of re-engineering, to meet accelerated financial reporting deadlines in future years.	7/16/04	8/20/04

# Appendix

## Appendix VII (cont.) Significant Recommendations From Prior Semiannual Reporting Periods Without Final Action as of March 31, 2004\*

Report Number	Date Issued	Recommendation	Management Decision Date	Final Action Target
4-13	3/2/04	Request the District Director to seek recovery from the lender of principal, interest, and expenses totaling \$767,049 paid to First International Bank for Loan number 381-867-4008.	7/12/04	10/31/04
4-16	3/17/04	That the Associate Deputy Administrator for Management and Administration seek recovery of at least \$1,690,838 for amounts overcharged by referring the overcharging matter to the GSA contracting officer for FSS 621-3 (now 520-3) for appropriate action.	5/12/04	12/31/04
4-17	3/23/04	That the CFO develop a methodology, utilizing representative samples if necessary, to verify the completeness and accuracy of performance measure data reported by program offices.	5/14/04	10/22/04
4-17	3/23/04	That the CFO implement procedures to ensure timely and accurate reporting and reconciliation of intragovernmental amounts. These procedures should include establishing timelines for resolving differences with non-fiduciary trading partners, as well as quality assurance reviews to ensure the accuracy of both amounts confirmed and amounts reported.	5/14/04	11/30/04

\*These are a subset of the universe of recommendations without final actions.



# Appendix

## Appendix VIII 6-Month Significant Recommendations Summary\* as of September 30, 2004

Report Number	Title	Date Issued	Recommendation
4-18	Audit of SBA's Loan Application Tracking System	4/5/2004	That the Chief Information Officer identify and require all SBA program offices with partial ownership of LAS and its subsystems to properly accredit or authorize the LAS for production for the next system accreditation.
4-19	Audit of SBA's Information Systems Controls Fiscal Year 2003	4/29/2004	That the SBA Administrator ensure that sufficient resources are provided to enable OCIO to meet its responsibilities under the Clinger Cohen Act, FISMA, and OMB Circulars A-50, A-127, and A-130.
4-19	Audit of SBA's Information Systems Controls Fiscal Year 2003	4/29/2004	That the Chief Information Officer revise and enhance existing policies and procedures to ensure: control weaknesses identified in certification and accreditation reviews and audit reports are resolved in a timely manner and ensure senior management is provided timely information regarding the progress towards implementing corrective actions; OCIO monitoring controls are effective to preclude reoccurrence of previously noted weaknesses; technical personnel are provided technical training to enable personnel to successfully carry out their duties and responsibilities; that technical skills are sufficient to meet new technical requirements prior to implementing new hardware and software; and OCIO effectively participates in all phases of system development in a timely manner so that system controls are properly designed and developed to provide adequate security, and reliability, completeness, and accuracy for all significant system initiatives both within and outside of OCIO.
4-19	Audit of SBA's Information Systems Controls Fiscal Year 2003	4/29/2004	That the Chief Information Officer, in conjunction with system owners: develop policies and procedures to require system owners to provide plans of action to OCIO for correcting weaknesses identified from audits, management reviews, and certification and accreditation reviews; ensure that plans adequately address management actions to resolve or minimize weaknesses in the short term while implementing longer term system corrective actions; develop reporting processes to follow-up on system owner corrective action plans; and ensure that sufficient resources are made available to monitor system owner corrective action plans.

\*The OIG has not included some significant recommendations from limited distribution reports because of their sensitive nature.

