

Agency Financial Report

Fiscal Year 2010

Capital



Contracting



Counseling



Disaster



SBA
U.S. Small Business Administration

FOREWORD

The Government Performance and Results Act, enacted in 1993, requires federal agencies to establish standards for measuring their performance and effectiveness. The law requires agencies to develop annual performance plans that contain quantifiable measures of what they intend to accomplish, and issue performance reports describing their success in meeting those standards and measures. Since March 2000, performance reports are to be released annually by all CFO agencies.

Since FY 2007, the Small Business Administration has chosen to participate in an alternative approach to the Office of Management and Budget's consolidated Performance and Accountability Report. This report, the Agency Financial Report, is the first of three reports required under the alternative program. The other two reports — the Annual Performance Report and the Summary of Performance and Financial Information — will be delivered in February 2011.

The Association of Government Accountants has awarded the
SMALL BUSINESS ADMINISTRATION

THE CERTIFICATE OF EXCELLENCE IN ACCOUNTABILITY REPORTING

In recognition of SBA's outstanding efforts in preparing its

PERFORMANCE AND ACCOUNTABILITY REPORT

for the fiscal years ended September 30, 2006, 2007, 2008 and 2009



Information about SBA's programs is available at: www.sba.gov

SBA's plans and reports are available at: <http://www.sba.gov/aboutsba/budgetsplans/index.html>

Recovery Act - <http://www.sba.gov/recovery/index.html>

Para información acerca de los programas de la SBA: www.sba.gov/espanol/

Supplemental information relative to the AFR may be found in the CD that comes with this report.

Requests for printed copies, or questions and comments regarding the content, presentation and usefulness of this report are welcome and may be addressed to: performancereports@SBA.gov

Or, you may write to:
U.S. Small Business Administration
Office of Performance Management and the Chief Financial Officer
409 Third Street, S.W.
Washington, DC 20416

Or, you may call:
Timothy Gribben
Director, Office of Performance Management
(202) 205-6449

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Primer of SBA's Primary Loan Programs

7(a) Loan Guarantees

This is SBA's primary and most flexible loan program. Although it is delivered through commercial lending institutions, it is for businesses that would not otherwise have qualified for a loan through normal lending channels. The SBA guarantees a portion of 7(a) loans made and administered by commercial lending institutions. SBA 7(a) loans can be guaranteed for a variety of general business purposes including working capital, machinery and equipment, furniture and fixtures, and land and buildings. Loan maturity is up to 10 years for working capital and generally up to 25 years for fixed assets. The 7(a) loan program has several tailored delivery methods. The express programs – SBAExpress, Community Express, and Patriot Express – offer streamlined and expedited loan procedures for particular groups of borrowers. Rural Lender Advantage offers smaller loans tailored for the unique needs of rural lenders. Export Express, international trade loans, and Export Working Capital are 7(a) programs designed to help the exporting community. Finally, the SBA offers Certified Lender and Preferred Lender 7(a) loans through select lenders who have a proven track record with the SBA.

The Recovery Act of 2009 reduced fees for lenders and borrowers receiving 7(a) loans while also increasing the maximum guaranty up from 85 to 90 percent. These popular Recovery Act provisions have been extended in the Small Business Jobs Act of 2010 along with a permanent increase in the maximum loan size amount from \$2 million to \$5 million. The Recovery Act created, and the Jobs Act expanded and extended until 2013, another 7(a) specialty program called Dealer Floorplan Financing. This program provides loans to dealers of cars, trucks, RVs, boats, and other titleable inventory.

504 CDC Program

The 504 program provides long-term, fixed-rate financing for major assets such as real estate and heavy equipment. The loans provide financing to acquire fixed assets for business expansion or modernization. They are delivered by Certified Development Companies which are private, non-profit corporations set up to contribute to the economic development of their communities. SBA 504 loans cannot be used for working capital or inventory. A typical 504 loan is made up of a 50 percent senior lien by a private lender, a 40 percent junior lien by a CDC (which is 100 percent guaranteed by SBA), and a 10 percent equity buy-in from the owner. The Small Business Jobs Act of 2010 increased the maximum loan size to \$5 million (\$5.5 million for manufacturers).

Microloan Program

This program provides small short term loans for working capital or the purchase of inventory, supplies, furniture, fixtures, machinery and/or equipment. It is designed for small businesses and not-for-profit child care centers needing small scale financing and technical assistance for start-up or expansion. These loans are delivered through specially designated intermediary lenders who are nonprofit organizations with experience in lending and technical assistance. The Small Business Jobs Act of 2010 increased the maximum loan size from \$35,000 to \$50,000.

Message from the Administrator

November 15, 2010

I am pleased to present the U.S. Small Business Administration's FY 2010 Agency Financial Report. The SBA has chosen to produce the Agency Financial Report as an alternative to the consolidated Performance and Accountability Report.

This report details the Agency's efforts in its mission to maintain and strengthen the nation's economy by enabling the establishment and vitality of small businesses and by assisting in the economic recovery of communities after disasters. The Agency continues to move forward with goals in areas such as access to capital, opportunities in government contracting, entrepreneurial development, and disaster assistance.



Key SBA accomplishments in FY 2010 include:

Increase in SBA lending: Due to the continued effectiveness of Recovery Act loan provisions, the SBA increased lending support from over \$17 billion (47,897 loans) in FY 2009 to over \$22 billion (54,833 loans) in FY 2010. Also, at the end of FY 2010, the SBA reached its high-priority performance goal of 3,000 active lenders in its 7(a) loan program.

Increase in small business contracting in the federal government: Through stronger efforts to coordinate and reach out to other federal agencies, the SBA helped more than 30 percent of all federal Recovery Act contracting dollars go to small businesses. In addition, the SBA worked with government agencies to increase the percentage of contracts going to small business from 21.5 percent (FY 2008) to 21.9 percent (FY 2009), just shy of the goal of 23 percent.

Increase in entrepreneurial education resources: SBA's grant-funded resource partners continued to experience high demand for their free and low-cost services from entrepreneurs and small business owners. For example, SBA resource partners helped over 15,000 entrepreneurs start a business in FY 2010, an 8 percent increase over FY 2009.

Continued optimization of disaster assistance resources: The SBA quickly responded to dozens of federally-declared disasters, including the BP Deepwater Horizon Oil Spill for which the SBA established 29 disaster assistance centers in four states and approved over 1,200 loans and loan deferments to affected small businesses.

In addition, in the final days of FY 2010, the President signed the most significant piece of small business legislation in more than a decade: the Small Business Jobs Act of 2010. The SBA implemented many of the key provisions almost immediately, helping 5,000 businesses receive SBA Jobs Act loans (totaling nearly \$3 billion in lending support) within 30 days of its enactment.

Through the Agency's new Strategic Plan for FY 2011 through FY 2016, the SBA is renewing its commitment to growing businesses and creating jobs, building an SBA that meets the needs of today's and tomorrow's small businesses, and serving as the voice for small business. The SBA will continue to work toward operational excellence, while actively identifying and removing elements of waste, fraud, and abuse from its programs. In addition, we

will work to address issues that may emerge such as the need for stronger oversight of increased risk exposure due to our efforts to increase the number of SBA lenders.

I am pleased to provide an assurance that SBA's financial and performance data in this report are reliable and complete. SBA's auditor issued an unqualified opinion on our FY 2010 financial statements. The auditor did not note any material internal control weaknesses.

Sincerely,

A handwritten signature in black ink that reads "Karen G. Mills". The signature is written in a cursive style and is positioned above the printed name and title.

Karen G. Mills
Administrator

MANAGEMENT'S DISCUSSION & ANALYSIS

SBA's Mission

The mission of the U.S. Small Business Administration is to maintain and strengthen the nation's economy by enabling the establishment and vitality of small businesses and by assisting in the economic recovery of communities after disasters.

Success Story



Using Cutting Edge Technology to Prepare for Emergencies Engineering & Computer Simulations, Inc., Orlando, Florida

Waymon Armstrong is the owner of Engineering & Computer Simulations, Inc. a small business that uses computer simulations to help government and private sector clients prepare for and respond to natural disasters, medical emergencies and combat. This year he was honored by the SBA as the 2010 National Small Business Person of the Year. SBA Administrator Karen Mills made the announcement during the annual celebration of National Small Business Week.

“Waymon Armstrong is a perfect example of the innovation, inspiration and determination that exemplify America’s most successful entrepreneurs,” said Mills. He believed in his brainchild to the point where he deferred his own salary for three years to keep it afloat. When layoffs loomed for his staff after 9/11, their loyalty and belief in the company was so great that they were willing to work without pay for four months.

“Waymon’s commitment to his employees and to his business demonstrates the qualities that make small businesses such a powerful force for job creation in the American economy and in their local communities,” said Mills. “These are the same qualities that will lead us to economic recovery.” The SBA is especially proud that his company benefited from two grants under SBA’s Small Business Innovation and Research Program.

Started in 1997, Engineering & Computer Simulations is today one of Inc. Magazine’s 500 fastest growing private companies in America. The ECS engineering team brings together an experienced group of professionals that value innovation and creativity while focusing on customers’ needs. The successful company doubled its revenues in 2008 and expanded its staff by 33 percent in 2009. It has seen a 640 percent sales growth over the past three years.

Executive Summary

The Small Business Administration acts as a direct lender or guarantor of small business loans and provides management and technical assistance as well as contracting opportunities to small businesses. The SBA also provides disaster assistance to communities that have suffered through a catastrophe, with the intention of rebuilding the devastated economy and community simultaneously. Throughout FY 2010, the SBA relied on four strategic goals to guide the Agency's actions:

1. Drive business formation, job growth and economic expansion, particularly in under-served markets.
2. Provide timely financial assistance to homeowners, renters, nonprofit organizations and businesses affected by disaster.
3. Improve the economic environment for small business by ensuring their needs are being met.
4. Optimize core operations to increase responsiveness to customers, streamline processes and improve compliance and controls.

In the past two years, the SBA has played a critical role in helping revive the nation's economy. With the Recovery Act passage in February 2009, the SBA embarked on a period of rapid expansion with lowered fees and higher guaranties on the major loan products. Recovery Act funding, originally intended to last until the end of FY 2010, ran out in November 2009. The SBA received a course of temporary extensions of funding from Congress until passage of the Small Business Jobs Act in September 2010 made many of the provisions permanent. The SBA seized the moment of growth in programs and loan volumes to improve the financial management practices and fine-tune performance measures. Indeed, the Agency received an unqualified audit opinion with no material weaknesses in FY 2010. The government-wide response to the economic crisis, combined with the collaborative regular reporting required by the Recovery Act (and available at Recovery.gov), has helped push the SBA into a new era of intra- and inter-agency cooperation to help small businesses expand and prosper.

Financial Results

The SBA is the smallest of the major federal credit agencies, behind the Department of Agriculture, the Department of Education, the Department of Housing and Urban Development, and the Department of Veteran Affairs. For FY 2010 SBA's total budgetary resources were \$8.3 billion as well as \$10 billion for loan financing (nonbudgetary). SBA's guaranteed portion of the outstanding loan principal balance rose 3.6 percent in FY 2010 to \$64.4 billion. The overall outstanding principal balance grew at 3.2 percent in FY 2010 to a new high of \$93.3 billion. Growth in SBA's portion occurred primarily as a result of the popularity of the Recovery Act's higher guaranty limits as well as its extensions, with new guaranties up 23 percent compared to FY 2009. On the downside, SBA's portfolio of loans receivable continued to grow in FY 2010 due to increases in the purchases of guaranteed business loans. This portfolio of purchased guaranties and defaulted loans remained at \$9.1 billion, though its composition changed as direct disaster loans shrank \$392 million while defaulted guaranteed business loans grew \$337 million.

The financial management team has paid particular attention to improving the Agency's record on improper payments. The SBA Inspector General issued audit reports on the 7(a) Guaranty Purchase and Disaster improper payments in FY 2009. As a result of the findings and recommendations of these reports, the SBA changed its methodology in both programs in the sampling and testing for improper payments. After an uptick in FY 2009, FY 2010 saw a decline in improper payment rates from 3.8 percent to 1.9 percent in the 7(a) guaranty program but an increase from 20.9 percent to 34.2 percent in Disaster improper payments. The latter generally results from loan documentation errors and indicates a need to adhere to the documentation requirements of SBA's Standard Operating Procedures, a need that will be addressed with additional training as well as a dedicated team to review and report on improper payments from the disaster processing center.

Improper payments will receive additional emphasis for improvement when the Improper Payment Elimination and Recovery Act enacted in July 2010 becomes effective in FY 2011.

Program Results

The SBA continued its rebound in lending volumes to pre-crisis levels, averaging \$1.4 billion in monthly gross loan approvals for 7(a) and 504 in FY 2010 as compared to the \$1.5 billion monthly average in FY 2008. The response of lenders to the Recovery Act provisions spurred a sizeable change in the number of active lenders for the 7(a) program, a High Priority Performance Goal for the Agency. In FY 2010, 3,061 lenders made a 7(a) or ARC loan compared to the 2,408 lenders active in FY 2008, an increase of 27 percent. This increased access to capital supported 556,045 jobs in FY 2010 and assisted 49,085 small businesses, providing small businesses and the many people they affect with the necessary financial support to survive these tough economic times.

The SBA continued to advocate for small businesses pursuing government contracting opportunities as well. Congress has given the Agency the responsibility of overseeing the government-wide small business goal setting program, intending 23 percent of all contracts to go to small businesses.

SBA's resource partners – the small business development centers, women's business centers, and SCORE – provide counseling and expertise to over a million small businesses and entrepreneurs. These resource partners provide guidance in developing business plans, implementing new technologies, accessing capital, winning government contracts, developing marketing plans, and many other undertakings vital to the success of a small business throughout its lifecycle. The SBA provided \$134 million in FY 2010 in grant funding for these programs to provide necessary, targeted technical

services to entrepreneurs throughout the nation. Additionally, an estimated 600,000 users will access free online courses through SBA's Small Business Training Network.

For FY 2010, the SBA approved \$570 million in disaster loans. The Office of Disaster Assistance's dedication to continual process improvement meant that 100 percent of home applications were processed within 14 days, 100 percent of loans were disbursed within 5 days of closing, and 99 percent of business applications were processed within 18 days.

Management Results

The SBA continues to work with its program offices to provide the best possible measures of performance. In FY 2010, the SBA conducted a full review of the performance measures, consolidating several into more accurate counts (i.e. jobs supported replaced jobs created/retained) while helping several program offices develop new measures to follow the Recovery Act and Small Business Jobs Act new programs and provisions. In addition, staff conducted webinars and training sessions for recipients of Recovery Act funds to assist in the reporting requirements of Recovery.gov. Finally, the SBA participated with the Office of Management and Budget (OMB) to develop High Priority Performance Goals for the Agency. These goals helped organize the new strategic plan, future budget submissions, and fostered intra-agency cooperation for a common endeavor. Indeed, the renewed focus allowed the SBA to meet two of the four high priority goals ahead of schedule, increasing the number of active lenders to over 3,000 and decreasing processing times for disaster loans. The SBA management team has put in place a strong foundation for the Agency in the realm of performance management as the government continues to move toward a more collaborative approach, both intra- and inter-agency.

SBA BY THE NUMBERS

(All Dollars in Millions)

		FY 2007	FY 2008	FY 2009	FY 2010
Total Portfolio⁽¹⁾	Outstanding Principal Balance	\$84,512	\$88,095	\$90,451	\$93,340
Financial Assistance⁽²⁾					
7(a) Regular Loans	Dollars of Gross Loans Approved	\$ 14,292	\$ 12,671	\$ 9,191	\$ 12,407
504 Regular Loans	Dollars of Gross Loans Approved	\$ 6,314	\$ 5,290	\$ 3,834	\$ 4,433
Microloans	Dollars of Gross Loans Approved for Microborrowers	\$ 33	\$ 32	\$ 35	\$ 45
SBIC	Dollars of Gross Financings Invested in Small Businesses	\$ 759	\$ 1,030	\$ 788	\$ 2,047
7(a) Loans	Number of Gross Loans Approved	99,606	69,434	41,289	47,000
504 Loans	Number of Gross Loans Approved	10,669	8,883	6,608	7,833
Microloans	Number of Gross Loans Approved for Microborrowers	2,523	2,771	2,797	3,789
SBIC	Number of Small Businesses Financed	2,057	1,905	1,481	1,331
Disaster Assistance^{(2) (6)}					
	Dollars of Gross Loans Approved	\$ 820	\$ 826	\$ 1,130	\$ 574
	Number of Gross Loans Approved	14,014	15,128	21,780	15,356
Management Assistance					
SCORE	Number Small Businesses Assisted	336,411	360,559	380,357	407,240
SBDC	Number Small Businesses Assisted	600,665	558,487	583,770	589,352
WBC	Number Small Businesses Assisted	146,828	159,879	155,383	160,735
Procurement Assistance					
Prime Contracting	Annual Value of Federal Contracts	\$ 83,275	\$ 93,305	\$ 96,800	N/A ⁽³⁾
Prime Contracting (%) ⁽⁵⁾	% of Federal Contracts to SBs	22.0%	21.5%	21.9%	N/A ⁽³⁾
Surety Bond	Number Bid and Final Bonds Guaranteed	5,809	6,055	6,135	8,348
HUBZone	Annual Value of Federal Contracts	\$ 8,463	\$ 10,157	\$ 12,413	N/A ⁽³⁾
8(a) Program	Number of Small Businesses Assisted	9,479	9,462	8,854	N/A ⁽³⁾
Regulatory Assistance					
Advocacy	Regulatory Cost Savings	\$ 2,568	\$ 10,760	\$ 6,990	\$ 14,994 ⁽⁴⁾

(1) This is the gross cumulative outstanding disbursed amount that includes all Disaster loans and SBA guaranteed loans (including the non-guaranteed portion) less loan payments and payoffs, plus loan increases.

(2) There are three basic ways to present loan data: 1) Gross Loans Approved—the total loans approved; 2) Net Loans Approved (gross loans approved *plus* any loan increases *minus* any cancellations); and 3) Disbursed loans (the amount that is actually given to the borrower). In the "Financial Assistance" and "Disaster Assistance" part of the table Gross Loans Approved is presented because it is the only loan data that will never change.

(3) Federal agencies have not yet certified their FY 2010 data. The SBA expects to receive the FY 2010 certified data by the 3rd or 4th quarter of FY 2011.

(4) The FY 2010 is an estimate. This number will be finalized in February 2011 in Advocacy's annual report to Congress.

(5) The federal government is required to give small businesses at least 23 percent of all contracting dollars.

(6) In FY 2010, the SBA changed the method for determining these Disaster numbers. All prior numbers have been adjusted to ensure consistency and comparability.

SBA's History and Organization

Congress created the U.S. Small Business Administration in 1953 to “aid, counsel, assist and protect, insofar as is possible, the interests of small business concerns.” The charter also stipulated that the SBA would ensure small businesses a “fair proportion” of government contracts and sales of surplus property. SBA’s mission is to maintain and strengthen the nation’s economy by enabling the establishment and vitality of small businesses and by assisting in the economic recovery of communities after disasters. Agency programs also include management assistance and specialized outreach to veterans, women and underserved markets.

The SBA provides financial assistance to small businesses in the form of loans and venture capital. Since enactment of the Federal Credit Reform Act of 1990, the SBA has made or guaranteed in excess of \$242 billion in business loans. Through the Small Business Investment Company program, the SBA has put \$57.6 billion worth of venture capital into more than 107,000 small businesses since 1990.

