March 2009

HUBZONE PROGRAM

Fraud and Abuse Identified in Four Metropolitan Areas

GAO Highlights

Highlights of GAO-09-440, a report to Chairwoman, Committee on Small Business, House of Representatives

Why GAO Did This Study

The Small Business Administration's (SBA) Historically Underutilized Business Zone (HUBZone) program provides federal contracting assistance to small firms located in economically distressed areas, with the intent of stimulating economic development. In July 2008, GAO identified substantial vulnerabilities in SBA's application and monitoring process that demonstrated the HUBZone program is vulnerable to fraud and abuse. GAO also investigated 10 case studies of HUBZone firms in the Washington, D.C., area that misrepresented their eligibility.

GAO was asked to determine (1) whether additional cases of fraud and abuse exist outside of the Washington, D.C., area; (2) what actions, if any, SBA has taken to establish an effective fraud prevention program for the HUBZone program; and (3) what actions, if any, SBA took against the 10 case study firms in GAO's July 2008 testimony.

To meet these objectives, GAO identified selected HUBZone firms based on certain criteria, such as magnitude of HUBZone contracts and firm location. GAO also interviewed SBA officials and reviewed SBA data.

What GAO Recommends

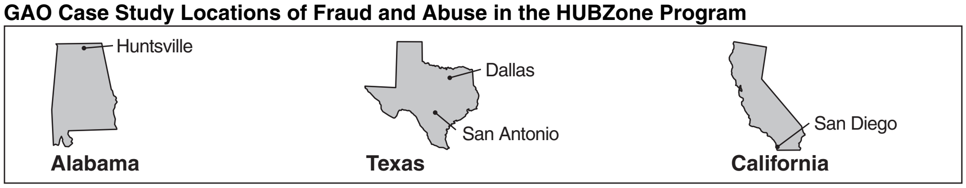
GAO makes four recommendations to improve SBA's ability to screen, monitor, and investigate fraud and abuse within the HUBZone program. SBA agreed with three of them.

To view the full product, including the scope and methodology, click on GAO-09-440. For more information, contact Greg Kutz at (202) 512-6722 or kutzg@gao.gov

What GAO Found

GAO found that fraud and abuse in the HUBZone program extends beyond the Washington, D.C., area. GAO identified 19 firms in Texas, Alabama, and California participating in the HUBZone program that clearly do not meet program requirements (i.e., principal office location or percentage of employees in HUBZone and subcontracting limitations). For example, one Alabama firm listed its principal office as "Suite 19," but when GAO investigators performed a site visit they found the office was in fact trailer 19 in a residential trailer park. The individual living in the trailer had no relationship to the HUBZone firm. In fiscal years 2006 and 2007, federal agencies obligated nearly $30 million to these 19 firms for performance as the prime contractor on HUBZone contracts and a total of $187 million on all federal contracts. The map below illustrates the geographical locations for the cases we examined.

GAO Case Study Locations of Fraud and Abuse in the HUBZone Program



Source: GAO.

Although SBA has initiated steps in strengthening its internal controls as a result of GAO's 2008 testimonies and report, substantial work remains for incorporating a fraud prevention system that includes effective fraud controls consisting of (1) front-end controls at the application stage, (2) fraud detection and monitoring of firms already in the program, and (3) the aggressive pursuit and prosecution of individuals committing fraud. In addition, SBA did not adequately field test its interim process for processing applications. If it had done so, SBA would have known that it did not have the resources to effectively carry out its review of applications in a timely manner. As a result, SBA had a backlog of about 800 HUBZone applications as of January 2009. At that time, SBA's interim application process was taking about 6 months—well over its 1-month goal set forth in SBA regulations.

SBA has taken some enforcement steps on the 10 firms previously identified by GAO that knowingly did not meet HUBZone program requirements. However, SBA's failure to promptly remove firms from the HUBZone program and examine some of the most egregious cases from GAO's July 2008 testimony has resulted in an additional $7.2 million in HUBZone obligations and about $25 million in HUBZone contracts to these firms. For example, a construction firm from the July 2008 testimony admitted that it did not meet HUBZone requirements and was featured in several national publications by name. It has continually represented itself as HUBZone certified and has received $2 million in HUBZone obligations and a $23 million HUBZone set-aside contract since the July 2008 testimony.