# Appendix

## Appendix VIII (cont.) 6-Month Significant Recommendations Summary as of September 30, 2004

Report Number	Title	Date Issued	Recommendation
4-19	Audit of SBA's Information Systems Controls Fiscal Year 2003	4/29/2004	That the Chief Information Officer: implement procedures to ensure compliance with Procedural Notice 9000-1406 "Removal of Old Computer User Accounts;" require network security administrators to review all current network accounts to identify and eliminate unnecessary accounts and require periodic documented reviews of all generic network accounts to ensure that they are authorized and needed; provide resources sufficient to monitor and assess network administration activities to ensure compliance with federal laws and regulations, SBA policies and procedures, National Institute of Standards and Technology guidance, and industry best practices; and in coordination with program directors, develop procedures for controlling contractor personnel access to the network and applications. Procedures should also be established to: require Contracting Officers' Technical Representatives (COTRs) to notify security administrators in writing of each contractor personnel needing a network and application account along with privileges to assign to the account; and require all network and application accounts established for contractor personnel to be established with a renewal or termination date not to exceed one year or the length of the contract, whichever is less. In coordination with the Office of Human Capital Management, procedures should be developed for network and application security administrators to receive notification of termination of SBA employees.
4-19	Audit of SBA's Information Systems Controls Fiscal Year 2003	4/29/2004	That the Chief Financial Officer instruct the Director of Denver Finance Center to establish adequate physical security for routers by either moving routers to a restricted area where access is limited to only authorized individuals, such as the server room, or develop compensating controls, such as constructing a security cage.

# Appendix

## Appendix VIII (cont.) 6-Month Significant Recommendations Summary as of September 30, 2004

Report Number	Title	Date Issued	Recommendation
4-19	Audit of SBA's Information Systems Controls Fiscal Year 2003	4/29/2004	That the Chief Information Officer: reduce the number of network accounts assigned "Domain Admin" privileges to only those individuals with a specific need within Network Integration Branch; create new network accounts for non-headquarter network administrators with limited domain administrative privileges to add and delete users and add, delete, and modify objects within office Organization Units; and develop and implement procedures to perform periodic reviews of highly-privileged accounts to assess the continuing need for accounts and privileges.
4-19	Audit of SBA's Information Systems Controls Fiscal Year 2003	4/29/2004	That the Chief Information Officer: develop procedures to ensure that network system administrators: assess vulnerabilities in the current network configuration; make appropriate changes to the Windows 2000 operating system to address the vulnerabilities identified; develop an action plan to address the vulnerabilities; provide status reports on actions taken, Document a standard Domain Controller configuration and standard domain policy configurations; and provide technical training to network system administrators in line with NSA, NIST, and best business practices for securing Windows 2000.
4-19	Audit of SBA's Information Systems Controls Fiscal Year 2003	4/29/2004	That the Chief Information Officer: develop network administration policies and procedures to assure that vendor patches and security hot-fixes are installed timely; develop standards in conformance with government standards and industry best practices to properly configure the platforms residing on the network; develop procedures to periodically perform self-assessments using the SANS Top Twenty vulnerabilities and establish an internal goal of reducing SBA's vulnerability rating; require network administrators to develop a corrective action plan to address each weakness identified in the table at the end of this attachment with milestones for resolving each weakness; and require network administrators to provide monthly status reports to the Chief Information Officer.

# Appendix

## Appendix VIII (cont.) 6-Month Significant Recommendations Summary as of September 30, 2004

Report Number	Title	Date Issued	Recommendation
4-19	Audit of SBA's Information Systems Controls Fiscal Year 2003	4/29/2004	That the Chief Information Officer in consultation with OHCM, develop procedures for escalating administrative consequences for personnel identified as not compliant, such as: advise first-time offenders to immediately change their passwords to conform to the policy; temporarily disable accounts for a second offense, and notify the account owner and immediate supervisor; and suspend accounts for a third offense, and send a request for adverse personnel action to the office director OHCM, and the account holder.
4-25	Audit of an SBA Guaranteed Loan	6/22/2004	Seek recovery of \$177,166 from the lender, less any subsequent recoveries.
4-26	Audit of an Early Defaulted Loan	6/22/2004	Request the Associate Administrator to seek recovery of the SBA guaranty repair of \$235,008.
4-28	Audit of an SBA Guaranteed Loan	7/9/2004	Seek recovery of \$142,549 from the lender.
4-29	Audit of an Early Defaulted Loan	7/12/2004	Request the Associate Administrator to seek recovery of the SBA guaranty repair of \$373,760.
4-30	Single Audit of Federal Financial Assistance Programs Service Corps of Retired Executives (SCORE)	7/13/2004	That the Associate Administrator for Business and Community Initiatives (AA/OBCI) determine if SCORE implemented adequate written control procedures for monitoring and testing of the accuracy of the Chapters financial reporting.
4-32	Audit of an SBA Guaranteed Loan	7/29/2004	Seek recovery of \$542,663 from the lender.
4-33	Audit of an SBA Guaranteed Loan	7/30/2004	That SBA recover \$362,207 from the lender.
4-34	Audit of SBA's Process for Complying with the Federal Managers' Financial Integrity Act Reporting Requirements	7/29/2004	That the Chief Financial Officer develop policies and procedures for SBA managers that explain FMFIA and their responsibilities regarding FMFIA. The policies and procedures should establish guidelines for the evaluation by Agency managers of their systems of internal accounting and administrative controls.
4-34	Audit of SBA's Process for Complying with the Federal Managers' Financial Integrity Act Reporting Requirements	7/29/2004	That the Chief Financial Officer provide detailed guidance to the oversight, program and district offices to explain how and when they are to perform and document a complete risk assessment according to GAO Standards.
4-34	Audit of SBA's Process for Complying with the Federal Managers' Financial Integrity Act Reporting Requirements	7/29/2004	That the Chief Financial Officer report the deficiencies related to the internal control assessment and FMFIA reporting process identified by the OIG as a material weakness in the annual assurance statement that is released in SBA's Performance and Accountability Report for FY 2004, unless all recommendations included in this report are addressed before that time.