The disaster loan program is the only form of SBA assistance that is not limited to small businesses. Disaster loans help homeowners, renters, businesses of all sizes, and nonprofit organizations to fund rebuilding and recovery efforts. The Agency does this by focusing on the restoration of real and personal property and assisting businesses to return to operations as quickly as possible. On average, the Agency makes disaster loans totaling approximately \$500 million to \$1 billion each year, and has an active portfolio of about \$8 billion. Since its inception, the SBA has approved over 1.9 million disaster loans for nearly \$49 billion.

The SBA plays a vital role in enabling America’s entrepreneurs and has stamped its mark on many small businesses that have grown to become household names and leaders in their fields. These firms include Nike, Staples, Apple, Federal Express, Ben & Jerry’s, Outback Steakhouse, Hewlett Packard, and a host of others. For their outstanding achievements, dedication and hard

work, Engineering & Computer Simulations was named the 2010 National Small Business of the Year. SBA Administrator Karen Mills saluted the company and its owner Waymond Armstrong as “a perfect example of the innovation, inspiration and determination that exemplify America’s most successful entrepreneurs.” He believed in his brainchild to the point where he deferred his own salary for three years to keep his company afloat. When layoffs loomed for his staff after 9/11, their loyalty and belief in the company was so great that they were willing to work without pay for four months. “Mr. Armstrong’s commitment to his employees and to his business demonstrates the qualities that make small businesses such a powerful force for job creation in the American economy and in their local communities; these are the same qualities that will lead us to economic recovery.” The Agency is proud that Engineering & Computer Simulations benefited from two grants under SBA’s Small Business Innovation and Research program.

Organization by Key Assistance Areas

The SBA is an organization with a nationwide presence. Its headquarters is located in Washington, D.C., while its business products and services are delivered with the help of 10 regional offices, 68 district offices and a vast network of resource partners in all 50 states, the District of Columbia, Puerto Rico, American Samoa, the U.S. Virgin Islands, and Guam.

The SBA is organized around five key functional areas: Financial Assistance, Procurement Assistance, Management Assistance, Disaster Assistance and Regulatory Assistance. The category of Other Assistance captures all other activities. Following are brief descriptions of SBA offices and programs and some of the products and services they provide.

Financial Assistance

The Office of Capital Access assists small businesses in obtaining capital via the 7(a), 504 and

Microloan programs and the Small Business Investment Company program. OCA is also responsible for the Surety Bond Guarantee and the International Trade Assistance programs.

Procurement Assistance

The Office of Government Contracting and Business Development provides assistance to small businesses in obtaining federal procurement opportunities through the government-wide prime and subcontracting programs. Additionally, the 8(a) Business Development program assists small businesses to be better prepared to take advantage of procurement opportunities. GC/BD also sets size standards for small businesses which determine the size a business must be to be considered a small business.

Management Assistance

The Office of Entrepreneurial Development provides business counseling and training through its partners network composed of small business development centers, women business centers and SCORE. In addition, district offices provide counseling and training that complements the assistance provided by SBA partners.

Disaster Assistance

The Office of Disaster Assistance provides affordable, timely and accessible financial assistance to homeowners, renters and businesses following a disaster.

Regulatory Assistance

The Office of Advocacy provides an independent voice for small business to advance its views, concerns, and interests before Congress, the federal government, federal courts and state policy makers.

The National Ombudsman receives complaints and comments from small businesses and acts as a “trouble shooter” between small businesses and federal agencies.

Other Assistance

The Office of Veterans Business Development formulates and delivers policies and programs that provide assistance to veterans seeking to start and develop small businesses.

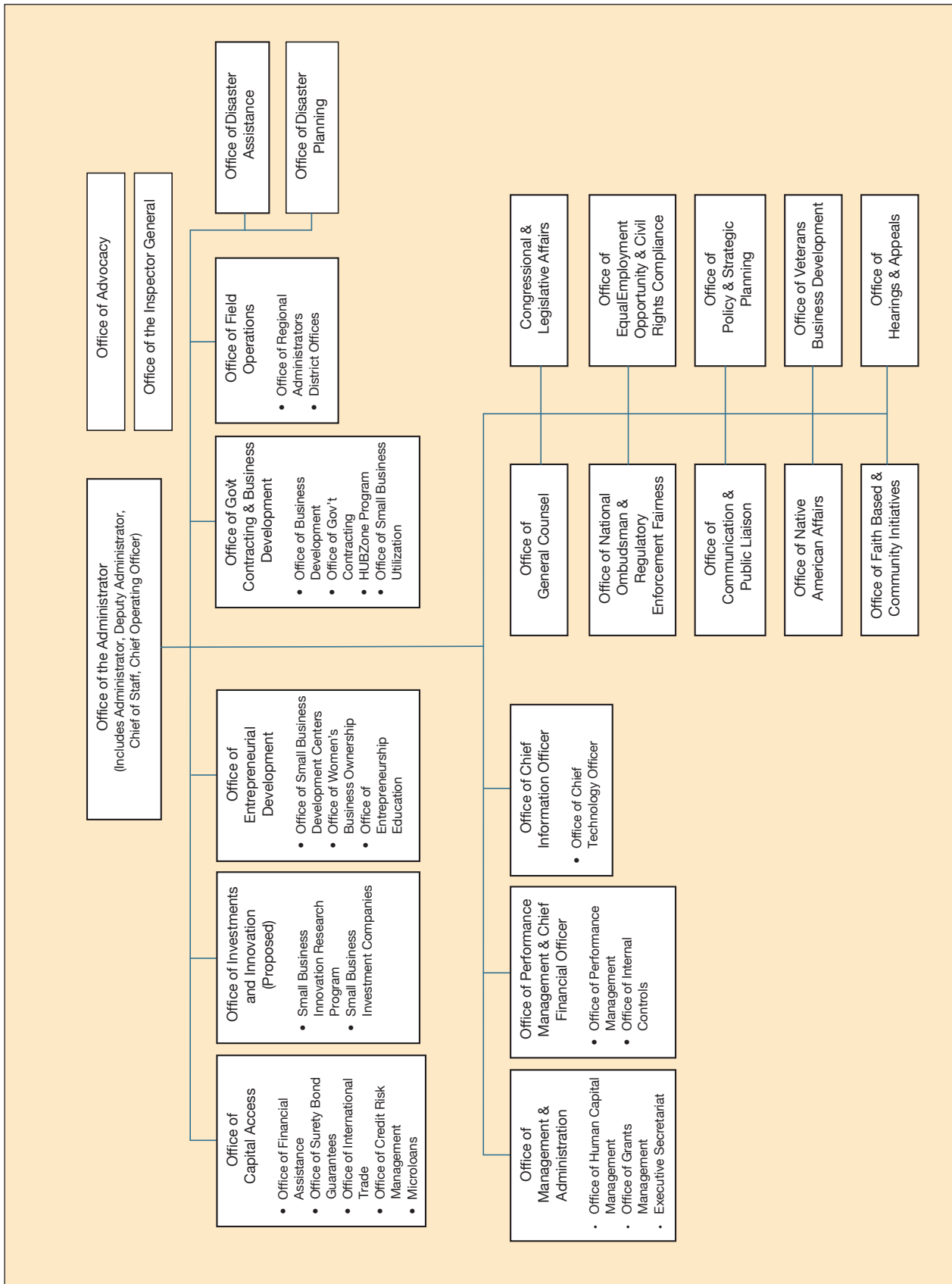
The Office of Native American Affairs focuses on the assistance provided to American Indians, Alaska Natives, Native Hawaiians, and the indigenous people of Guam and American Samoa.

*Did
you
know*

The SBA partners with banks and credit unions to offer billions of dollars a year in loans to small business owners.

In FY 2010, the SBA supported over 22 billion dollars in lending to small businesses. Learn more at <http://www.sba.gov/aboutsba/sbaprograms/elending>.

SBA'S ORGANIZATION CHART



Summary Performance Information on Key SBA Offices/Programs

The following table presents key SBA FY 2010 performance data. SBA's 7(a), 504, and Disaster loans are the three largest SBA guaranty and direct loan programs. These programs make up the bulk of SBA's loan portfolio. The other indicators have been included as an example of the impact of other SBA programs and to highlight the soundness of SBA's financial systems (appropriate for the Agency's financial report). Detailed performance information on all SBA programs will be presented, and all variances explained, in the FY 2010 Annual Performance Report which will be submitted in February 2011.

Program	Performance Indicator	Type of Indicator	FY 2007 Actual	FY 2008 Actual	FY 2009 Actual	FY 2010 Goal	FY 2010 Actual	FY 2010 Variance
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Strategic Goal 1 - Growing Businesses and Creating Jobs

Financial Assistance

7(a)	Active Lending Partners (#)	Outcome	2,383	2,408	2,771	2,800	3,061	9% G
7(a)	Small Businesses Assisted (#) ⁽¹⁾	Outcome	90,146	62,441	37,153	37,500	41,705	11% G
7(a)	Jobs Supported (#) ⁽¹⁾	Outcome	776,729	586,955	423,980	625,500	473,502	-24% R
504	Small Businesses Assisted (#) ⁽¹⁾	Outcome	10,409	8,675	6,461	5,600	7,664	37% G
504	Jobs Supported (#) ⁽¹⁾	Outcome	126,069	111,996	74,849	133,000	82,543	-38% R

Contracting Assistance

Prime Contracting	Federal Contract Dollars Awarded to Small Businesses (% of Total Applicable Federal Contract Dollars)	Outcome	22%	21.5%	21.9%	23.0%	N/A ⁽³⁾	N/A
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Disaster Assistance

Disaster	Average Time to Process Business Physical Application (days)	Output	11	11	14	18	10	44% G
Disaster	Home Loans Processed Within Standard (%)	Output	97%	94%	94%	85%	100%	15% G

Management and Technical Assistance

SBDC	Small Business Created (#)	Outcome	7,331	12,730	12,543	7,500	13,639	82% G
WBC	Small Business Created (#)	Outcome	618	727	727	618	689	12% G
SCORE	Small Business Created (#)	Outcome	1,082	943	931	1,082	1,077	0% Y

Strategic Goal 2 - Building an SBA that Meets the Needs of Today's and Tomorrow's Small Businesses

Financial Management

Financial Reporting	Unqualified Opinions for Audit Year	Outcome	Yes	Yes	Yes	Yes	Yes	0% G
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Strategic Goal 3 - Serving as the Voice for Small Businesses

Regulatory Assistance

Advocacy	Regulatory Cost Savings to Small Businesses (\$ in Billions)	Outcome	\$ 2.60	\$ 10.76	\$ 6.99	\$ 5.50	N/A ⁽²⁾	N/A
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¹ A more precise methodology was developed in FY 2009 to calculate "Jobs supported" and "Small Businesses Assisted." In addition to the change in methodology, the figures are net of fully cancelled loans. Prior year results have been restated to reflect this change. "Jobs supported" replaced the title "Jobs Created/Retained." "Jobs supported" more clearly described the measured activity.

² The FY 2010 "Actual" will be finalized in February 2011 in Advocacy's annual report to Congress.

³ The FY 2010 "Actual" will be finalized in the third or fourth quarter of FY 2011.

Green G	The Actual result meets or exceeds target
Yellow Y	The Actual result is within 10% of meeting the target
Red R	The Actual result is less than 90% of target

Variance Explanations

7(a) Jobs Supported (#) (-24%) - the Goal of 625,500 Jobs Supported was established in FY 2009 and was based on "Loans Disbursed." In FY 2010 the methodology was changed to "Loans Approved Less Cancellations" which significantly reduced the identified loans.

504 Jobs Supported (#) (-38%) - the Goal of 82,543 Jobs Supported was established in FY 2009 and was based on "Loans Disbursed." In FY 2010 the methodology was changed to "Loans Approved Less Cancellations" which significantly reduced the identified loans.

Analysis and Highlights of Financial Statements and Results

Highlights of Financial Results

(Dollars in Thousands)

At End of Fiscal Year	Unaudited		% Change
	FY 2010	FY 2009	
CONDENSED BALANCE SHEET DATA			
Fund Balance with Treasury	\$ 6,116,325	\$ 3,469,465	76.29%
Credit Program Receivables	9,076,679	9,128,496	-0.57%
All Other Assets	37,472	28,498	31.49%
Total Assets	\$ 15,230,476	\$ 12,626,459	20.62%
Liability for Loan Guaranties	\$ 4,467,006	\$ 3,994,636	11.83%
Debt with Treasury	11,753,781	10,878,283	8.05%
Downward Reestimate Payable to Treasury	130,993	64,875	101.92%
All Other Liabilities	413,241	377,265	9.54%
Total Liabilities	16,765,021	15,315,059	9.47%
Unexpended Appropriations	2,295,070	1,983,504	15.71%
Cumulative Results of Operations	(3,829,615)	(4,672,104)	18.03%
Total Net Position	(1,534,545)	(2,688,600)	42.92%
Total Liabilities and Net Position	\$ 15,230,476	\$ 12,626,459	20.62%
For the Fiscal Year			
STATEMENT OF NET COST BY STRATEGIC GOAL			
Goal 1: Expand America's Ownership Society			
Loan Subsidy Cost including Reestimates	\$ 4,193,713	\$ 4,803,699	-12.70%
All Other Cost Net of Revenue	545,027	439,889	23.90%
Goal 2: Provide Timely Financial Assistance Affected by Disaster			
Loan Subsidy Cost including Reestimates	208,372	354,947	-41.29%
All Other Cost Net of Revenue	238,341	320,381	-25.61%
Goal 3: Improve Economic Environment for Small Business	17,814	14,506	22.80%
Costs Not Assigned	73,930	62,294	18.68%
Total Net Cost of Operations	\$ 5,277,197	\$ 5,995,716	-11.98%
STATEMENT OF NET COST BY EXPENSE TYPE			
Loan Subsidy Cost and Required Annual Reestimates	\$ 4,402,085	\$ 5,158,646	-14.67%
Goal 1 Administrative Costs	545,027	439,889	23.90%
Goal 2 Administrative Costs	238,341	320,381	-25.61%
Goal 3 Costs	17,814	14,506	22.80%
Congressional Initiative Grants	52,035	43,635	19.25%
Other Costs Not Assigned	21,895	18,659	17.34%
Total Net Cost of Operations	\$ 5,277,197	\$ 5,995,716	-11.98%
CONDENSED STATEMENT OF CHANGES IN NET POSITION			
Beginning Cumulative Results of Operations	\$ (4,672,104)	\$ (1,362,736)	-242.85%
Total Financing Sources	6,119,686	2,686,348	127.81%
Less: Net Cost of Operations	5,277,197	5,995,716	-11.98%
Ending Cumulative Results	(3,829,615)	(4,672,104)	18.03%
Beginning Unexpended Appropriations	1,983,504	1,696,866	16.89%
Total Budgetary Financing Sources	311,566	286,638	8.70%
Ending Unexpended Appropriations	2,295,070	1,983,504	15.71%
Ending Net Position	\$ (1,534,545)	\$ (2,688,600)	42.92%
CONDENSED STATEMENT OF BUDGETARY RESOURCES			
Net Appropriations & Budget Authority Received, Budgetary	\$ 6,554,119	\$ 3,050,068	114.88%
Spending Authority from Offsetting Collections	8,218,384	4,471,595	83.79%
Unobligated Balances Forward	2,701,923	2,976,819	-9.23%
Other Budgetary Resources, Net	866,343	1,838,573	-52.88%
Total Budgetary Resources	\$ 18,340,769	\$ 12,337,055	48.66%
Obligations Incurred, Budgetary	\$ 6,598,610	\$ 3,453,667	91.06%
Obligations Incurred, Nonbudgetary	6,515,175	6,181,465	5.40%
Balances, Available and Unavailable	5,226,984	2,701,923	93.45%
Total Status of Budgetary Resources	\$ 18,340,769	\$ 12,337,055	48.66%

Analysis of Financial Results

The SBA prepares its financial statements as a critical aspect of ensuring accountability and stewardship for the public resources entrusted to it. The financial statements are prepared in accordance with guidance issued by the Office of Management and Budget pursuant to the Chief Financial Officers Act of 1990. While these statements have been prepared from SBA's books and records in accordance with generally accepted accounting principles for federal entities and the formats prescribed by OMB, they are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records. The statements should be read with the realization that they are a component of the U.S. Government, a sovereign entity. One implication of this is that the liabilities presented herein cannot be liquidated without the enactment of appropriations, and ongoing operations are subject to the enactment of future appropriations.

This analysis is intended to help readers understand the Agency's financial results, position and condition as portrayed in the principal financial statements and notes. It explains major changes in assets, liabilities, costs, and budgetary resources; includes comparisons of the current year to the prior year; and discusses the relevance of particular balances and amounts reflected in the principal financial statements and notes. This section also depicts trends via the use of charts and graphs to further understanding of the financial condition and results of the Agency. The SBA is primarily a credit agency and therefore the trends and financial condition of credit program receivables and reestimates are emphasized in this analysis. The Highlights of Financial Results chart provides a condensed summary of the balances in the financial statements for the current and prior year and the percentage change.

The Portfolio Analysis section in this MD&A discusses in some detail the major trends impacting SBA's portfolio of loan guaranties and receivables. The purpose of this section is to provide an operational analysis of SBA's credit programs, rather than a financial statement analysis. As a

result, the definitions of the loan and guaranty balances in the Portfolio Analysis section may differ somewhat from the balances used in this Analysis of Financial Results. For example, for the 7(a) program the total amount of guaranteed loans is used in the Portfolio Analysis, where only SBA's guaranteed portion is used in the Analysis of Financial Results, as it ties to balances in the financial statements.

Background

The SBA is the smallest of the major federal credit agencies, behind the Department of Agriculture, the Department of Education, the Department of Housing and Urban Development and the Department of Veterans Affairs. Most of SBA's available budgetary resources are devoted to its credit programs. For FY 2010 SBA's total budgetary resources were \$8.3 billion, and nonbudgetary resources in the loan financing funds were \$10 billion. The apportioned budgetary resources are the amounts available to enter into new obligations and to liquidate them. Budgetary resources are made up of new budget authority and unobligated balances of budget authority provided in previous years. The loan financing funds are nonbudgetary accounts that record all the cash flow activity resulting from post 1991 direct loans and loan guaranties. This activity in the financing account is reported separately in the Budget of the United States Government and is excluded from the budget surplus/deficit totals.

The portion of the outstanding principal guaranteed by the SBA as of September 30, 2010 was \$64.4 billion. This amount is up 3.58 percent from the \$62.2 billion guaranteed at September 30, 2009. New guaranties disbursed by SBA participating banks during FY 2010 were up 23 percent compared to FY 2009 (see footnote 6C in the financial statements for further detail on loans disbursed and outstanding at year end). **Chart I** depicts the increase in guaranteed loans disbursed during FY 2010 to near pre-recession levels. This increase in the guaranteed loans disbursed is due to the passage of the American Recovery and Reinvestment Act legislation. In February 2009,

CHART I GUARANTIED LOANS DISBURSED

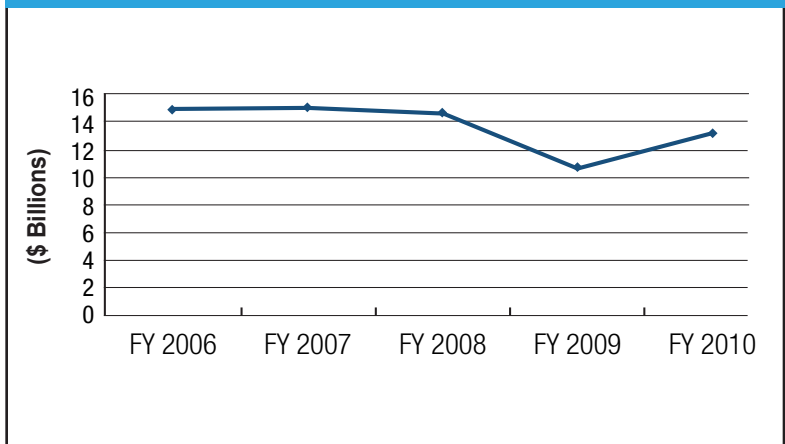
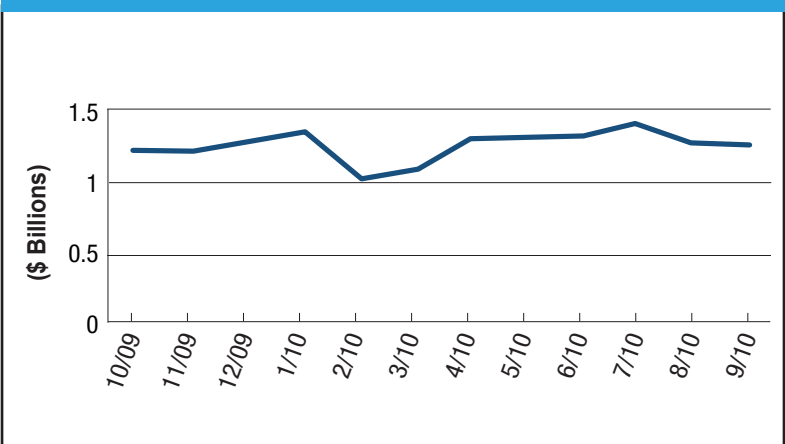


CHART II GUARANTIED LOANS DISBURSED MONTHLY



through ARRA, Congress appropriated \$730 million to the SBA to provide new lending incentives that included the Agency temporarily waiving its fees on 7(a) and 504 loans and increasing the guaranties it offers banks on 7(a) loans. These funds were exhausted during November 2010 and ARRA lending was suspended. The U.S. Congress subsequently provided an additional \$305 million through several appropriations to extend ARRA lending in FY 2010. On May 31, 2010 the temporary authority to increase the 7(a) guaranty percentage expired, contributing to a reduction in SBA guaranteed loan volume during the last four months of FY 2010. **Chart I** reflects the increase in disbursements in FY 2010 (due to carryover from FY 2009 as well as the passage of the extensions). The SBA expects disbursements to continue to grow in early FY 2011 because of the passage of the Small Business Jobs Act of 2010 on September 27, 2010. The Jobs Act extended ARRA fee relief for the 7(a) and 504 programs and increased the guaranty on 7(a) loans

through December 31, 2010, and, furthermore, appropriated \$505 million to pay for the fee relief and guaranty increase. **Chart II** depicts the monthly disbursements of guaranteed loans during FY 2010. As reflected in the chart, there is an increase in March and April which is when additional ARRA extensions were appropriated and there is a downward trend in August and September because the ARRA lending expired.

SBA's portfolio of loans receivable continued to grow in FY 2010 due to increases in purchases of guaranteed business loans. The portfolio consists of guaranteed loans outstanding, defaulted guaranteed business loans receivable, direct disaster loans and direct business loans receivables. Credit program receivables for the SBA are comprised of business and disaster direct loans and defaulted business loans purchased per the terms of SBA's loan guaranty programs which are offset by an allowance for subsidy. These credit program receivables were valued at \$9.1 billion in FY 2010 which was little variation from FY 2009. As reflected in **Chart III**, the biggest changes in the credit program receivables included a reduction in the direct disaster loans of \$392 million offset by an increase in the defaulted guaranteed business loans of \$337 million. As reflected in **Chart IV**, the defaulted guaranteed business loan receivables increased by \$2 billion because of a continued increase in purchases, and this was offset by an increase in the allowance on these receivables respectively. The increase in the allowance was in part because of a

reduction in the calculation of the projected recovery percentage in FY 2010 due to the continued effect of the economic recession. **Charts III and IV** depict that the credit program receivables decreased due to a decrease in direct disaster loans (there were no major disasters in FY 2010) and this was partially offset by an increase in defaulted guarantied business loans.

As reflected in **Chart V**, this increase in defaulted guarantied business loans resulted from increased purchases due to the continuation of the economic recession during FY 2010. Purchases of SBA's share of defaulted guarantied loans increased from \$3.9 billion in FY 2009 to \$4.8 billion in FY 2010.

SBA's assets and liabilities result primarily from its credit program activities. They consist of Fund Balances with Treasury, credit program receivables, liabilities for loan guaranties, and Debt with Treasury. SBA's loans and guaranties are financed by a combination of subsidy appropriations, fees charged to lenders and borrowers, and borrowings from the Treasury.

Congress provides appropriations to cover the estimated long-term costs of SBA's disaster loan approvals, while SBA's guarantied business loan program costs are largely financed through fees, augmented by appropriations for ARRA loans. These new loan costs are defined as the net present value of the estimated cash outflows and inflows associated with the loans. The remaining portion of each new direct loan disbursed is financed under permanent indefinite authority to borrow

CHART III TOTAL CREDIT PROGRAM RECEIVABLES

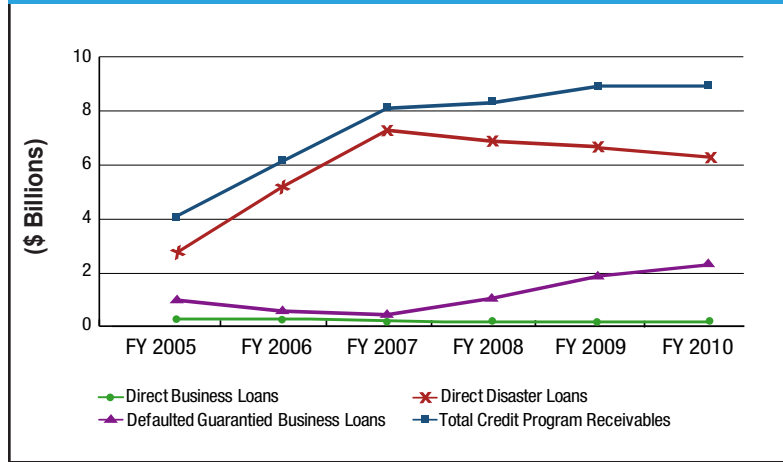


CHART IV CREDIT PROGRAM RECEIVABLES

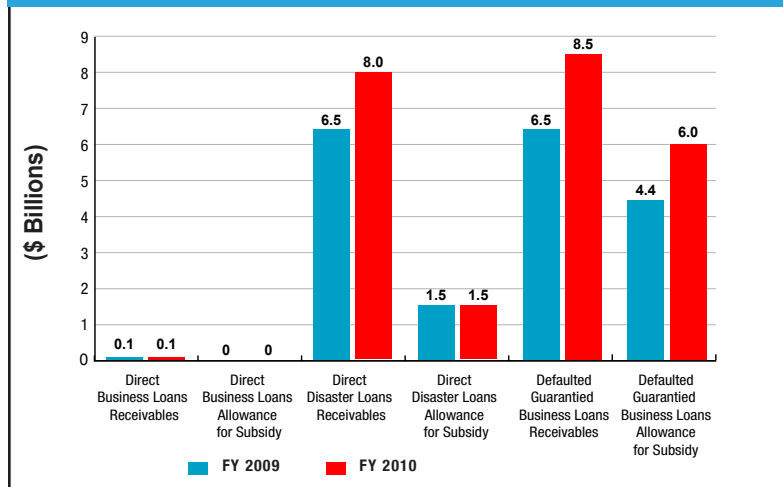
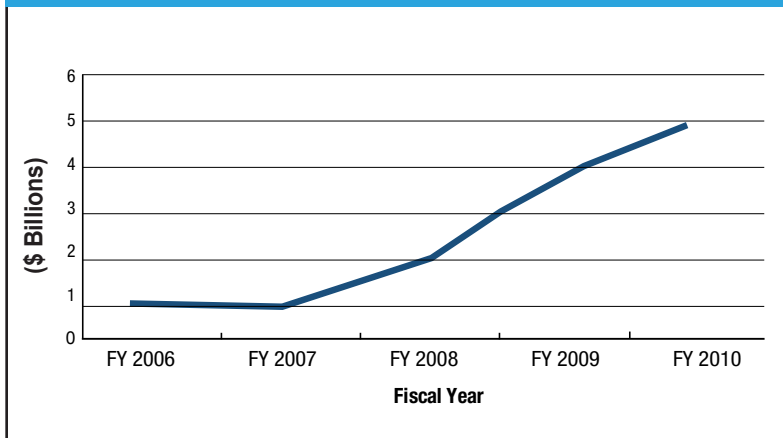


CHART V PURCHASES OF GUARANTIED LOANS



funds from Treasury's Bureau of the Public Debt. Borrowings are repaid to the Treasury as loans are repaid to the SBA.

Under the Credit Reform Act of 1990, the SBA is required to reestimate the subsidy cost through the life of each cohort of direct loans or loan guaranties to account for differences between the assumptions of cash flow and actual cash flow or revised assumptions about future cash flow. These reestimates represent additional costs or savings to the government and are recorded in the budget. Reestimates that indicate an increase in the subsidy cost are financed by permanent indefinite authority.

Financial Position

ASSETS

The SBA had total assets of \$15.2 billion at the end of FY 2010, up 20.6 percent from FY 2009. Assets increased primarily due to a \$2.6 billion increase in the Fund Balance with Treasury partially offset by a \$52 million decrease in Credit Program Receivables. The Fund Balance with Treasury increased primarily in the Loan Guaranty Financing Fund (\$2.2 billion). This increase consisted primarily of the collection of the prior year upward subsidy reestimate as well as FY 2010 subsidy (\$5 billion), collection of fees (\$386 million), collection of principal (\$856 million) and borrowings (\$1.2 billion). This increase was partially offset by purchases of defaulted loans in FY 2010 (\$4.8 billion). The decrease in the Credit Program Receivables is due to the reduction in the direct disaster loans portfolio. Per the provisions of the Federal Credit Reform Act of 1990, credit program receivables are valued at the present value of expected future cash flows.

LIABILITIES

The SBA had total liabilities of \$16.8 billion at the end of FY 2010, up 9.5 percent from FY 2009. Liabilities consist primarily of the Liability for Loan Guaranties and Debt with Treasury. The Liability for Loan Guaranties is defined as the estimate of the net present value of the future

amount the SBA will pay, net of fee collections, to liquidate expected purchases of guarantied loans under its guarantied loan programs. The Liability for Loan Guaranties increased \$472.4 million primarily due to the year end reestimate as well as subsidy and fees collected (offset partially by claim payments). There was a net upward reestimate of \$3.6 billion in the loan guaranty program at September 30, 2010. Refer to the following Results of Operations section which discusses the impact of the reestimates and to the chart in Note 6E of the financial statements which reconciles this account.

Debt with Treasury increased \$875.5 million as a result of borrowings to cover the increases in purchases of defaulted loans. Purchases of SBA's share of defaulted guarantied loans increased from \$3.9 billion to \$4.8 billion from FY 2009 to FY 2010. Due to this unexpected surge in purchases as a result of the continued effect of the economic recession, the SBA borrowed funds from Treasury to cover the purchases.

NET POSITION

Net position, which is the sum of Unexpended Appropriations and Cumulative Results of Operations, increased in FY 2010 to \$1.5 billion. Cumulative Results of Operations is the accumulated difference between expenditures and financing sources since the inception of the Agency. The loss shown as Cumulative Results of Operations decreased to \$3.8 billion at the end of FY 2010 (from \$4.7 billion last year) due to unfunded upward subsidy reestimates that decreased in FY 2010 on the 7(a) loan guaranty program from FY 2009. Unfunded expenses do not yet have a financing source. They result in an increase in the loss the SBA reports as Cumulative Results of Operations. The largest category of unfunded expenses at the SBA is year end reestimates which are funded in the following year. Unexpended Appropriations increased \$311.6 million this year because the appropriations used in FY 2010 were less than the appropriations received. This is primarily due to funding in the Small Business Jobs Act that appropriated SBA \$505 million to

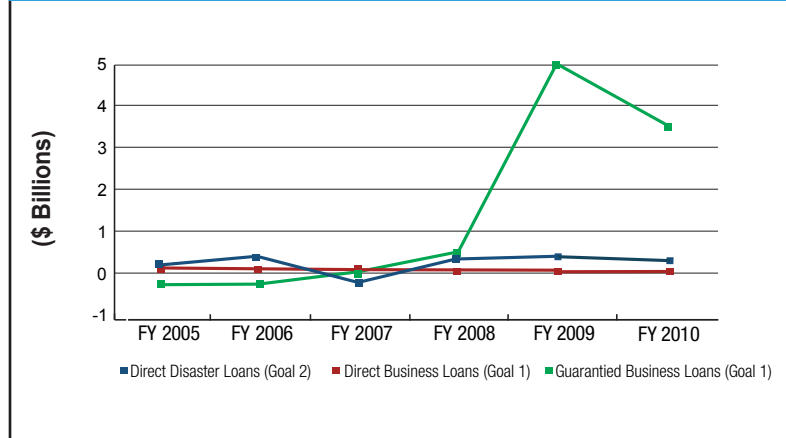
stimulate small business lending. These funds were appropriated but not disbursed at the end of the year, resulting in the increase in the unexpended appropriations balance.

Results of Operations

The Results of Operations primarily reflects the costs of SBA credit programs from subsidy expenses during the year for new loans and subsidy reestimates at year end. The credit subsidy cost is the net present value of expected cash inflows and outflows over the life of a guaranteed loan, or the difference between the net present value of expected cash flows and the face value of a direct loan. The SBA receives appropriations annually to fund its credit programs. When loans are disbursed, the SBA records subsidy expense. In accordance with the Federal Credit Reform Act, the subsidy costs are reestimated annually. Reestimates update original loan program cost estimates to reflect actual experience and changes in forecasts of future cash flows. Increased reestimated costs are funded in the following year by permanent indefinite authority, while decreased costs are returned by the SBA to a Treasury general fund. During FY 2010, the net reestimated costs for the 7(a) and the SBIC Participating Securities programs decreased (guaranteed business loan program, Strategic Goal 1) compared to FY 2009. Those decreases were the largest components of the change (net decrease) in the Agency's net cost.

Chart VI reflects the decreases in the reestimates for the Disaster direct programs as well as the

CHART VI CREDIT PROGRAM SUBSIDY REESTIMATES



guaranteed business loan program from FY 2009 to FY 2010.

The decrease in the overall Net Cost from FY 2009 to FY 2010 in Strategic Goal 1: *Drive business formation, job growth and economic expansion, particularly in under-served markets* (formerly Expand America's ownership society, particularly in under-served markets), is primarily due to the decrease in the upward reestimates for the business loan guaranty programs. The same decrease also applies in Strategic Goal 2: *Provide timely financial assistance to homeowners, renters, nonprofit organizations and business affected by disaster*, for the Disaster direct programs. While there were still significant upward reestimates in both of these programs (composing the majority of the FY 2010 Net Cost), the upward reestimates were less this year than in FY 2009.

Strategic Goal 1 includes significant upward reestimates in the 7(a) Loan Guaranty program, the 504 CDC program, as well as the SBIC program. The 7(a) Loan Guaranty program, SBA's flagship and largest program had a net upward reestimate in FY 2010 of \$1.5 billion. While the 2009 cohort performed better than expected in FY 2010, many earlier cohorts performed worse. Actual cohort performance, in particular performance of the 2005-2008 cohorts, made up a significant portion of the reestimate. The remainder of the reestimate was mostly due to updated model assumptions and methodologies, which will allow for more accurate projections of future cash flows. These methodology changes in recognition of the economic times resulted in increased purchase projections for the remaining years within the cohorts.

Similarly, the 504 Certified Development Companies program had a net upward reestimate of \$1.6 billion. While the 2009 cohort performed better than expected in FY 2010, many earlier

cohorts performed worse. The majority of the reestimate was due to updated model assumptions and methodologies, which will allow for more accurate projections on future cash flows. These methodology changes resulted in increased purchase projections and decreased recovery projections for the remaining years within the cohorts. The remainder of the reestimate was mostly due to higher than projected purchases in FY 2010, in particular for cohorts 2005-2008.

The SBIC Debentures program had a net upward reestimate of \$40 million. The reestimate was mostly due to lower than projected recoveries during FY 2010 and a decrease in projected recoveries for the remaining years within the cohorts.

The SBIC Participating Securities program had a net upward reestimate of \$337 million. The reestimate was mostly due to the downturn in the economy that resulted in lower than projected recoveries and higher than projected purchases during FY 2010 and an increase in projected purchases for the remaining years within the cohorts.

The 504 ARRA program had a net upward reestimate of \$156 million despite better than projected performance in FY 2010. The reestimate was due in large part to updated model assumptions and methodologies, which will allow for more accurate projections of future cash flows. These methodology changes resulted in increased purchase projections and decreased recovery projections for the remaining years within the cohorts.

Strategic Goal 2 includes a new upward reestimate in the Disaster direct loan program at year-end. The Disaster program had a net upward reestimate of \$161 million primarily in the 2006 cohort, which mostly consists of loans for the Gulf Coast hurricanes of 2005. Loans in the 2006 cohort currently account for about 56 percent of the outstanding portfolio of direct disaster loans. The upward reestimate was primarily the result of performance probabilities being updated with actual performance during

FY 2010 that resulted in an increase in projected defaults.

BUDGETARY RESOURCES

Total Budgetary Resources increased \$6 billion from FY 2009 to FY 2010. This increase consists of increases in Spending Authority from Offsetting Collections and Appropriations Received. Spending Authority increased \$3.7 billion from FY 2009 to FY 2010. The increase in Spending Authority is due to the collections of the FY 2009 upward reestimates in the loan guaranty financing fund in FY 2010. Upward reestimates are funded in the following year after the accrual in the financial statements.

Appropriations Received increased \$3.5 billion from FY 2009 to FY 2010. The increase in Appropriations Received is mainly the increase in Spending Authority discussed previously and is the result of the receipt of appropriations for upward reestimates during FY 2010. The SBA received funding for the FY 2009 upward reestimate in FY 2010. Appropriations Received was also increased due to appropriations provided by the Small Business Jobs Act in September 2010 as well as the extensions for the Recovery Act (FY 2009 was similarly affected by ARRA appropriations in February 2009). **Chart VII** depicts that the substantial increase in Appropriations Received is for business loans due to the upward subsidy reestimate.

STATUS OF BUDGETARY RESOURCES

Total Status of Budgetary Resources increased \$6 billion from FY 2009 to FY 2010. Obligations incurred in the budgetary funds increased \$3.1 billion due to the transfer of the FY 2009 upward reestimate to the financing funds. This is consistent with the increase in Appropriations Received discussed previously. Obligations increased in the nonbudgetary financing funds by \$334 million. This consisted of an increase of \$592 million in the guaranty financing fund offset partially by a decrease of \$258 million in the direct loan financing fund. The increase in the obligations of the guaranty financing fund is consistent with the

increase in purchases of defaulted guaranteed loans. The decrease in the obligations in the direct loan financing fund is consistent with the decrease in credit program receivables.

Unobligated balances at September 30, 2010 and 2009 are \$5.2 billion and \$2.7 billion which include \$3 billion and \$1.3 billion of unavailable unobligated balances. These balances are unavailable because they are unapportioned by OMB. The SBA accumulates the majority of these unobligated balances in its nonbudgetary financing accounts during the fiscal year (\$3.5 billion in FY 2010 and \$1.2 billion in FY 2009) from reestimates of subsidy costs for the life of each cohort of direct loans and loan guaranties. In addition, unobligated balances are accumulated in budgetary accounts from appropriations (\$1.8 billion in FY 2010 and \$1.5 billion in FY 2009) that are used to finance SBA's ongoing program operations.