# Appendix

## Appendix VIII (cont.) 6-Month Significant Recommendations Summary as of September 30, 2004

<b>Report Number</b>	<b>Title</b>	<b>Date Issued</b>	<b>Recommendation</b>
4-36	Audit of an Early Defaulted Loan	8/10/2004	Request the Associate Administrator to seek recovery of the SBA guaranty repair of \$740,000.
4-37	Memorandum Report – Survey of Risk Management by Industry Code	8/11/2004	Include an analysis of industry codes as a part of the loan and lender monitoring system to identify potential areas of financial risk and to better focus limited oversight resources.
4-38	Audit of an SBA Guaranteed Loan	8/24/2004	That the Associate Administrator for Financial Assistance seek recovery of \$83,576, less any prior recoveries, from the lender.
4-39	Management Advisory Report on the Transfer of Operations to the National Guaranty Purchase Center	8/31/2004	That the Associate Deputy Administrator for Capital Access, in coordination with the General Counsel, determine the appropriate number of loan officers, supervisors, and attorneys to be assigned to the Center by (i) establishing the elements of quality for the purchase and liquidation action review process, (ii) determining how much time it takes to complete a quality review at each level (loan officer, supervisor and attorney), and (iii) computing the staff levels needed to complete the estimated annual purchase and liquidation action workloads at an acceptable level of quality.
4-40	Audit of an SBA Guaranteed Loan	9/13/2004	Take the necessary action to Recover \$246,460 paid to purchase the guaranty from the secondary market.
4-43	Audit of an SBA Guaranteed Loan	9/17/2004	Request the Associate Administrator to seek recovery of the SBA guaranty repair of \$293,823.