Operational Portfolio Analysis

The SBA is the taxpayers' custodian of a loan portfolio of \$93.3 billion to small businesses, as shown in **Chart VIII**. This portfolio of outstanding principal loan amounts includes both guaranteed and direct business loans as well as direct disaster loans. SBA's two flagship guaranty business loan programs, 7(a) and 504, comprise roughly 80 percent of the outstanding loan portfolio. The direct disaster loan portfolio has steadily shrunk by nearly a billion dollars in the past four years as the United States

CHART VII APPROPRIATIONS RECEIVED

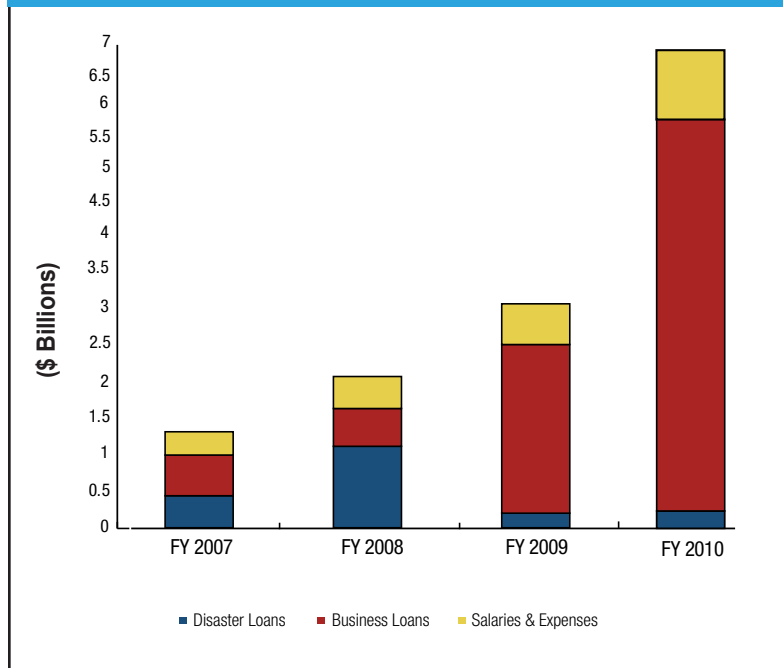
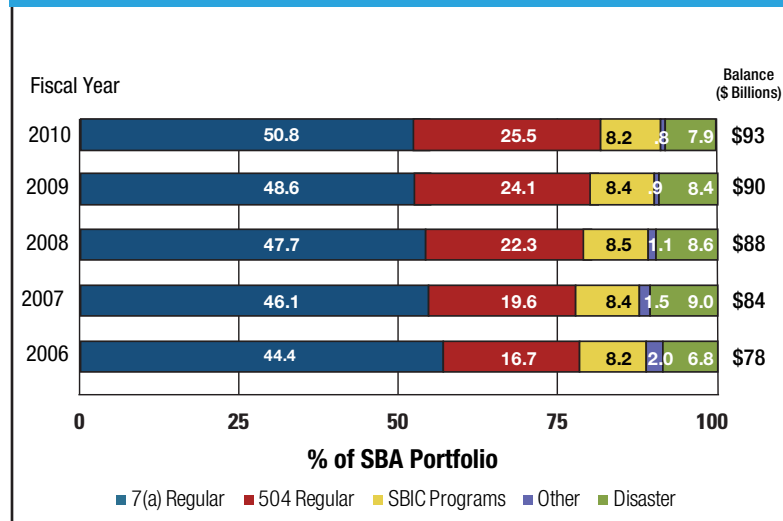


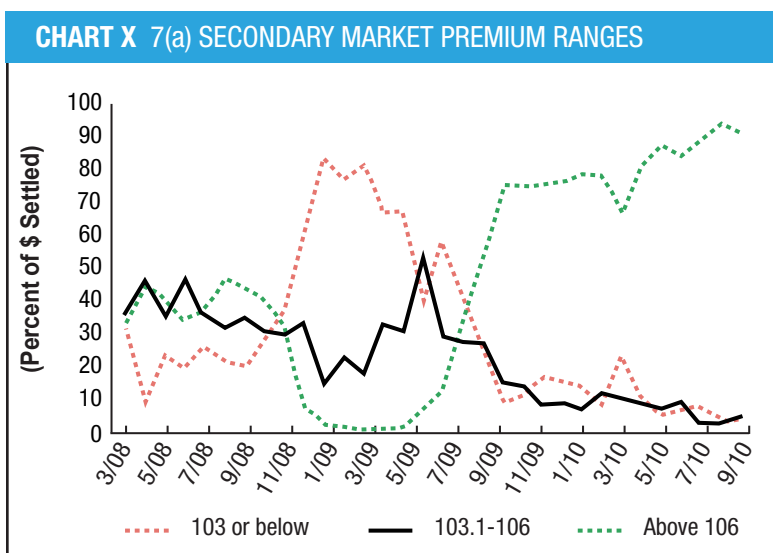
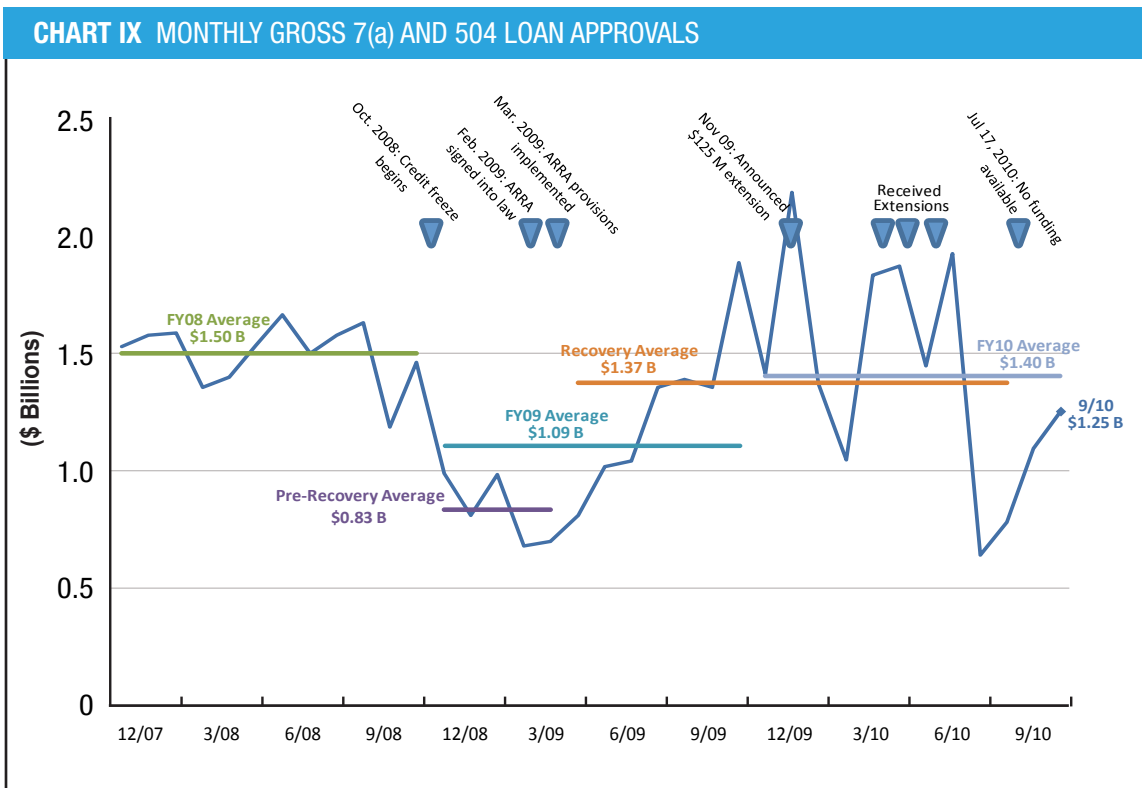
CHART VIII SBA OUTSTANDING LOAN PORTFOLIO



has largely avoided major hurricanes like those of 2005 and 2006 (Katrina, Rita and Wilma). The Deepwater Horizon oil spill in the Gulf of Mexico during FY 2010 did not result in a large increase in the disaster portfolio, most likely because small business owners are turning to the BP compensation fund first for their damaged businesses. According to a bi-annual survey conducted by the National Small Business Association, the SBA's loan products reach around 4 percent of small businesses in need of financing.

The 7(a) and 504 loan programs continue to drive the growth of the overall loan portfolio. In FY 2010, they accounted for all the growth in the portfolio, growing at a rate of 5 percent while the other programs contracted by 4.5 percent, leading to an overall portfolio rate of 3.2 percent. The most likely explanation for 7(a) and 504's popularity can be found in the month-by-month loan approval snapshot shown in **Chart IX**. The American Recovery and Reinvestment Act, passed in February 2009, contained several provisions for the flagship

programs that increased lending. First, the Recovery Act temporarily allowed the SBA to eliminate fees for borrowers on 7(a) loans and for both borrowers and lenders on 504 Certified Development Company loans. Second, the Recovery Act allowed the SBA to raise the guaranty on 7(a) loans up to 90 percent. Combined, these



two provisions made SBA loans cheaper for borrowers and lenders alike as well as less risky for lenders fearful of risk after the financial crisis of 2008. High demand for loans with Recovery Act fee relief and guaranty enhancement drained the entire amount appropriated for these loans by November 2009, nearly a year before the Recovery Act ended. Thus, over the course of FY 2010, the SBA received four extensions of Recovery Act provisions from Congress and, as seen in **Chart IX**, demand surged

with each extension and fell with every shortage. In the final week of FY 2010, Congress passed the Small Business Jobs Act which made these Recovery Act provisions permanent, along with other changes like higher loan size limits.

Loan Demand and Supply Revisited

In last year's Operational Portfolio Analysis, the relationship between loan supply (willingness of banks to lend) and loan demand (willingness of businesses to take on a loan) was highlighted. It was noted that a tight supply combined with weak demand had led to a slowdown in the number of loans approved. Furthermore, the Agency predicted that, as more current data become available, it is likely that the SBA will see the effects of the Recovery Act provisions to waive borrower fees and increase SBA loan guaranties on this loan equation. Reduced fees, a bottoming-out of the housing market, and a rebounding in the general economy will strengthen demand for small business loans while the decrease in risk associated with the higher loan guaranty will lead to an expansion of supply from banks. **Chart IX's** shape of the loan approvals pre- and post-extension of Recovery Act provisions strongly suggests that the SBA was correct regarding the latter half of the prediction. The demand on the secondary market for 7(a) loans became so high over the course of the year that, while zero loans made in January or February 2009 (pre-Recovery Act) sold at a 106 premium or above, in September 2010, 95 percent of the loans settled

CHART XI NET PERCENTAGE OF DOMESTIC RESPONDENTS TIGHTENING STANDARDS FOR COMMERCIAL AND INDUSTRIAL LOANS

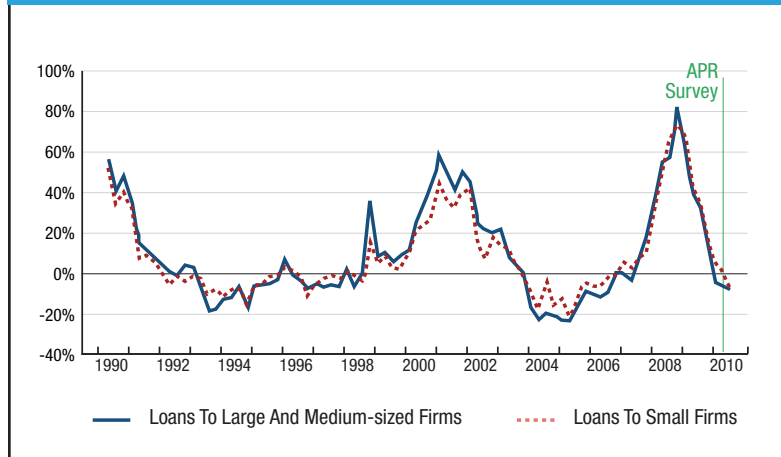
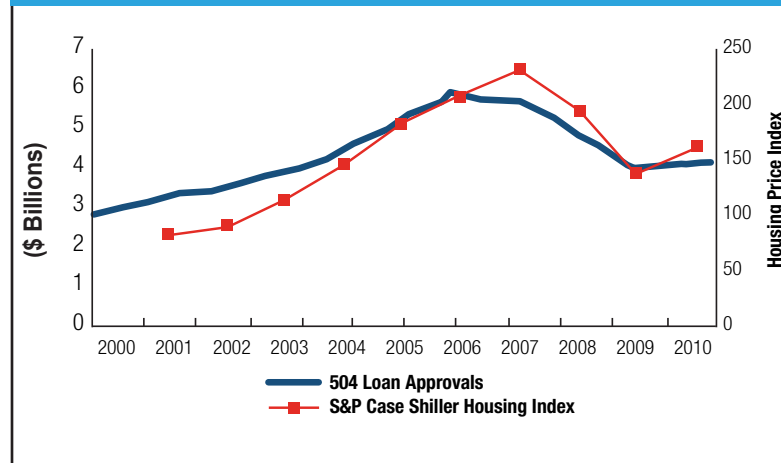


CHART XII S&P CASE-SHILLER HOUSING INDEX & SBA 504 LOAN APPROVALS



representing 94 percent of the total dollars were sold at or above premiums of 106 as seen in **Chart X**. In fact, 70 percent of the loans settled at 109.1 or more, indicating that investors saw great worth in the securitized bundles of 7(a) loans.

The changes to 7(a) and 504 accompanying the Recovery Act are probably a strong reason why the number of banks using SBA products has jumped 27 percent in the past two years. While banks may have found SBA's products particularly enticing, the Senior Loan Officer Opinion Survey, conducted quarterly by the Federal Reserve Board, shows the abrupt tightening of credit standards for all banks to small firms when the financial crisis began eased throughout 2010 and standards were even loosening by the summer of 2010, as evidenced by **Chart XI**.

However, the SBA expects continued depressed demand for loans from small businesses will hinder stronger growth in the loan portfolio. The decline is caused in large part by the mid-dling economy and muddled housing market. As evidenced by **Chart XII**, for years the SBA loan approval volumes have closely tracked the Case-Shiller National Housing Price Index. Many first-time entrepreneurs use the equity they have built in their houses as the collateral for their small business loans. As that equity shriveled with the burst of the housing market bubble in 2007, demand for loans had a corresponding decline. A deeper examination of the regional data for SBA shows the correlation's strength. Of the nine metropolitan areas that have had the deepest continued decline in home prices from their peak, SBA's corresponding district office has registered the steepest drop in loan demand from FY 2006 to FY 2010 — six offices rank in the top ten and all nine register in the top twenty. With the housing crisis now entering into a foreclosure crisis, the negative effects of a weak housing market on loan demand will likely persist for the foreseeable future.

The value of housing is only a part of the story however stagnation in the broader economy continues to result in lower demand for loans as small businesses postpone plans for expansion or large investments. According to the October 2010 Small Business Economic Trends survey published by the National Federation of Independent Business, a record 53 percent of small businesses reported no need for a loan. In fact, only 3 percent listed financing as their number one business problem; weak sales dominated their business concerns. A survey conducted by the National Small Business Association in July 2010 points to the long-term effects of this concern: over 80 percent of those businesses surveyed projected no growth opportunities for their firms in the next six months. Thus, hiring additional employees or making big investments will be delayed. The consumer Confidence Index similarly tracks this mid-dling economic condition, with confidence rates hovering in the mid-50s throughout FY 2010 as

compared to around 110 in FY 2007. The lack of confidence both by businesses and consumers creates a circle of stagnation since businesses remain unoptimistic about expanding and hiring, while consumers wait to spend and bring revenue to these businesses.

In the equation of loan supply and demand, the demand for loans will likely drive depressed loan volumes. Policy changes in the past two years attracted lenders to SBA loans, but only a renewed confidence in the future will allow the demand for loans to meet the supply again.

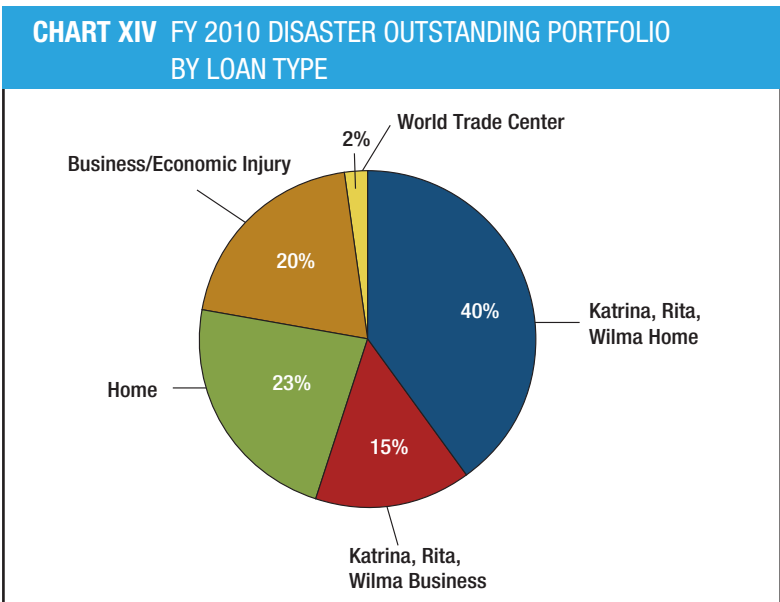
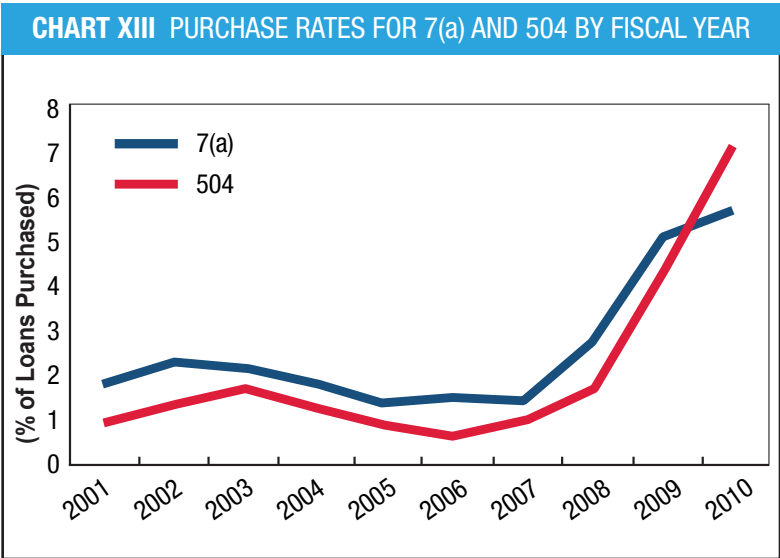
Default and Recovery Rates in Times of High Unemployment

Each year the SBA uses a variety of sophisticated econometric models that employ a variety of economic behavior pattern models as well as the economic assumptions released by the White House. These models predict the amount of SBA outstanding loans and loan guaranties taxpayers will pay over the life of a loan cohort, namely all loans made that fiscal year. At the same time the SBA estimates the amount for the upcoming fiscal year cohort it also reestimates all previous outstanding cohorts to adjust the model with the new data accumulated over the past year and the White House's new economic assumptions. In FY 2010, the SBA had a higher than normal reestimate of \$3.6 billion. This reestimate has several notable characteristics. First, it was necessary to factor in an unprecedented continuing period of high unemployment for the models, and the effects of purchase rates on defaulted loans remained uncertain. They were higher than expected (see **Chart XIII**), but now that there are two years of data, the SBA will attune future models more closely to the negative effects of continued high unemployment. Second, 80 percent of the reestimate occurred because of worse than expected performance in loans originated in FY 2005-2008. Traditionally, loan cohorts in their third to fifth year of repayments are most likely to default or run into trouble, but the effect this time was probably magnified because of the looser underwriting

procedures and credit standards by lenders prevalent in that time period. Also, many of the loans from those years were from the various SBA Express programs which traditionally have lower recovery rates post-default. Although SBA's models do not account for the value of a loan's collateral (the bank determines a loan's collateral), the FY 2005-2008 loans likely used real estate with inflated prices as collateral. As the housing market settles to a new level, recovery rates will likely lower for those particular cohorts, since their collateral decreased in value from the time of loan origination. Due to the Recovery Act and its extensions, loans made in the previous two fiscal years by the SBA have had higher guaranties than previously. To counter the risk associated with higher guaranties, the SBA altered the financial models accordingly with higher subsidies to take into account the increased exposure to individual loan performance.