# Appendix

## Appendix IX 6-Month Legal Actions Summary April 1, 2004, through September 30, 2004

State	Program	Alleged Violation(s) Prosecuted	Legal Action	Investigated Jointly With
AZ	BL	The owner of a telecommunications business provided false statements and claims to a financial institution during the financing of his business through the SBA 504 program.	Owner signed settlement agreement in the amount of \$22,000.	None
CA	BL	Seventeen business loan recipients and/or convenience store owners, along with two corporations, participated in a scheme to falsely obtain SBA guaranteed business loans. Two of the individuals owned or controlled 60 convenience stores. The owners used straw borrowers and nominee borrowers to apply for and obtain loans guaranteed by SBA, various banks, and non-bank lenders. The owners falsely concealed their financial interests in the individual businesses, along with the source of the cash injection for each SBA loan, and laundered the proceeds of each SBA loan through the use of wires and checks. As a result of the scheme, loans totaling \$20 million were applied for and loans totaling at least \$8 million were approved and received.	Seventeen individuals and two corporations indicted.	FBI, IRS, ICE, USDA, State of California Alcohol and Beverage Control
CO	8(a)	A computer equipment business owner, while an officer of the company, declared personal bankruptcy and received a discharge of approximately \$135,000 in debts. He directed company employees to divert approximately \$690,000 of his company income to several bogus companies, which he created in order to avoid paying creditors. The owner failed to disclose his income, assets, and control of the company to the bankruptcy court and SBA.	Owner pled guilty; received 24 months incarceration; 2 years supervised release; a \$6,000 fine; ordered to pay \$39,197.	IRS, FBI, DCIS
FL	BL	The owner of an automotive repair business obtained a \$560,000 SBA guaranteed loan to purchase land. The business owner conspired with the property owner to represent to the lender that the capital injection had been made. In reality, they entered into an \$80,000 mortgage agreement, which they concealed from the lender, in lieu of the capital injection.	Property owner and auto repair business owner both pled guilty.	None
IL	BL	At the request of an SBA loan applicant, a graphic artist agreed to create a counterfeit U.S. Certificate of Naturalization, showing that the applicant, an illegal alien, was a U.S. citizen. The applicant later presented the counterfeit certificate along with \$2,500 cash (of an agreed upon \$5,000 bribe) to an SBA official in order to influence an official act. As was previously reported, the applicant and his spouse were each indicted for conspiracy and attempted loan fraud.	Graphic artist arrested and subsequently indicted.	None

# Appendix

## Appendix IX (cont.) 6-Month Legal Actions Summary April 1, 2004, through September 30, 2004

State	Program	Alleged Violation(s) Prosecuted	Legal Action	Investigated Jointly With
MA	BL	Four individuals involved with an intermediary participating in SBA's Microloan Program perpetrated a scheme to pay themselves more than \$300,000 in unauthorized "consulting" and "technical assistance" fees. They attempted to hide the transactions by paying the fees to two shell companies they had created. They also improperly charged the business \$170,000 in recreational travel, and forged signatures of board members on business checks. Two of the four subjects previously entered guilty pleas. The accountant and a board member were convicted at trial.	Accountant convicted; received 6 months home detention; 4 years probation; 300 hours community service; \$5,000 fine; and ordered to pay \$45,000. The board member was convicted and received 6 months home detention; 3 years probation; 300 hours community service; a \$5,000 fine; and ordered to pay \$19,000.	FBI, HUD, DOC/OIG, IRS
MO	BL	The former president of a small business made false statements to two financial institutions in order to obtain a \$340,000 SBA guaranteed loan. Later, he defaulted on the loan, resulting in a principal loss of \$224,370. Investigation further determined that he bilked investors out of about \$1.6 million by inducing more than 10 individuals to invest money with him through a marketing scheme.	Former president arrested and pled guilty.	IRS
NY	BL	A disbarred attorney allegedly claimed his firm had been located in downtown New York City on September 11, 2001, and falsely received a \$247,000 SBA disaster loan. The investigation revealed that his firm was never located at that address.	Disbarred attorney arrested.	IRS
NY	DL	A doctor and a co-subject perpetrated a scheme to defraud the SBA in conjunction with an SBA business disaster loan for damages to her medical practice caused by Hurricane Floyd. The doctor claimed approximately \$70,000 worth of medical equipment stored in her mother's residence was destroyed in the storm along with the home. The investigation revealed that there never was any medical equipment stored in the home. Further, the co-subject, with the consent of the doctor, submitted altered invoices to the SBA for work performed on the home.	Doctor pled guilty. Co-subject pled guilty and received 3 years probation, including 6 months home confinement, and ordered to pay \$34,356.	FBI

# Appendix

## Appendix IX (cont.) 6-Month Legal Actions Summary April 1, 2004, through September 30, 2004

State	Program	Alleged Violation(s) Prosecuted	Legal Action	Investigated Jointly With
NY	DL	The president/owner and the managing partner of a small business received a \$228,200 SBA disaster loan claiming losses incurred during the September 11 terrorists attacks. The pair claimed they were subleasing office space from their parent company located in the World Trade Center when, in fact, they were salaried employees of another company at the time. As previously reported, both individuals were convicted at trial.	President/owner received 51 months incarceration; 3 years supervised release; and ordered to pay \$373,000. Managing partner received 33 months incarceration; 3 years supervised release; and ordered to pay \$245,000.	None
ODA	DL	The OIG provided information to SBA's Office of Disaster Assistance (ODA) revealing that a sea tow business loan applicant was operating with a bogus captain's license. Actions taken by the U.S. Coast Guard will prevent the applicant from operating his business.	ODA cancelled a \$19,400 disaster loan.	None
OH	BL	The general manager of a food manufacturing business and his spouse (the president of the company) formed two shell corporations for purposes of concealing substandard purchases and theft of loan proceeds from a \$700,000 SBA guaranteed loan. The proceeds from these fraudulent sales were then laundered through bank accounts held in the names of the shell corporations and converted to personal use.	Both the former general manager and spouse were charged by Information.	None
OH	BL	The SBA and a financial institution approved a \$99,500 loan to a jewelry store president and his wife. The investigation disclosed that during the loan application process, the president failed to disclose the existence of a \$923,718 civil judgment filed against him and a company he previously owned. Additionally, he concealed his extensive criminal history.	The former president pled guilty.	FBI
OR	BL	A former loan agent engaged in a scheme to defraud a financial institution of more than \$500,000. The agent submitted false loan applications containing the names and personal identity information of six people, fictitious business information, and forged signatures. The agent used the proceeds of these loans for personal gain, including paying debts and gambling.	The former loan agent pled guilty.	FBI



# Appendix

## Appendix IX (cont.) 6-Month Legal Actions Summary April 1, 2004, through September 30, 2004

State	Program	Alleged Violation(s) Prosecuted	Legal Action	Investigated Jointly With
PA	8(a)	A former SBA 8(a) program participant made false statements to the SBA that someone else controlled the SBA certified company that he operated. In addition he mailed fictitious financial statements, which the bonding company relied upon to issue bonding. As a result of the company's defaults on contracts, the bonding company paid more than \$2.9 million in payment bonds and incurred an additional \$3 million in losses on performance bonds to have the contracts completed.	Former 8(a) program participant received 5 years probation. He must also continue to make restitution to the bonding company pursuant to a \$500,000 settlement agreement.	NCIS, DCIS, VA/OIG
PA	8(a)	The president of a now defunct construction company transferred \$495,000 from his construction company account to a personal account in the Bahamas and abandoned company contracts and subcontractors. He falsely stated in his SBA 8(a) Annual Update Form that he had relocated and that he controlled the day-to-day operations of the company. He also submitted false financial statements to a bank to support a \$300,000 line of credit and false statements to the bonding company. Ultimately the construction company defaulted on the contracts, resulting in a loss of almost \$6 million.	Former president received 7 years; 5 years probation; a \$2,500 fine, and ordered to pay over \$6.4 million in restitution.	NCIS, VA/OIG, DCIS.
PR	BL	Three businessmen participated in a scheme to falsely obtain two SBA guaranteed microloans totaling \$50,000. A co-owner, who had been denied an SBA microloan because of a poor credit history, conspired with the other co-owner and the office manager, who each received a \$25,000 microloan. On the applications, they both claimed that the loan was to purchase inventory for their respective businesses when the monies were actually used for the benefit of the undisclosed recipient.	Three businessmen indicted.	FBI
TX	BL	A Texas man received a \$420,000 SBA guaranteed loan. During the loan process, he provided a signed resume and an SBA Form 912 on which he falsely claimed U.S. citizenship.	Subject indicted.	DHS, SSA, Harris County Organized Crime Task Force, Texas ABC

# Appendix

## Appendix IX (cont.) 6-Month Legal Actions Summary April 1, 2004, through September 30, 2004

State	Program	Alleged Violation(s) Prosecuted	Legal Action	Investigated Jointly With
TX	BL	The proprietor of a convenience store and service station falsely represented that he was a U.S. citizen on his SBA Form 912, inducing a bank and the SBA into funding a \$1.2 million SBA guaranteed loan.	Business loan recipient pled guilty and received credit for time served; 1 year supervised release; \$500 fine; and is required to surrender to Immigration for deportation.	DHS, SSA, USDA, Texas DPS, Texas ABC
TX	BL	Business loan agent conspired to commit a wire and bank fraud scheme involving at least \$28 million in loans guaranteed by the SBA. For a 2-year period, the loan agent brokered loans to individuals interested in purchasing convenience stores. On behalf of solicited borrowers, he submitted false loan application documents and related cashier checks as phony capital injections to the lenders.	Business loan agent pled guilty.	FBI
TX	BL	Eight SBA business loan recipients falsely represented to be U.S. citizens on their SBA loan applications and their renewal applications for a Texas Alcoholic Beverage Commission permits.	Eight business loan recipients indicted.	DHS, SSA, USDA, Texas DPS, Texas ABC
TX	BL	Four convenience store proprietors falsely obtained nine convenience store SBA guaranteed business loans totaling \$9.5 million. The proprietors solicited individuals to apply for SBA guaranteed loans; submitted false and fraudulent documents; artificially inflated certain checking account deposits; and used escrowed loan proceeds to purchase cashier checks used as down payments for loans to conceal the fact that the down payments were funded by the loan proceeds.	Four convenience store proprietors indicted.	FBI
TX	BL	Two convenience store proprietors falsely claimed to be U.S. citizens on sworn renewal applications for Texas Alcoholic Beverage Commission permits.	Two proprietors pled guilty. One received 360 days incarceration and a \$2,000 fine. The other awaits sentencing.	DHS, SSA, USDA, Texas DPS, Texas ABC
TX	BL	A business loan applicant falsely represented to be a U.S. citizen on his renewal application for a Texas Alcoholic Beverage Commission permit and on his SBA Form 912 when applying for an SBA guaranteed loan.	Business loan applicant indicted	DHS, SSA, USDA, Texas DPS, Texas ABC

# Appendix

## Appendix IX (cont.) 6-Month Legal Actions Summary October 1, 2003, through March 31, 2004

State	Program	Alleged Violation(s) Prosecuted	Legal Action	Investigated Jointly With
TX	BL	A business loan applicant falsely represented, in a personal financial statement, that he had cash assets of \$200,000. This false statement was made in an attempt to influence the action of the SBA in connection with a loan application for \$2.7 million to purchase a local motel property.	Business loan applicant pled guilty and received 2 years probation; \$1,000 fine; and 60 hours community service.	FBI
TX	BL	Twelve SBA loan recipients falsely represented to be U.S. citizens on their SBA Forms 912.	Twelve business loan recipients indicted.	DHS, SSA, Harris County Organized Crime Task Force, Texas Alcoholic Beverage Commission
TX	BL	The proprietor of a convenience store and service station falsely represented to be a U.S. citizen on SBA Form 912. As a result of his actions, he falsely induced the SBA and the bank into funding an \$875,000 SBA guaranteed loan.	Proprietor indicted.	DHS, SSA, USDA, Texas DPS, Texas ABC
TX	BL	The president of a convenience store and service station falsely represented to be a U.S. citizen on a sworn renewal application for a Texas Alcoholic Beverage Commission permit and on an SBA Form 912. The president's false representation induced a bank and the SBA to fund an SBA guaranteed loan for over \$1.1 million.	President pled guilty and received 2 years probation.	None

Program codes: BL=Business Loans; DL=Disaster Loans; GC=Government Contracting and Business Development/Section 8(a) Business Development; IC = Investment Company

Joint-investigation Federal agency acronyms: BATF=Bureau of Alcohol, Tobacco, and Firearms; DCIS=Defense Criminal Investigative Service; DHS=Department of Homeland Security; DOC/OIG=Department of Commerce OIG; DOL/OIG=Department of Labor OIG; FBI=Federal Bureau of Investigation; HUD=Department of Housing and Urban Development; ICE=Immigration and Customs Enforcement; IRS=Internal Revenue Service; IRS-CID=IRS Criminal Investigation Division; NCIS=Naval Criminal Investigative Service; SSA/OIG=Social Security Administration OIG; TEXAS-ABC=Texas Alcoholic Beverage Commission; TEXAS-DPS=Texas Department of Public Safety; TIGTA=Treasury Inspector General for Tax Administration; USDA/OIG=United States Department of Agriculture OIG; VA/OIG=Department of Veterans Affairs OIG.

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# Appendix

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## Appendix X Office of Inspector General