Disaster

SBA's portfolio of direct disaster loans has declined in volume by over a billion dollars in the past 4 years, dropping from \$8.96 billion in FY 2007 to \$7.93 billion by the end of FY 2010. The three hurricanes of FY 2006 – Katrina, Rita and Wilma – continue to compose the greatest portion of the outstanding disaster portfolio, \$4.39 billion or 55 percent of the



total as seen in **Chart XIV**. By comparison, the three costliest disasters of FY 2010 – the Tennessee floods, the Rhode Island/Massachusetts floods, and the BP oil spill – led to only \$272.21 million of gross loan approvals. It is likely that the BP compensation fund set up to help businesses affected by the Deepwater Horizon disaster led to a lower-than-expected amount of SBA disaster loans for the same event. As long as the United States continues to avoid major disasters, a decline in the overall portfolio is a welcome and expected trend.

Analysis of SBA's Systems, Controls and Legal Compliance

Internal Control Environment

INTERNAL CONTROL

The SBA believes that maintaining integrity and accountability in all programs and operations is critical for good government, demonstrates responsible stewardship over assets and resources, ensures high quality, is a sign of responsible leadership, ensures the effective delivery of services to customers, and maximizes desired program outcomes. The SBA has developed and implemented management, administrative and financial system controls to reasonably ensure that:

- programs and operations achieve intended results efficiently and effectively;
- resources are used in accordance with the mission of the Agency;
- programs and resources are protected from waste, fraud and mismanagement;
- program and operations activities are in compliance with laws and regulations; and
- reliable, complete and timely data are maintained and used for decision-making at all levels.

The Federal Managers' Financial Integrity Act of 1982 requires federal agencies to conduct an annual assessment of internal control and report the results to the President. The conclusion of the Administrator's Annual FMFIA assurance statement is based on the self-assessment of program managers, internal control reviews, and audits and reviews done by the Government Accountability Office and the SBA's Office of the Inspector General.

The SBA continues to strengthen and improve the execution of its mission through the application of sound internal controls. The Office of Internal Controls is responsible for implementing the requirements of the Office of Management and Budget's revised Circular No. A-123, Appendix A,

Internal Control Over Financial Reporting. The OIC conducted SBA's sixth annual assessment of internal control over financial reporting to comply with this circular. The revised A-123 requires the managers of federal agencies to take the responsibility for assessing internal controls over financial reporting similar to that imposed on publicly traded companies by the Public Company Accounting Reform and Investor Protection Act of 2002 (the "Sarbanes-Oxley Act" or "SOX").

The Senior Assessment Team, chaired by the Chief Financial Officer and comprised of SBA managers from the major programs and support offices, directed this effort. The OIC reviewed the key business processes impacting financial operations and the financial statements. In addition, the SAT members reviewed some of the business processes with no material impact on the financial statements, but which have some potential for risk or exposure for the Agency.

Based on the evaluation of 14 business processes, the OIC identified a number of deficiencies in the internal control over financial reporting, including several in SBA's key business areas. However, the OIC determined that most of the items were relatively minor and one reached the level of significant deficiency.

In addition, OIC also performed a review of the Sacramento Loan Processing Center to help the Office of Capital Access determine the effectiveness and efficiency of the internal controls in place for loan approvals made under the American Recovery and Reinvestment Act of 2009. All deficiencies noted were minor and none reached the level of significant deficiency.

Given the size of its \$93 billion loan portfolio, the SBA's lender and loan monitoring and review activities represent a critical component of the Agency's internal control framework. The Agency's Office of Credit Risk Management rates

lenders that disburse SBA-guaranteed loans according to risk. This analysis allows the SBA to focus resources on those lenders that represent the most risk in terms of exposure and credit quality. Larger lenders are subject to periodic on-site reviews. Other lenders are on a case by case basis. The SBA also conducts reviews of Certified Development Companies, examinations of Small Business Investment Companies, guaranteed loan purchase reviews and reviews of improper payments for business and disaster loans.

LEGAL COMPLIANCE

The SBA's independent auditor has identified one instance of non-compliance with applicable laws and regulations as of September 30, 2010. Due to a system error, 473 of 8,229 charged-off disaster loans, or 5.7 percent were not referred to Treasury for cross-servicing and for the Treasury offset as required by the Debt Collection Improvement Act. This represents \$11.3 million of the \$247.5 million disaster loans charged-off in FY 2010, or 4.6 percent. The system issue has been identified and is in the process of being remedied and a mitigation plan has been developed to ensure that this issue will not recur. All loans eligible for Treasury referral will be referred within the next six months. In FY 2009, through the SBA's self-assessment process it was identified that the Agency was not referring non-disaster loans for the Treasury off-set program; this was corrected in FY2010. There were no issues identified in the testing of the improved internal controls over non-disaster loans by both our independent auditors and our OMB A-123 team in the current year and we anticipate the same successful resolution for the disaster loans in FY2011.

AUDIT FOLLOW-UP

SBA's OIG conducts audits and reviews of the Agency's operations, and the Office of the Chief Financial Officer works closely with SBA management and the OIG to complete actions necessary to respond to OIG audits. The OCFO tracks the completion of these audit recommendations, and posts the status of all open OIG recommendations on the SBA's Intranet for managers'

information. In addition, the Agency's financial and program-related internal control has improved substantially over the years through the remediation of audit recommendations made by the Agency's independent auditor in the annual financial statements audit. Finally, the SBA also considers and responds to recommendations from audits and reviews conducted by the GAO.

During FY 2010, the OCFO continued to strengthen internal control over financial reporting and credit subsidy cost modeling through additional quality assurance procedures for validating loan program data at key points. The SBA also continued to strengthen its financial management team through communication on emerging issues and training activities.

INFORMATION SYSTEMS

This year the SBA continued to have a significant deficiency in the information technology security controls—including access controls, segregation of duties, software configuration and security management. The Agency is sensitive to the need to protect SBA data, and plans to work diligently to improve both process and performance in this critical area. The following steps to remediate findings pointed out in the Auditors' Report are currently underway:

- **Continuous Monitoring:** SBA's IT Security team in the Office of the CIO (OCIO), under the direction of the Chief Information Officer, has begun fiscal year 2011 with a rigorous weekly session that includes reports and evaluation by an OCIO team on the critical success factors (CSFs) that underlay IT security, and key performance indicators for each CSF.
- **Enterprise Change Control:** SBA's Change Manager has convened a working group of cross-SBA IT system owners to implement a delegated-authority Enterprise Change Control Board which will mitigate the FY10 finding that concluded a non-inclusive control over changes in SBA's IT infrastructure.

- **Configuration Management:** SBA's OCIO has begun a project to define and implement a configuration management database to account for and include all IT system assets.
- **Tracking of Plans of Action and Milestones (POAMs):** SBA's OCIO now incorporates POAMs for all SBA IT systems in the Agency's Audit Tracking system, with triggers to identify POAM vintages and milestones. The Audit Tracking system is reviewed with IT Security and system owners on a weekly basis.
- **Data Loss Protection:** SBA has invested in a leading data loss protection forensic tool and has configured it to sense and block all exports of personally identifiable information, as well as controlled unclassified information.
- **Network Access Control:** the SBA is promulgating a new policy that blocks connection of non-SBA government equipment to the SBA infrastructure.
- **IT Security role-based training:** in order to promote a program of continuous training for IT system owners, security managers, and associated personnel, SBA's OCIO is implementing a monthly "IT Security Officer (ITSO)" joint meeting, led by SBA's Chief Information Security Officer (CISO). The monthly ITSO meeting will bring together system owners and those with associated roles in order to conduct training.
- **Log correlation and analysis:** the SBA has invested in software sensors and log extraction software in order to collect, compile, and statistically analyze critical server logs. The analysis will be used to discover patterns in user and server activity that may point to non-standard network practices, and direct follow-on forensic activity.

Success Story



"Fishing" for Business While Overcoming Adversity

Tommy's Seafood Inc. New Orleans, Louisiana

Louisiana small business owners Tommy and Maria Delaune suffered a one-two punch from Hurricane Katrina and the Deepwater BP oil spill. They run Tommy's Seafood, a New Orleans seafood processor and wholesaler with 20 employees.

When Hurricane Katrina hit in August 2005, the business suffered major damage at its two facilities, including loss of equipment and inventory. They applied for an SBA disaster loan in October 2005, and the loan was approved seven months later. But the loan for \$960,000 wasn't fully disbursed until October 2006, a year later.

The SBA overhauled the disaster loan program after the 2005 Gulf Coast hurricanes. Staff increases, improved technology and training, and a streamlined loan process resulted in vast improvements. The needs of disaster victims are now being met more efficiently.

Tommy's Seafood got hit again in April 2010 when the Deepwater BP oil spill forced closures of fishing waters in the Gulf of Mexico, where their suppliers work. Tommy and Maria had to look 500 miles away to find more seafood to process, so they had higher expenses and lower profit margins. This time around, however, their experience with the SBA was "amazing," according to Maria. Their Economic Injury Disaster loan for \$460,900 was approved in 16 days, and it was fully disbursed just a month later. In addition, the SBA deferred their existing Katrina loan for 12 months, allowing them to use more of their resources to deal with the financial strain caused by the oil spill.

Summary of Financial Statement Audit and Management Assurances

As required by OMB Circular A-136, Section II.5.6, the following summarizes SBA's financial statement audit and SBA's Management Assurances:

Summary of Financial Statement Audit

Audit Opinion	Unqualified					
Restatement	No					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Financial Reporting	1	0	1	N/A	N/A	0

Summary of Management Assurances

Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)						
Statement of Assurance	Unqualified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Financial Reporting	1	0	1	N/A	N/A	0
Effectiveness of Internal Control over Operations (FMFIA § 2)						
Statement of Assurance	Unqualified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None	0	0	N/A	N/A	N/A	0
Conformance with financial management system requirements (FMFIA § 4)						
Statement of Assurance	Systems conform to financial management system requirements.					
Non-Conformances	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None	0	0	N/A	N/A	N/A	0
Conformance with Federal Financial Management Improvement Act (FFMIA)						
				Agency		Auditor
Overall Substantial Compliance				Yes		Yes
1. System Requirements					Yes	
2. Accounting Standards					Yes	
3. USSGL at Transaction Level					Yes	

FMFIA and FFMIA Assurance Statement for FY 2010


The Small Business Administration continued to strengthen the internal controls over its programs and operations during FY 2010. Creating a culture of responsibility and accountability while eliminating and preventing waste, fraud and abuse is critical to meeting our mission at the SBA. I am pleased to report that the SBA is on course to achieve its internal control objectives.

SBA management is responsible for establishing and maintaining effective internal controls and financial management systems that meet the objective of the Federal Managers Financial Integrity Act. The SBA conducted its assessment of the effectiveness of internal controls over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with OMB Circular A-123, Management's Responsibility for Internal Control. Agency managers have issued assertions as to the status of their FY 2010 internal controls, and these assertions are supported by internal testing, checklists and other management reviews. Although Agency managers reported some operating deficiencies, these were not of a material nature. Based on the results of this evaluation, I can provide reasonable assurance that internal controls were operating effectively and no material weaknesses were identified in the design or operation of internal controls.

In addition, the SBA conducted its assessment of the effectiveness of internal controls over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations, in accordance with the requirements of Appendix A of OMB Circular A-123. Based on the results of this evaluation, I can provide reasonable assurance that internal controls over financial reporting were operating effectively and no material weaknesses were identified in the design or operation of internal controls over financial reporting.

SBA's independent auditors issued an unqualified opinion on the Agency's FY 2010 financial statements for the sixth year in a row. However, our auditor identified one instance of non-compliance with applicable laws and regulations as of September 30, 2010. Due to a system error, 473 of 8,229 charged-off disaster loans, or 5.7 percent, were not referred to Treasury for cross-servicing and for the Treasury offset as required by the Debt Collection Improvement Act. This represents \$11.3 million of the \$247.5 million disaster loans charged-off in FY 2010, or 4.6 percent. The system issue has been identified and is in the process of being remedied and a mitigation plan has been developed to ensure that this issue will not recur. All loans eligible for Treasury referral will be referred within the next six months. In FY 2009, through SBA's self-assessment process it was identified that the Agency was not referring non-disaster loans for the Treasury off-set program; this was corrected in FY 2010. There were no issues identified in the testing of the improved internal controls over non-disaster loans by both our independent auditors and our OMB A-123 team in the current year and we anticipate the same successful resolution for the disaster loans in FY2011.

The Federal Financial Management Improvement Act requires federal agencies to implement and maintain financial management systems that are in substantial compliance with federal financial management systems requirements, federal accounting standards, and the United States Government Standard General Ledger. The SBA provides reasonable assurance that its financial management systems substantially comply with FFMIA for FY 2010.



Karen Gordon Mills
Administrator
November 15, 2010

Improper Payments Summary

The Improper Payment Information Act of 2002 requires that agencies: (1) review programs and identify those susceptible to significant improper payments; (2) report to Congress on the amount and cause of improper payments; and (3) develop approaches for reducing such payments. Appendix C to OMB Circular A-123 provides additional guidance on agency compliance with IPIA requirements. In addition, OMB Circular A-136 provides guidance on the form and content of IPIA reporting. Finally, the Improper Payment Elimination and Recovery Act enacted in July 2010, effective in FY 2011, places additional emphasis on improper payment improvement. SBA's improper payment program and reporting is subject to this guidance.

SBA's four major credit programs are currently included under IPIA reporting. They are the 7(a) business loan program, the Section 504 Certified Development Company loan program, the Small Business Investment Company program and the Disaster Assistance loan program. SBA's risk assessment of the 7(a), 504, and SBIC guaranty approval programs for improper payment indicate a low level of risk, due to the internal controls applied in these programs, and improper payments are extremely low or nonexistent. The SBA considers the 7(a) guaranty purchase program to have a medium risk of improper payments due to the delegation of program authority to SBA's lending partners in this nationwide program. The Disaster program has a low risk of loss, but improper payment reviews have found that compliance with the paperwork required in Disaster program lending procedures needs improvement.

The SBA Inspector General issued audit reports on the 7(a) Guaranty Purchase (July 2009) and Disaster Improper Payments (March 2009). As a result of findings and recommendations in these reports the SBA has changed its methodology used in both of these programs in the sampling and testing for improper payments. This further resulted in an increase of the improper payment rates and dollars found in FY 2009.

The 7(a) guaranty purchase operation includes centers in Herndon, Virginia, Fresno, California, and Little Rock, Arkansas that report to headquarters in Washington DC. The FY 2010 7(a) guaranty purchase improper payment rate was determined to be 1.87 percent or \$44.8 million compared with last year's improper payment rate of 3.81 percent. The Disaster program operation includes a processing center in Fort Worth and operation centers in Atlanta and Sacramento, as well as a Buffalo customer service center. The FY 2010 Disaster improper payment rate was determined to be 34.2 percent or \$127.1 million compared to 20.9 percent reported last year.

The 7(a) guaranty purchase review contains a number of judgmental considerations concerning whether the originating lender exercised reasonable commercial care and prudence in the execution, servicing and liquidation of the loan in accordance with SBA loan program requirements; and whether or not the lender's actions or inactions have placed the SBA at financial risk or contributed materially to the loan default. The evaluation of the lender's exercise of reasonable commercial lending practices is critical and needs to be consistent with the lending practices exercised related to loans that did not default. The exercise of this judgment is critical to the viability of the 7(a) program as lenders can choose whether or not to participate in the 7(a) program and is especially relevant since over 85 percent of SBA 7(a) loans are approved by lenders using delegated authority where they make the credit underwriting decisions.

Disaster improper payments are generally the result of loan documentation errors and do not result in a disaster victim receiving funds that they are not eligible to receive. Further, the disaster loan program operation has a built in recovery system in that the majority of loans made are collateralized and all loans have to be repaid, and SBA's loan servicing and liquidation operation attains maximum recovery. The increased rate in FY 2010 indicates a need to adhere to the documentation requirements of SBA's Standard

Operating Procedures. Additional training has been instituted to ensure that staff is aware of all paperwork requirements and waiver procedures when appropriate. Also, a dedicated team that reports directly to SBA headquarters will complete the annual Improper Payment review and continuously review the work of the Production and Disbursement Center in Fort Worth. Finally, areas of concern will be identified and corrected in a timely manner.

In accordance with OMB guidance, the SBA includes loan guaranty approvals issued during FY 2010 in its Improper Payment program reporting for its 7(a), 504 and SBIC programs. Although these guaranties haven't yet resulted in federal outlays, they possibly could in the future and they are therefore included. Most frequently, the reason for an improper payment in this category would be the lack of appropriate eligibility or a non-compliance with lending procedures. The result of SBA's testing for 7(a) and 504 guaranties issued

in FY 2010 indicated a zero percent improper payment rate for both programs. The SBIC program testing found three potential improper payments where excessive prepayment penalties were not approved by SBIC program officials as required (although they may have been approved if the SBIC had requested approval) for 0.99 percent or \$14.6 million when extrapolated.

In summary, the SBA places a top priority on the detection and remediation of improper payment occurrence. The 7(a) guaranty purchase, SBIC and Disaster loan programs have staffs that monitor and review their operations for improper payments and implement improvements. In addition the SBA provided additional staff during FY 2010 to support its internal controls over financial management activities in accordance with OMB Circular A-123 requirements. These resources will be applied to future improvement of the SBA's Improper Payment program.

*Did
you
know*

What do Intel, FedEx and Outback Steakhouse have in common? They all received SBA assistance. Learn about the SBA Investment Division at <http://www.sba.gov/aboutsba/sbaprograms/inv>.

FINANCIAL REPORTING

Success Story



Successful Entrepreneur Cites Military Experience Hughes Group, LLC, Lakewood, Washington

Patrick L. Hughes, owner and managing member of Hughes Group, LLC turned 28 years of military experience into a thriving business.

The veteran-owned company, established by Hughes in 1999, is an SBA 8(a) and HUBZone-certified firm, and is classified as a service disabled veteran-owned small business. The company provides aircraft, administrative and training, integrated logistics and information technology solutions to the armed forces and business community. Its wide range of

services to the federal government and major private sector companies includes aircraft refueling and maintenance, postal services, personnel placement, property book management, food services, web hosting and design, and help desk support. “Because of my military experience I have been able to grow the business into eleven states,” reports Hughes.

Hughes was honored by the SBA as the 2010 National Minority Small Business Person of the Year at the 28th annual National Minority Enterprise Development (MED) Week conference in Washington, D.C. “We are honoring the Hughes Group today for its extraordinary commitment to excellence in providing innovative products and services to the federal government and commercial markets,” said SBA Administrator Karen G. Mills. “Mr. Hughes’ commitment to excellence has made his small business the third fastest growing minority business in Washington state and has helped spur job creation in the small business community and the nation’s economy.” Mr. Hughes is the recipient of SBA loans made possible by the Recovery Act of 2009.

Message from the Chief Financial Officer

November 15, 2010

In compliance with the Reports Consolidation Act, I am pleased to submit the U.S. Small Business Administration's Agency Financial Report for FY 2010.

SBA's loan activities have increased dramatically since passage of the American Recovery and Reinvestment Act in February 2009. As the popularity of the Recovery Act provisions for SBA loans (higher guaranties and reduced fees) led demand to swiftly outpace the original amount appropriated for Recovery Act loans, Congress passed four temporary extensions in FY 2010 before making many of the provisions permanent in the Small Business Jobs Act on September 27, 2010. Modeling and managing the waves of funds associated with the extensions was challenging but I am happy to report that our financial management team was once again up to the task. An independent audit has earned the SBA an unqualified and clean opinion with no material weaknesses. In addition, for the fourth straight year the SBA has won the prestigious CEAR (Certificate of Excellence in Accountability Reporting) award.

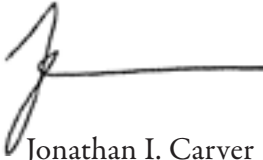
During FY 2010 we changed course on our ambitious Loan Management and Accounting System (LMAS) project. In accordance with OMB guidance, the SBA reviewed and subsequently discontinued this ongoing loan and financial system modernization project. As a result, the \$5.2 million accumulated cost to develop LMAS was written off to expense in the FY 2010 results. The SBA divided the LMAS program into smaller, more manageable projects which are funded separately, and which are intended to provide meaningful deliverables and decision points as the financial systems modernization effort progresses. This approach was also designed to enable the SBA to adjust the plans and implementation strategy based on lessons learned and on changing circumstances and funding levels.

FY 2010 saw further integration of performance and budget at the SBA. Early in the year we participated in the Administration's High Priority Performance Goals initiative. In the end, we chose four goals: increase the number of active SBA lending partners to 3,000 by the end of FY 2011; increase small business participation in federal government contracting; process 85 percent of home and business disaster loans within 14 and 18 days, respectively; and improve our Small Business Innovation Research program. The announcement of these goals spurred the Agency and as of September 30, we had already met the lender goal and exceeded the processing time goal for disaster loans.

Our integration efforts continued over the summer as we developed a new Agency strategic plan and budgetary submissions based on the framework of these goals. The creation of new programs during the Recovery Act and the Small Business Jobs Act offered us an opportunity to update and refine our performance measures. We seized it and, as a result, our performance is more accurately tracked and the quality of our data is continually improving. I believe our forward-looking performance and budget integration efforts will serve the SBA well as the government continues to move toward a more collaborative environment, both intra-agency and inter-agency.

Finally, I want to thank the independent Audit and Financial Management Advisory Committee who, since late FY 2004, engages with us in the financial reporting process and audit cycle, providing oversight of activities and making recommendations for our financial statement footnotes and the AFR prior to publication. We are proud to have one of the few independent audit committees within the federal government and appreciate the opportunity to have such an esteemed group of professionals advising us. I thank them for their support and dedication to continued improvement.

Sincerely,

A handwritten signature in black ink, appearing to be 'Jonathan I. Carver', followed by a horizontal line extending to the right.

Jonathan I. Carver
Chief Financial Officer

Audit and Financial Management Advisory Committee's Report

The Audit and Financial Management Advisory Committee (the Committee) assists the Administrator in overseeing the U.S. Small Business Administration's (SBA's) financial operations. As part of that responsibility, the Committee meets with Agency management, the Agency's Inspector General, and its external auditors to review and discuss SBA's external financial audit coverage, the effectiveness of SBA's internal controls over its financial operations, and its compliance with certain laws and regulations that could materially impact SBA's financial statements. SBA's external auditors are responsible for expressing an opinion on the conformity of SBA's audited financial statements with the U.S. generally accepted accounting principles. The Committee reviews the findings of the Inspector General and external auditors, and SBA's responses to those findings, to ensure that SBA's plan for corrective action includes appropriate and timely follow-up measures. In addition, the Committee reviews the draft Agency Financial Report (AFR), including its financial statements, and provides comments to management who has primary responsibility for the AFR. The Committee met three times during the year with respect to these responsibilities on FY 2010 financial management and reporting. During these sessions, the Committee met with the Inspector General and external auditors without SBA management being present and discussed with the external auditors the matters that are required to be discussed by generally accepted auditing standards. Nothing came to our attention as a result of these discussions to indicate changes were needed to the financial statements and notes thereto that are included in the FY 2010 AFR.



Edward J. Mazur
Chairman
Audit and Financial Management Advisory Committee

Inspector General's Audit Report



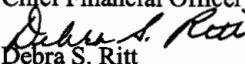
U.S. SMALL BUSINESS ADMINISTRATION
OFFICE OF INSPECTOR GENERAL
AUDITING DIVISION

AUDIT REPORT

Issue Date: November 12, 2010

Number: 11-03

To: Jonathan I. Carver
Chief Financial Officer

From: 
Debra S. Ritt
Assistant Inspector General for Auditing

Subject: Audit of SBA's FY 2010 Financial Statements

Pursuant to the Chief Financial Officer's Act of 1990, attached is a copy of the *Independent Auditors' Report* issued by KPMG LLP on the Small Business Administration's financial statements for the fiscal year ended September 30, 2010. The audit was performed under a contract with the Office of Inspector General (OIG) and in accordance with *Generally Accepted Government Auditing Standards*; Office of Management and Budget's (OMB) Bulletin 07-04, *Audit Requirements for Federal Financial Statements*, as amended; the Government Accountability Office (GAO)/President's Council on Integrity and Efficiency (PCIE) *Financial Audit Manual*; and GAO's *Federal Information System Controls Audit Manual*.

The KPMG report concluded that SBA's consolidated financial statements presented fairly, in all material respects, the financial position of SBA as of and for the years ended September 30, 2010 and 2009. It also presented fairly, in all material respects, SBA's net costs, changes in net position, and combined statements of budgetary resources for the years then ended.

With respect to internal controls, KPMG continued to report a significant deficiency related to Information Technology security controls. Details regarding the matters that led to the auditor's conclusion on internal controls are further discussed in Exhibit I of the *Independent Auditors' Report*. KPMG's test for compliance with certain laws, regulations, contracts and grant agreements determined that the Agency did not fully comply with the Debt Collection Improvement Act of 1996 because guidelines regarding referrals of delinquent debt for Treasury cross-servicing and offset were not consistently followed. Details regarding the auditor's conclusion are included in the "Compliance and Other Matters" section of the *Independent Auditors' Report*. The auditors did not report any other instances or matters regarding noncompliance.

We provided a draft of KPMG's report to SBA's Chief Financial Officer (CFO), who concurred with its findings and recommendations and agreed to implement the recommendations. The CFO is delighted that SBA has again received an unqualified

audit opinion and believes these results accurately reflect the quality of the Agency's financial statements and its improved accounting, budgeting and reporting processes.

We reviewed a copy of KPMG's report and related documentation and made necessary inquiries of their respective representatives. Our review was not intended to enable us to express, and we do not express, an opinion on the SBA's financial statements, KPMG's conclusions about the effectiveness of internal control, or its conclusions about SBA's compliance with laws and regulations. However, our review disclosed no instances where KPMG did not comply, in all material respects, with *Generally Accepted Government Auditing Standards*.

We appreciate the cooperation and assistance of SBA and KPMG. Should you or your staff have any questions, please contact me at (202) 205-7390 or Jeffrey R. Brindle, Director, Information Technology and Financial Management Group at (202) 205-7490.

Attachment

Independent Auditor's Report on FY 2010 Financial Statements



KPMG LLP
2001 M Street, NW
Washington, DC 20036-3389

Independent Auditors' Report

Office of Inspector General,
U.S. Small Business Administration:

We have audited the accompanying consolidated balance sheets of the U.S. Small Business Administration (SBA) as of September 30, 2010 and 2009, and the related consolidated statements of net cost and changes in net position, and combined statements of budgetary resources (hereinafter referred to as "consolidated financial statements") for the years then ended. The objective of our audits was to express an opinion on the fair presentation of these consolidated financial statements. In connection with our Fiscal Year (FY) 2010 audit, we also considered SBA's internal control over financial reporting and tested SBA's compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on these consolidated financial statements.

Summary

As stated in our opinion on the consolidated financial statements, we concluded that SBA's consolidated financial statements as of and for the years ended September 30, 2010 and 2009, are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles.

Our consideration of internal control over financial reporting resulted in identifying certain deficiencies that we consider to be a significant deficiency, as defined in the Internal Control Over Financial Reporting section of this report, as follows:

Improvement Needed in Information Technology (IT) Security Controls

We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses as defined in the Internal Control Over Financial Reporting section of this report.

The results of our tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements disclosed one instance of noncompliance that is required to be reported under *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended.

Noncompliance with the Debt Collection Improvement Act

The following sections discuss our opinion on SBA's consolidated financial statements; our consideration of SBA's internal control over financial reporting; our tests of SBA's compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements; and management's and our responsibilities.

KPMG LLP is a Delaware limited liability partnership, the U.S. member firm of KPMG International Cooperative ("KPMG International"), a Swiss entity.



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Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of SBA as of September 30, 2010 and 2009, and the related consolidated statements of net cost and changes in net position, and the combined statements of budgetary resources for the years then ended.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of SBA as of September 30, 2010 and 2009, and its net costs, changes in net position, and budgetary resources for the years then ended, in conformity with U.S. generally accepted accounting principles.

The information in the Management's Discussion and Analysis, Required Supplementary Information, and Required Supplementary Stewardship Information sections is not a required part of the consolidated financial statements, but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information and, accordingly, we express no opinion on it.

Internal Control Over Financial Reporting

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

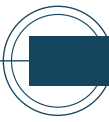
Our consideration of internal control over financial reporting was for the limited purpose described in the Responsibilities section of this report and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. In our FY 2010 audit, we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified a deficiency in internal control over financial reporting described in Exhibit I that we consider to be a significant deficiency in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Exhibit II presents the status of the prior year material weakness, and Exhibit III presents the status of the prior year significant deficiency.

We noted certain additional matters that we have reported to management of SBA in a separate letter dated November 12, 2010.

Compliance and Other Matters

The results of certain of our tests of compliance as described in the Responsibilities section of this report, exclusive of those referred to in the *Federal Financial Management Improvement Act of 1996* (FFMIA), disclosed one instance of noncompliance that is required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 07-04, and is described below.



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Page 3 of 4

Debt Collection Improvement Act of 1996 (DCIA). During our testwork over loan charge-offs, we noted SBA did not refer loans to Treasury for cross-servicing in accordance with the DCIA. Specifically, we noted ten loan charge-off transactions that were not referred to Treasury for cross-servicing. Two of the ten loans were loan guaranties that were not referred at time of charge-off. The remaining eight loans were not referred due to outdated referral system programming logic which prevented the automatic referral of charged-off loans to Treasury. Through additional research covering the population of Disaster loans charged-off during FY 2010, SBA identified a total of 473 disaster loans that were not referred for cross-servicing. Of the 473 loans identified, 334 loans were not referred due to the referral dates being out of the system range parameter; thus preventing the system from transmitting the loan referrals to Treasury. SBA was unable to determine why the remaining 139 charged-off loans were not referred. According to SBA management, efforts are underway to address the issues noted which caused the system errors. Further, SBA management agreed to perform an analysis of Disaster loans charged-off in prior years to identify and correct potential additional issues of noncompliance. Exhibit IV presents the status of the prior year noncompliance finding.

The results of our other tests of compliance as described in the Responsibilities section of this report, exclusive of those referred to in FFMIA, disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 07-04.

The results of our tests of FFMIA disclosed no instances in which SBA's financial management systems did not substantially comply with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level.

* * * * *

Responsibilities

Management's Responsibilities. Management is responsible for the consolidated financial statements; establishing and maintaining effective internal control; and complying with laws, regulations, contracts, and grant agreements applicable to SBA.

Auditors' Responsibilities. Our responsibility is to express an opinion on the FY 2010 and 2009 consolidated financial statements of SBA based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Bulletin No. 07-04. Those standards and OMB Bulletin No. 07-04 require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of SBA's internal control over financial reporting. Accordingly, we express no such opinion.



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An audit also includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall consolidated financial statement presentation.

We believe that our audits provide a reasonable basis for our opinion.

In planning and performing our FY 2010 audit, we considered the SBA's internal control over financial reporting by obtaining an understanding of SBA's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls as a basis for designing our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of SBA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of SBA's internal control over financial reporting. We did not test all controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

As part of obtaining reasonable assurance about whether SBA's FY 2010 consolidated financial statements are free of material misstatement, we performed tests of SBA's compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of the consolidated financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 07-04, including the provisions referred to in Section 803(a) of FFMI. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations, contracts, and grant agreements applicable to SBA. However, providing an opinion on compliance with laws, regulations, contracts, and grant agreements was not an objective of our audit and, accordingly, we do not express such an opinion.

* * * * *

SBA's response to the findings identified in our audit are presented in Exhibit V. We did not audit SBA's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of SBA's management, SBA's Office of Inspector General, OMB, the U.S. Government Accountability Office, and the U.S. Congress and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

November 12, 2010

U.S. Small Business Administration

Significant Deficiency

The significant deficiency identified for the year ended September 30, 2010, is summarized below:

(1) Improvement Needed in Information Technology (IT) Security Controls

We made many recommendations to address IT weaknesses identified during the Fiscal Year (FY) 2009 SBA audit. Although SBA has made some progress related to the FY 2009 weaknesses, improvements are still necessary. During FY 2010, we noted additional weaknesses in security access controls, including configuration and patch management, and segregation of duties. We are not providing details in this report on the specific weaknesses due to their sensitivity, but we have provided the details under a separate cover to SBA management.

Security Access Controls

Integral to an organization's security program management efforts, system security access controls should provide reasonable assurance that IT resources, such as data files, application programs, and IT-related facilities/equipment, are protected against unauthorized modification, disclosure, loss, or impairment.

A summary of the security access weaknesses we identified during the FY 2010 SBA financial statement audit follows:

- We identified several high and medium risk security vulnerabilities affecting various financial systems. We provided the detailed vulnerabilities to SBA management.
- We identified weaknesses in network access controls.
- We noted several high and medium risk security vulnerabilities affecting another key financial system, which is hosted by an SBA service provider. Although the service provider was monitoring the vulnerabilities and a plan to mitigate such weaknesses was developed, it was not implemented at the time of our review.
- We identified system patches that were not applied in a timely manner to a key financial system. Based on review of the Plan of Actions and Milestones (POA&M) for the system, we could not determine whether corrective actions were made timely.
- Password configuration settings for two key financial systems need improvement. We noted that one financial system did not enforce user password history, password complexity or account lockout after a specified number of failed login attempts. Another key financial system did not enforce password history, password complexity, password changes after 90 days, or account lockout after a specified number of failed login attempts. In addition, we found that password length settings are not compliant with SBA Standard Operating Procedure (SOP) 90.47.2, *Automated Information Systems Security Program*.
- Physical access control procedures are not current and have not been implemented at one SBA location.
- Several users have unnecessary access to a SBA financial subsystem.
- User accounts are not periodically reviewed for three key financial systems.
- There are weak controls over the monitoring and review of audit logs for four of seven systems we reviewed.

Exhibit I

U.S. Small Business Administration

Significant Deficiency

Recommendations – Security Access Controls:

We recommend that the Chief Information Officer (CIO) coordinate with SBA program offices to:

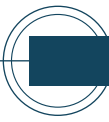
1. Improve the vulnerability tracking and monitoring process to fully address high and medium risk vulnerabilities for key financial systems. Ensure that the vulnerability reports are reviewed and analyzed on a regular basis. Periodically monitor the existence of necessary services and protocols running on servers and network devices. Develop a more thorough approach to track and mitigate patch management and configuration management vulnerabilities identified during monthly scans.
2. Prevent users from anonymously connecting unauthorized devices by developing and implementing procedures to ensure mandatory domain authentication for IP address issuance.
3. Improve the POA&M review and approval process for key financial systems. In addition, include all unresolved weaknesses on the POA&M (including vulnerabilities identified at service providers).
4. Enforce financial system password controls for System Administrators and Database Administrators (DBAs) and physical access controls in accordance with SBA SOP 90.47.2.
5. Develop and implement procedures for user access reviews to ensure that proper access rights are set for financial subsystems.
6. Oversee the review and validation of financial system accounts on a periodic basis.
7. Implement a process to monitor the audit logs of all financial applications on a regular basis.

Segregation of Duties

The primary focus of an organization's segregation of duties controls is to provide reasonable assurance that incompatible duties are effectively segregated. Without such controls, there is a risk that unauthorized changes could be implemented into the IT environment, and users may have access that is inappropriate for their duties. As a result, the confidentiality, integrity, and availability of financial data are at risk of possible loss, modification, or disclosure.

A summary of the segregation of duties control deficiencies we identified during the FY 2010 SBA financial statement audit follows:

- Application programmers for a key financial system have the ability to make changes and implement the changes into the production environment.
- Access to the development and production libraries of a key financial system is not restricted based on job role/functions or privileges.
- Certain Information Security staff and DBAs have incompatible access privileges for a financial system, which enable them to perform the user administration functions (i.e., grant any role, create user, become user, alter user, or drop user). We determined that compensating IT controls are not in place to mitigate this weakness.



U.S. Small Business Administration

Significant Deficiency

Recommendations – Segregation of Duties:

We recommend the Chief Financial Officer:

8. Implement procedures and conduct audits of financial system software changes to ensure all changes are sufficiently approved and tested.

We also recommend the CIO:

9. Restrict access to software program libraries based on the principle of least privilege, and periodically review access to the libraries.
10. Separate user and data administration functions for financial systems, or implement compensating IT controls such as management review of user administration functions.

Security Management

An entity-wide information security management program is the foundation of a security control structure and a reflection of senior management's commitment to addressing security risks. This security management program should establish a framework, and continuous cycle of activity for assessing risk, developing and implementing effective security procedures, and monitoring the effectiveness of these procedures.

A summary of the security management weaknesses we identified during the FY 2010 SBA financial statement audit follows:

- A mandatory training program for IT security personnel has not been implemented.
- We could not obtain sufficient evidence that media was sanitized properly in accordance with SBA policy.
- SBA implemented end-user security policies and procedures in May 2010, but the policies were not implemented during FY 2010.

Recommendations – Security Management:

We recommend the CIO:

11. Develop a comprehensive security education and training program for all IT security personnel and a method for monitoring the training program.
12. Implement and enforce the procedures documented in SOP 90.47.2 for sanitizing media to be disposed and for maintaining a log of employees who sanitize media to validate the appropriateness of the sanitization process.
13. Coordinate with program offices using end-user programs containing sensitive data, such as Personally Identifiable Information and financial data, to implement end-user computing procedures in accordance with the guidance.

Exhibit I**U.S. Small Business Administration**

Significant Deficiency

Software Configuration Management

The primary focus of an organization's software configuration management process is to control the software changes made to networks and systems. Without such controls, there is a risk that security features could be inadvertently, or deliberately, omitted or turned off, or that processing irregularities or malicious code could be introduced into the IT environment.

A summary of the configuration management weaknesses we identified during the FY 2010 SBA financial statement audit follows:

- The configuration management process is not centralized, and the Enterprise Change Control Board governance processes are not fully implemented across SBA.
- SBA personnel could not provide sufficient evidence to support software change authorizations for several financial systems.

Recommendations – Software Configuration Management:

We recommend the CIO:

14. Enforce an organization-wide configuration management process, to include policies and procedures for maintaining documentation that supports testing and approvals of software changes.

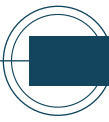


Exhibit II

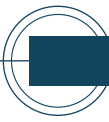
U.S. Small Business Administration
Status of Prior Year Material Weakness

Fiscal Year 2009 Finding	Fiscal Year 2010 Status of Finding
During Fiscal Year (FY) 2009, we reported a material weakness in internal control related to SBA's financial reporting.	During FY 2010, SBA made significant operational improvements over the controls surrounding the year-end financial reporting process. These improvements included automating previously manual processes and increasing the level of financial statement review performed by personnel within the Office of the Chief Financial Officer. In addition, our testwork did not identify any significant misstatements in FY 2010. Therefore, in FY 2010, this matter is closed.

Exhibit III

U.S. Small Business Administration
 Status of Prior Year Significant Deficiency

Fiscal Year 2009 Finding	Fiscal Year 2010 Status of Finding
Improvement Needed In Information Technology (IT) Security Controls	<p>During our review of SBA’s IT general and application controls, we noted minimal improvements made to address prior year findings. Therefore, control deficiencies continue to exist.</p> <p>Therefore, in fiscal year 2010, the presentation of the issue was modified to reflect current year operations, and we continue to report a significant deficiency in internal controls as it relates to IT systems and their impact on the consolidated financial statements. See Exhibit I for additional information.</p>



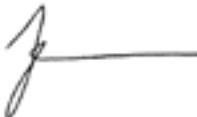
U.S. Small Business Administration

Status of Prior Year Noncompliance

Fiscal Year 2009 Finding	Fiscal Year 2010 Status of Finding
<p><i>Debt Collection Improvement Act of 1996 (DCIA)</i></p> <p>During our Fiscal Year (FY) 2009 audit, as stated in its <i>Federal Managers' Financial Integrity Act (FMFIA)</i> Assurance Statement, SBA management reported the agency was noncompliant with the DCIA in FY 2009. The noncompliance was due to instances where SBA did not refer a substantial number of charged off loans to Treasury for offset and cross servicing.</p>	<p>During our review over SBA's compliance with the DCIA, we noted improvements made in SBA's Treasury offset and cross-servicing referral process. However, during FY 2010 we noted instances of noncompliance related to timely referrals of loan charge-offs to Treasury for cross-servicing.</p> <p>Therefore, in FY 2010, the issue is again presented in the Compliance and Other Matters section of our Independent Auditors' Report.</p>

CFO Response to Draft Audit Report on FY 2010 Financial Statements

Exhibit V

DATE: November 12, 2010
TO: Debra Ritt, Assistant IG for Auditing
FROM: Jonathan Carver, Chief Financial Officer 
SUBJECT: Draft Audit Report on FY 2010 Financial Statements

The Small Business Administration is in receipt of the draft Independent Auditors' Report from KPMG that includes the auditor's opinion on the financial statements and review of the Agency's internal control over financial reporting and compliance with laws and regulations. The independent audit of the Agency's financial statements and related processes is a core component of SBA's financial management program.

We are delighted that the SBA has again received an unqualified audit opinion from the independent auditor with no reported material weaknesses. We believe these results accurately reflect the quality of the Agency's financial statements and our improved accounting, budgeting and reporting processes. As you know, the SBA has worked hard over the past several years to address the findings from our independent auditors. Our core financial reporting data and processes have improved substantially, and we are proud that the results of our efforts have been confirmed by the independent auditor.

The audit report includes a continuing significant deficiency in SBA's information technology controls. As the auditors noted in their report on the 2010 financial statements, the SBA made substantial progress in resolving IT deficiencies. The SBA will continue to improve the Agency's IT security during the upcoming fiscal year. The SBA is developing plans to track, monitor, and aggressively mitigate vulnerabilities in all Agency systems. Furthermore, the SBA will clarify and strengthen detailed procedures required to ensure security access controls are in place to protect SBA data from unauthorized modification, disclosure, and loss.

The audit report identified one instance of non-compliance with applicable laws and regulations as of September 30, 2010. Due to a system error, 473 of 8,229 charged off disaster loans, or 5.7 percent, were not referred to Treasury for cross-servicing and for the Treasury offset as required by the Debt Collection Improvement Act. This represents \$11.3 million of the \$247.5 million disaster loans written-off in FY 2010, or 4.6 percent. The system issue has been identified and is in the process of being remedied, and a mitigation plan has been developed to ensure that this issue will not recur. All loans eligible for Treasury referral will be referred within the next six months. An issue with referring non-disaster loans was identified in FY 2009 through SBA's self-assessment process and was corrected in FY2010. There were no issues identified in the testing of the improved internal controls over non-disaster loans by both our independent auditors and our OMB A-123 team in the current year, and we anticipate the same successful resolution for the disaster loans in FY 2011.

We appreciate all of your efforts and those of your colleagues in the Office of the Inspector General as well as those of KPMG. The independent audit process continues to provide us with new insights and valuable recommendations that will further enhance SBA's financial management practices. We continue to be committed to excellence in financial management and look forward to making more progress in the coming year.

Financial Statements and Notes

The U.S. Small Business Administration prepares its financial statements as a critical aspect of ensuring accountability and stewardship for the public resources entrusted to the SBA. Preparation of these statements is also an important part of SBA's financial management goal of providing accurate and reliable information that may be used to assess performance and allocate resources.

SBA's management is responsible for the accuracy and propriety of the information contained in the principal financial statements and the quality of internal controls. The statements are, in addition to other financial reports, used to monitor and control budgetary resources. The SBA prepares these financial statements from its books and records in accordance with generally accepted accounting principles in the United States as well as formats as prescribed by the Office of Management and Budget.

The **Consolidated Balance Sheet** summarizes the assets, liabilities, and net position by major category as of the reporting date. Intragovernmental assets and liabilities resulting from transactions between federal agencies are presented separately from assets and liabilities resulting from transactions with the public.

The **Consolidated Statement of Net Cost** shows, by strategic goal, the net cost of operations for the reporting period. Net cost of operations consists of full program costs incurred by the SBA less the exchange revenues earned by those programs.

The **Consolidated Statement of Changes in Net Position** presents SBA's beginning and ending net position by two components - Cumulative Results of Operations and Unexpended Appropriations. It summarizes the change in net position by major transaction category. The ending balances of both components of net position are also reported on the Balance Sheet.

The **Combined Statement of Budgetary Resources** provides information about funding and availability of budgetary resources and the status of those resources at the end of the reporting period. Data on the Combined Statement of Budgetary Resources is consistent with information reflected on the Report on Budget Execution and Budgetary Resources (SF 133), with the one exception of offsetting receipts. Offsetting receipts offset budget authority and outlays at the agency level in the Budget of the United States Government, but are not reflected in the SF 133. The SBA includes offsetting receipts in this statement for the purpose of reconciling outlay information presented in the Budget of the United States Government.

The **Required Supplementary Information** presents a Combining Statement of Budgetary Resources report by principal functional area.

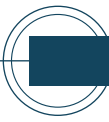
The **Required Supplementary Stewardship Information** provides information on SBA's investment in human capital.

U. S. Small Business Administration
Consolidated Balance Sheet
as of September 30, 2010 and 2009

(Dollars in Thousands)

	2010	2009
ASSETS		
Intragovernmental Assets		
Fund Balance with Treasury (Note 2)	\$ 6,116,325	\$ 3,469,465
Total Intragovernmental Assets	6,116,325	3,469,465
Assets - Public and Other		
Cash (Note 3)	3,031	2,662
Accounts Receivable, Net (Note 5)	30,961	16,081
Credit Program Receivables and Related Foreclosed Property, Net (Note 6)	9,076,679	9,128,496
General Property and Equipment, Net (Note 7)	2,817	8,535
Advances	663	1,220
Total Assets - Public and Other	9,114,151	9,156,994
Total Assets	\$ 15,230,476	\$ 12,626,459
LIABILITIES		
Intragovernmental Liabilities		
Interest Payable	\$ 1,435	\$ 2,143
Debt (Note 9)	11,753,781	10,878,283
Net Assets of Liquidating Funds Due to Treasury (Note 10)	68,359	78,584
Downward Reestimate Payable to Treasury (Note 1, Note 13)	130,993	64,875
Other (Note 8, Note 11)	14,234	16,062
Total Intragovernmental Liabilities	11,968,802	11,039,947
Other Liabilities - Public		
Accounts Payable (Note 1)	169,723	129,807
Accrued Grant Liability (Note 1)	62,576	59,000
Liability for Loan Guaranties (Note 6)	4,467,006	3,994,636
Federal Employee Compensation Act Actuarial Liability (Note 1, Note 8)	29,960	29,640
Surety Bond Guarantee Program Future Claims (Note 8)	19,539	20,817
Other (Note 8, Note 11)	47,415	41,212
Total Other Liabilities - Public	4,976,219	4,275,112
Total Liabilities	16,765,021	15,315,059
NET POSITION		
Unexpended Appropriations (Note 1)	2,295,070	1,983,504
Cumulative Results of Operations (Note 1)	(3,829,615)	(4,672,104)
Total Net Position	(1,534,545)	(2,688,600)
Total Liabilities and Net Position	\$ 15,230,476	\$ 12,626,459

The accompanying notes are an integral part of these statements.



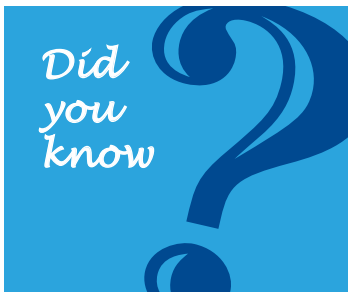
U. S. Small Business Administration
Consolidated Statement of Net Cost
 For the years ended September 30, 2010 and 2009

(Dollars in Thousands)

	<u>2010</u>	<u>2009</u>
STRATEGIC GOAL 1:		
Expand America's Ownership Society, Particularly in Underserved Markets		
Gross Cost	\$ 4,997,089	\$ 5,409,931
Less: Earned Revenue	258,349	166,343
Net Cost of Strategic Goal 1	4,738,740	5,243,588
STRATEGIC GOAL 2:		
Provide Timely Financial Assistance to Homeowners, Renters, Nonprofit Organizations and Businesses Affected by Disaster		
Gross Cost	814,451	1,081,232
Less: Earned Revenue	367,738	405,904
Net Cost of Strategic Goal 2	446,713	675,328
STRATEGIC GOAL 3:		
Improve Economic Environment for Small Business		
Gross Cost	17,814	14,506
Total Program Cost of Strategic Goal 3	17,814	14,506
COST NOT ASSIGNED TO STRATEGIC GOALS		
Gross Cost	73,930	62,294
Total Program Cost Not Assigned to Strategic Goals	73,930	62,294
Net Cost of Operations	\$ 5,277,197	\$ 5,995,716

Note 12, Note 14

The accompanying notes are an integral part of these statements.



The SBA helps small businesses win federal government contracts. In FY 2010 small businesses were awarded 96.8 billion dollars in federal prime contracts. <http://www.sba.gov/goaling>

U. S. Small Business Administration
Consolidated Statement of Changes in Net Position
 For the years ended September 30, 2010 and 2009

(Dollars in Thousands)

	<u>2010</u>	<u>2009</u>
Beginning Cumulative Results of Operations	\$ (4,672,104)	\$ (1,362,736)
Budgetary Financing Sources		
Appropriations Used	6,231,677	2,748,961
Donations of Cash and Cash Equivalents	24	25
Other Financing Sources		
Imputed Financing from Costs Absorbed by Others	32,765	25,549
Other - Cancelled Authority	(3)	-
Other - Current Year Liquidating Equity Activity	(760)	(863)
Other - Non-entity Activity	(144,017)	(87,324)
Total Financing Sources	6,119,686	2,686,348
Less: Net Cost of Operations	5,277,197	5,995,716
Ending Cumulative Results of Operations	\$ (3,829,615)	\$ (4,672,104)
Beginning Unexpended Appropriations	\$ 1,983,504	\$ 1,696,866
Budgetary Financing Sources		
Appropriations Received	6,554,119	3,050,068
Appropriations Transferred In	-	2,953
Adjustment - Cancelled Authority	(7,598)	(11,777)
Other Adjustments	(3,278)	(5,645)
Appropriations Used	(6,231,677)	(2,748,961)
Total Budgetary Financing Sources	311,566	286,638
Ending Unexpended Appropriations	\$ 2,295,070	\$ 1,983,504
Ending Net Position	\$ (1,534,545)	\$ (2,688,600)

The accompanying notes are an integral part of these statements.

U. S. Small Business Administration
Combined Statement of Budgetary Resources
 For the years ended September 30, 2010 and 2009

(Dollars in Thousands)

	September 30, 2010		
	Budgetary	Nonbudgetary Financing	Total
BUDGETARY RESOURCES			
Unobligated Balance			
Brought Forward October 1	\$ 1,506,612	\$ 1,195,311	\$ 2,701,923
Recoveries of Prior Year Obligations	53,179	81,604	134,783
Budget Authority			
Appropriations Received	6,554,119	–	6,554,119
Borrowing Authority	–	2,737,959	2,737,959
Spending Authority from Offsetting Collections			
Earned	395,025	7,823,359	8,218,384
Change in Unfilled Customer Orders	(116,593)	(5,571)	(122,164)
Total Budget Authority	6,832,551	10,555,747	17,388,298
Nonexpenditure Transfers, Net			
Budget Authority	–	–	–
Permanently Not Available	(25,123)	(1,859,112)	(1,884,235)
Total Budgetary Resources	\$ 8,367,219	\$ 9,973,550	\$ 18,340,769
STATUS OF BUDGETARY RESOURCES			
Obligations Incurred, Net			
Direct	\$ 5,981,675	\$ 6,515,175	\$ 12,496,850
Reimbursable	616,935	–	616,935
Total Obligations Incurred, Net	6,598,610	6,515,175	13,113,785
Unobligated Balances, Available	215,473	2,060,909	2,276,382
Unobligated Balances, Not Available	1,553,136	1,397,466	2,950,602
Total Status of Budgetary Resources	\$ 8,367,219	\$ 9,973,550	\$ 18,340,769
CHANGE IN OBLIGATED BALANCES			
Obligated Balance Brought Forward, Net October 1			
Unpaid Obligations Brought Forward	\$ 613,478	\$ 389,934	\$ 1,003,412
Uncollected Customer Payments from Federal Sources Brought Forward	–	(235,874)	(235,874)
Total Obligated Balance Brought Forward, Net	613,478	154,060	767,538
Obligations Incurred	6,598,610	6,515,175	13,113,785
Gross Outlays	(6,482,855)	(6,379,919)	(12,862,774)
Recoveries of Prior Year Unpaid Obligations	(53,179)	(81,604)	(134,783)
Change in Uncollected Customer Payments from Federal Sources	–	5,571	5,571
Obligated Balance, Net, End of Period			
Unpaid Obligations	676,054	443,586	1,119,640
Uncollected Customer Payments from Federal Sources	–	(230,303)	(230,303)
Total Obligated Balance, Net, End of Period	\$ 676,054	\$ 213,283	\$ 889,337
NET OUTLAYS			
Gross Outlays	\$ 6,482,855	\$ 6,379,919	\$ 12,862,774
Offsetting Collections	(278,430)	(7,823,359)	(8,101,789)
Net Outlays Before Offsetting Receipts	6,204,425	(1,443,440)	4,760,985
Offsetting Receipts	(110)	(77,891)	(78,001)
Net Outlays	\$ 6,204,315	\$ (1,521,331)	\$ 4,682,984

Note 15

The accompanying notes are an integral part of these statements.

U. S. Small Business Administration
Combined Statement of Budgetary Resources
 For the years ended September 30, 2010 and 2009

(Dollars in Thousands)

	September 30, 2009		
	Budgetary	Nonbudgetary Financing	Total
BUDGETARY RESOURCES			
Unobligated Balance			
Brought Forward October 1	\$ 1,429,754	\$ 1,547,065	\$ 2,976,819
Recoveries of Prior Year Obligations	64,639	220,652	285,291
Budget Authority			
Appropriations Received	3,050,068	–	3,050,068
Borrowing Authority	–	3,455,566	3,455,566
Spending Authority from Offsetting Collections			
Earned	429,412	4,042,183	4,471,595
Change in Unfilled Customer Orders	32,755	157,011	189,766
Total Budget Authority	3,512,235	7,654,760	11,166,995
Nonexpenditure Transfers, Net			
Budget Authority	2,953	–	2,953
Permanently Not Available	(49,302)	(2,045,701)	(2,095,003)
Total Budgetary Resources	\$ 4,960,279	\$ 7,376,776	\$ 12,337,055
STATUS OF BUDGETARY RESOURCES			
Obligations Incurred, Net			
Direct	\$ 2,602,745	\$ 6,181,465	\$ 8,784,210
Reimbursable	850,922	–	850,922
Total Obligations Incurred, Net	3,453,667	6,181,465	9,635,132
Unobligated Balances, Available	537,389	889,666	1,427,055
Unobligated Balances, Not Available	969,223	305,645	1,274,868
Total Status of Budgetary Resources	\$ 4,960,279	\$ 7,376,776	\$ 12,337,055
CHANGE IN OBLIGATED BALANCES			
Obligated Balance Brought Forward, Net October 1			
Unpaid Obligations Brought Forward	\$ 421,630	\$ 561,165	\$ 982,795
Uncollected Customer Payments from Federal Sources Brought Forward	–	(78,863)	(78,863)
Total Obligated Balance Brought Forward, Net	421,630	482,302	903,932
Obligations Incurred	3,453,667	6,181,465	9,635,132
Gross Outlays	(3,197,180)	(6,132,044)	(9,329,224)
Recoveries of Prior Year Unpaid Obligations	(64,639)	(220,652)	(285,291)
Change in Uncollected Customer Payments from Federal Sources	–	(157,011)	(157,011)
Obligated Balance, Net, End of Period			
Unpaid Obligations	613,478	389,934	1,003,412
Uncollected Customer Payments from Federal Sources	–	(235,874)	(235,874)
Total Obligated Balance, Net, End of Period	\$ 613,478	\$ 154,060	\$ 767,538
NET OUTLAYS			
Gross Outlays	\$ 3,197,180	\$ 6,132,044	\$ 9,329,224
Offsetting Collections	(462,167)	(4,042,183)	(4,504,350)
Net Outlays Before Offsetting Receipts	2,735,013	2,089,861	4,824,874
Offsetting Receipts	(59)	(489,336)	(489,395)
Net Outlays	\$ 2,734,954	\$ 1,600,525	\$ 4,335,479

Note 15

The accompanying notes are an integral part of these statements.

NOTE 1. Significant Accounting Policies

Reporting Entity

The Small Business Act of 1953 created the Small Business Administration as an independent federal agency. SBA's mission is to maintain and strengthen the nation's economy by aiding, counseling, assisting and protecting the interests of small businesses and to help businesses and families recover from natural disasters. The SBA operates through the execution of a congressionally approved budget that funds its programs.

Basis of Accounting and Presentation

The SBA prepares financial statements to report its financial position and results of its operations as required by the Chief Financial Officers Act of 1990 and the Government Management Reform Act of 1994. The financial statements are prepared from the Agency's records in accordance with generally accepted accounting principles using formats prescribed by the Office of Management and Budget. The statements are in addition to other financial reports used to monitor and control budgetary resources. As a federal agency, the SBA cannot incur obligations without authority from the Congress and an apportionment by the OMB.

These financial statements reflect transactions recorded on both a proprietary accrual accounting basis and a budgetary obligation basis, in accordance with concepts and guidance provided by OMB, the Federal Accounting Standards Advisory Board, and the Department of the Treasury. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when incurred, without regard to receipt or payment of cash. Budgetary accounting recognizes the legal commitment or obligation of funds in advance of the proprietary accruals and facilitates compliance with legal constraints and controls over the use of federal funds.

Use of Estimates

SBA's management makes assumptions and uses estimates to prepare the financial statements based upon the facts that exist when the statements are prepared. Actual results may differ from those estimates and the differences may be significant. The most significant differences between actual results and SBA's estimates may occur in the valuation of credit program receivables and liabilities for loan guaranties under guidelines in the Federal Credit Reform Act of 1990. The SBA recognizes the sensitivity of credit reform modeling to slight changes in some model assumptions and therefore continually reviews its model factors and statistical modeling technique to reflect the most accurate credit program costs possible in its annual financial statements.

Budgets and Budgetary Accounting for Loan Programs

SBA's loan disbursements are financed by appropriations for long-term loan subsidy cost and borrowings from the Department of the Treasury for the remaining non-subsidized portion of the loans. The Congress may provide one year, multi-year or no year appropriations to cover the estimated long-term costs of the loan programs. The non-subsidized portion of each loan disbursement, financed initially under permanent indefinite authority to borrow funds from the Treasury, is repaid from collections of loan fees, repayments and default recoveries. The Congress limits the dollar amount of obligations that can be made for direct loans and loan guaranties in its annual appropriation bill. Similarly, appropriations received for the long-term cost of loan guaranties are reserved when the guaranteed loans are disbursed.

A permanent indefinite authority is available to fund any reestimated increase of subsidy costs that occurs after the year in which a loan is disbursed. Reestimated reductions of subsidy costs are returned to the Treasury and are unavailable to the SBA. As required by the Federal Credit Reform Act of 1990, the SBA uses budgetary “program accounts” to account for appropriations in its credit programs and non-budgetary “financing accounts” to account for credit program cash flow. Estimates and reestimates of credit program subsidy expenses are recorded in SBA’s program accounts. Financing accounts are used to account for Treasury borrowings, the collection of loan fees, repayments and default recoveries, and the disbursement of loans and loan expenses.

Accounts Payable

Accounts Payable are amounts due to public entities that will be liquidated during the next operating cycle. Included in the liability are payables to SBA lenders for their share of loan collections and to vendors for goods and services.

Accrued Grant Liability

Disbursements of grant funds are recognized as expenses at the time of disbursement. However, some grant recipients incur expenditures prior to initiating a request for disbursement based on the nature of the expenditures. The SBA accrues a liability for expenditures incurred by grantees prior to receiving grant funds for the expenditures. The amount to be accrued is determined through an analysis of historic grant expenditures. The Small Business Development Center program and several other grant programs are subjected to this treatment.

Contingencies

The SBA is a party in various administrative proceedings, legal actions, environmental suits and claims brought against the Agency. In the opinion of SBA’s management and legal counsel, the ultimate resolution of these proceedings, actions, suits and claims will not materially affect the financial position or results of SBA’s operations. The likelihood of loss to the SBA ranges from remote on several items to a reasonably possible amount of \$2.0 million on one item.

Cumulative Results of Operations

Cumulative Results of Operations, presented on the Balance Sheet and on the Statement of Changes in Net Position, is the accumulated difference between expenditures and financing sources since the inception of the Agency. Unfunded expenses do not yet have a financing source and thus increase the loss the SBA reports as Cumulative Results of Operations. The largest category of unfunded expenses at the SBA is year-end reestimates which are funded in the following year. The majority of the Cumulative Results of Operations reported results from these unfunded reestimates.

Unexpended Appropriations

Unexpended Appropriations is the portion of SBA’s appropriations received which are either undelivered or unobligated. Delivered orders result in expended appropriations and reduce the total reported as Unexpended Appropriations. Undelivered orders are the amount of orders of goods or services which have not been actually or constructively received.

Employee Benefits

LEAVE

A liability for employee annual leave is accrued as it is earned and reduced as leave is taken. Each year the balance of accrued annual leave is adjusted to reflect current pay rates as well as forfeited “use or lose” leave. Amounts are reported as unfunded to the extent current or prior year appropriations are not available to fund annual leave earned but not taken. Sick leave and other types of non-vested leave are expensed as taken.

EMPLOYEE HEALTH AND LIFE INSURANCE BENEFITS

SBA employees may choose to participate in the contributory Federal Employees Health Benefit and the Federal Employees Group Life Insurance Programs. The SBA matches a portion of the employee contributions to each program. Matching contributions are recognized as current operating expenses.

EMPLOYEE PENSION BENEFITS

SBA employees participate in either the Civil Service Retirement System or the Federal Employees’ Retirement System and Social Security. These systems provide benefits upon retirement and in the event of death, disability, or other termination of employment and may also provide pre-retirement benefits. They may also include benefits to survivors and their dependents, and they may contain early retirement or other special features. SBA’s contributions to both retirement plans, as well as to the government-wide Federal Insurance Contribution Act, administered by the Social Security Administration, are recognized on the Consolidated Statement of Net Cost as current operating expenses.

Federal employee benefits also include the Thrift Savings Plan. For FERS employees the SBA matches employee contributions to the plan, subject to limitations. The matching contributions are recognized as current operating expenses.

IMPUTED FINANCING COSTS

The SBA recognizes the full cost of providing all employee benefits and future retirement benefits, including life and health insurance, at the time employee services are rendered. Eligible retired SBA employees can continue to participate in health and life insurance plans. The cost of these benefits is funded through Agency contributions, employee compensation to the extent withheld from employee and retiree pay, from matching of employee withholding for Thrift Savings Plan and FICA, and by the Office of Personnel Management which administers the retirement programs for SBA employees.

The OPM calculates imputed costs as the actuarial present value of future benefits attributed to services rendered by covered employees and eligible retired SBA employees during the accounting period, net of the amounts contributed by employees, retirees, and the Agency. The SBA recognizes these imputed costs in the Statement of Net Cost and as a part of net cost funded by an imputed financing source included in determining SBA’s net position.

FEDERAL EMPLOYEES COMPENSATION ACT

The Federal Employees Compensation Act provides income and medical cost protection to covered federal civilian employees injured on the job and to beneficiaries of employees whose deaths are attributable to job-related injury or disease. The FECA program is administered by the Department of Labor. Labor pays valid claims as they occur, which are billed to the SBA annually and funded and paid approximately 15 months later. Labor also calculates an estimated actuarial liability for future benefits based upon historical experience and other economic variables. Projected annual benefit payments are then discounted to present value using the forecasted interest rates for 10-year Treasury notes and bonds published by the OMB in its economic assumptions for the federal budget. The SBA recognizes a current unfunded cost for the actual claims paid and the change in the FECA actuarial liability each year.

NOTE 2. Fund Balance with Treasury

The Department of the Treasury processes cash receipts and disbursements on SBA's behalf to pay liabilities and finance loan program costs. SBA's cash receipts are deposited to accounts at the Treasury. SBA's fund balances with the Treasury are available to make expenditures to liquidate allowable obligations, except for Non-entity Fund Balance which is not available to the SBA to obligate or expend. Separate records are maintained for SBA's program, financing, liquidating and other accounts. Fund balances at the Treasury include expired year amounts, which are unavailable for obligation, as well as amounts currently available for new obligations.

(Dollars in Thousands)

AS OF SEPTEMBER 30,	2010	2009
Appropriated Funds	\$ 2,373,450	\$ 2,052,859
Financing Funds	3,671,657	1,349,371
Liquidating Funds	14,588	17,527
Revolving Fund	56,363	49,415
Trust Fund	263	289
Total Entity Fund Balance with Treasury	6,116,321	3,469,461
Non-entity Fund Balance	4	4
Total Fund Balance with Treasury	\$ 6,116,325	\$ 3,469,465
Status of Fund Balance with Treasury		
Unobligated Balance Available	\$ 2,276,382	\$ 1,427,055
Unobligated Balance Unavailable	2,950,602	1,274,868
Obligated Balance Not Yet Disbursed	889,337	767,538
Non-budgetary	4	4
Total Fund Balance with Treasury	\$ 6,116,325	\$ 3,469,465

Unobligated balances become available when apportioned by the OMB for obligation in the current fiscal year. Obligated balances not yet disbursed include unpaid obligations offset by uncollected customer payments from other federal government accounts. The unobligated and obligated balances are reflected on the Statement of Budgetary Resources.

NOTE 3. Cash

SBA field offices deposit collections from borrowers in Treasury General Accounts at financial institutions for credit to SBA's account at the Treasury. At the end of the fiscal year, collections temporarily held by SBA field offices pending deposit are recorded as Undeposited Collections – Cash in Transit and total \$3.0 million and \$2.6 million at September 30, 2010 and 2009.

NOTE 4. Fiduciary Activities: Master Reserve Fund and Master Reserve Account

Fiduciary activities are the receipt, management, protection, accounting, investment and disposition by the federal government of cash or other assets in which non-federal entities have an ownership interest that the federal government must uphold. Fiduciary cash and other assets are not assets of the government, and are not recognized on SBA's proprietary statements, but they are required to be disclosed in the notes to SBA's financial statements. Fiduciary balances may be on deposit with the Treasury or commercial banks.

SBA's fiduciary activities include the Master Reserve Fund and Master Reserve Account, both administered by SBA's fiscal agent, Colson Inc. The MRF and MRA are maintained in commercial bank accounts (not the Treasury). The balances in the MRF and MRA are invested according to SBA policy entirely in Treasury securities and repurchase agreements that are backed by Treasury securities. The MRF is an integral part of SBA's 7(a) secondary market program. The MRF was authorized by the Small Business Secondary Market Improvement Act of 1984 to facilitate the pooling of 7(a) guaranteed loans that are purchased by secondary market investors. The 7(a) secondary market program includes SBA's guaranty of timely payment, as well as a default guaranty, to 7(a) secondary market investors. The program encompassed \$15.5 billion and \$14.7 billion of outstanding secondary market loan principal at September 30, 2010 and 2009.

The MRA facilitates the operation of the 504 Development Company secondary market program. The MRA was authorized by Section 505 of the Small Business Investment Act of 1958 as a vehicle to receive, temporarily hold and distribute 504 program cash flows. The MRA receives monthly payments from the 504 borrowers and retains the payments until a semi-annual debenture payment is due to the secondary market investors. The 504 secondary market program includes SBA's guaranty of timely payment, as well as a default guaranty, to 504 secondary market investors. The program encompassed \$23.4 billion and \$23.0 billion of debentures outstanding at September 30, 2010 and 2009.

The composition of the MRF and MRA and a reconciliation of the changes in the assets are included in the following table:

(Dollars in Thousands)

FIDUCIARY ASSETS

AS OF SEPTEMBER 30,	2010	2009
Short Term Securities		
Money Market Funds	\$ 27,767	\$ 27,473
Treasury Bills	47,957	47,979
Repurchase Agreements	826,147	667,766
Total Short Term Securities	901,871	743,218
Long Term Securities		
Treasury Notes Including Interest	1,724,565	1,643,277
Total Long Term Securities	1,724,565	1,643,277
Net Assets	\$ 2,626,436	\$ 2,386,495

RECONCILIATION OF FIDUCIARY ASSETS

FOR THE YEARS ENDING SEPTEMBER 30,	2010	2009
Beginning Net Assets	\$ 2,386,495	\$ 2,370,628
Receipts		
Earned Income	63,178	65,219
Contributions	7,808,155	7,250,815
Net Realized Gain (Loss)	3,097	(109)
Total Receipts	7,874,430	7,315,925
Less Disbursements		
Payments to Investors	7,634,350	7,298,452
Expenses	139	1,606
Total Disbursements	7,634,489	7,300,058
Ending Net Assets	\$ 2,626,436	\$ 2,386,495

NOTE 5. Accounts Receivable

Accounts receivable include amounts owed by the public for guaranty fees in SBA’s loan and surety bond programs, refunds due from employees and others, as well as other amounts owed by lenders on guaranteed loans purchased by the SBA. An Allowance for Loss on uncollectible Surety Bond Guaranty fees is based on an analysis of delinquent balance aging. The uncollectible or unrecoverable amounts for Guaranty Fees Receivable, Refunds and Other accounts receivable are not significant and no allowance is provided.

(Dollars in Thousands)

AS OF SEPTEMBER 30,	2010	2009
Public		
Guaranty Fees Receivable	\$ 13,559	\$ 1,474
Refunds	18	229
Other	17,403	14,461
Total Public	30,980	16,164
Allowance For Loss	(19)	(83)
Net Public	\$ 30,961	\$ 16,081

NOTE 6. Credit Program Receivables and Liability for Loan Guaranties

A. Loan Program Descriptions and Cost Determinations

LOAN PROGRAM DESCRIPTIONS

The SBA administers guaranteed and direct loan programs that help small businesses obtain financing, and a direct loan program that assists homeowners, renters and businesses to recover from disasters.

MAJOR DIRECT LOAN AND LOAN GUARANTY PROGRAMS

Program group	Program type	Program
Disaster	Direct	Disaster Assistance Loans
Business	Direct	7(m) Microloan
Business	Guaranteed	7(a) Loan Guaranty
Business	Guaranteed	America’s Recovery Capital Loan
Business	Guaranteed	504 Certified Development Company
Business	Guaranteed	Small Business Investment Company Debenture
Business	Guaranteed	Small Business Investment Company Participating Securities
Business	Guaranteed	Secondary Market Guaranty

SBA’s Disaster Assistance loan program makes direct loans to disaster victims under four categories: (1) loans for homes and personal property, (2) physical disaster loans to businesses of any size, (3) economic injury loans to small businesses without credit available elsewhere, and (4) economic injury loans to eligible businesses affected by essential employees called up to active duty in the military reserves. The maximum interest rate is 4 percent for loan applicants without credit available elsewhere and 8 percent for applicants with credit available elsewhere.

SBA’s business loan programs include its flagship 7(a) Loan Guaranty program in which the SBA guarantees up to 90 percent of the principal amount of loans made by banks and other lending institutions to small

businesses not able to obtain credit elsewhere. The Section 504 Certified Development Company program guarantees 100 percent of the principal and interest payments on debentures issued by development companies that make small business loans secured primarily by real estate. The Small Business Investment Company Debentures and Participating Securities programs guarantee principal and interest payments on securities issued by investment capital firms, which in turn make investments in small businesses. The 7(m) Microloan program provides direct loans to nonprofit intermediaries, which use these funds to make loans up to \$35,000 to eligible small businesses. See Note 4 for further discussion of the Secondary Market Guaranty. America's Recovery Capital loan program is a new temporary guaranty loan program authorized by the American Recovery and Reinvestment Act of 2009 (ARRA or Recovery Act). ARC loans are deferred payment loans of up to \$35,000 available through SBA's 7(a) participating lenders. ARC loans are interest free to the borrower, 100 percent guaranteed by the SBA to the lender, and have no fees associated with them.

CREDIT PROGRAM RECEIVABLES AND LIABILITIES FOR LOAN GUARANTIES

The Federal Credit Reform Act of 1990 governs direct loans made after FY 1991. FCRA loans are valued at the present value of expected future cash flows, discounted at the interest rate of marketable Treasury securities. The subsidy allowance account represents the difference between the outstanding loans receivable balance and the net present value of the estimated cash flows of the loans over their remaining term. The subsidy allowance is subtracted from the outstanding loans receivable balance to obtain the net loans receivable balance. FCRA also governs loan guaranties made after FY 1991. A liability for outstanding guaranties is included on SBA's balance sheet. The liability is determined by calculating the net present value of expected future cash flows for outstanding guaranties in a manner similar to that used to determine the subsidy allowance for direct loans. Guaranteed loans purchased by the SBA upon borrower default are established as loans receivable and are valued in a similar manner as direct loans under FCRA.

Direct loans made prior to FCRA are recorded at cost with an allowance for uncollectible amounts calculated using historical loss experience. For loan guaranties made prior to FCRA, a liability for expected future losses on outstanding guaranties is established based on historical experience. Guaranteed loans purchased upon borrower default are established as loan receivables with an allowance for losses based on historical loss experience.

The SBA advances payments semiannually to the Federal Financing Bank for loans guaranteed under Section 503 of the Small Business Act. The advances are liquidated by receipt of the installment payments on loans made by state and local development companies. To the extent that those installments may not repay advances, balances from development companies that remain collectible are reported as credit program receivables.

Advances are similarly made to honor SBA's timely payment requirement of principal and interest due for debentures in SBA's Section 504 Certified Development Company and Small Business Investment Company programs. These advances are also reported as credit program receivables.

SUBSIDY FUNDING UNDER FEDERAL CREDIT REFORM

FCRA requires that the credit subsidy costs of direct loans and loan guaranties be expensed in the year loans are disbursed. The credit subsidy cost is the net present value of expected cash inflows and outflows over the life of a guaranteed loan, or the difference between the net present value of expected cash flows and the face value of a direct loan. The cost expressed as a percentage of loans disbursed is termed the subsidy rate. The SBA receives appropriations annually to fund its credit programs based on the subsidy rate that applies to the credit program level approved by Congress. The SBA records subsidy expenses when loans are disbursed. In accordance with FCRA, subsidy costs are reestimated annually.

INTEREST RECEIVABLE

Interest receivable is comprised of accrued interest on loans receivable and purchased interest related to defaulted guaranteed loans. Interest income is accrued at the contractual rate on the outstanding principal amount and is reduced by the amount of interest income accrued on non-performing loans in excess of 90 days delinquent. Purchased interest is carried at cost. A 100 percent loss allowance is established for all purchased interest on non-performing loans made prior to FY 1992.

FORECLOSED PROPERTY

Foreclosed property is comprised of real and business-related property acquired through foreclosure on loans and defaulted loan guaranties. Properties acquired as a result of defaulted loans committed after FY 1991 are shown at recoverable value which is adjusted to the present value of expected future cash flows for financial statement presentation through the allowance for subsidy. Other foreclosed property is shown at the appraised value. At September 30, 2010 SBA's foreclosed property was \$44.9 million related to 79 loans. The properties had been held for an average of 616 days. At September 30, 2009 foreclosed property was \$41.7 million related to 80 loans. The properties had been held for an average of 1,266 days.

VALUATION METHODOLOGY FOR POST-1991 DIRECT LOANS AND LOAN GUARANTIES

The value of direct and guaranteed loans committed after FY 1991 is based on the net present value of their expected future cash flow. The SBA estimates future cash flows for guaranteed and direct loans using economic and financial credit subsidy models. The SBA has developed a customized credit subsidy model for each of its major loan guaranty and direct loan programs.

SBA's models vary in the specific methodologies employed to forecast future program cash flows. In general, however, models for all major credit programs use historical data as the basis for assumptions about future program performance and then translate these assumptions into nominal cash flow estimates by applying rules about program structure. Nominal cash flow forecasts are discounted using the Office of Management and Budget's Credit Subsidy Calculator that has both forecasted and actual Treasury interest rates.

Historical data used as the basis for program performance assumptions is drawn primarily from data systems maintained by the SBA and its contractors. The historical data undergoes quality review and analysis prior to its use in developing model assumptions.

Key input to the subsidy models varies by program. Input includes items such as:

- Contractual terms of the loan or guaranty such as loan amount, interest rate, maturity and grace period
- Borrower characteristics
- Loan origination methods
- Economic indicators such as gross domestic product growth and unemployment rate
- Loan performance assumptions, for example: conditional purchase and prepayment rates and recovery rates
- Loan fee rates

VALUATION METHODOLOGY FOR PRE-1992 DIRECT LOANS AND LOAN GUARANTIES

The SBA values pre-credit reform direct and defaulted guaranteed loans by estimating an allowance for loan losses. This allowance is offset against gross loan receivables to obtain SBA's expected net collections from these assets. The SBA establishes a 100 percent allowance for pre-credit reform direct and guaranteed loans that are past due more than 180 days. A liability is also established for active pre-credit reform loan guaranties. The liability is estimated based on historical experience.

B. Credit Program Receivables and Related Foreclosure Property, Net

(Dollars in Thousands)

AS OF SEPTEMBER 30, 2010	Pre-1992 Loans	Post-1991 Loans	Total
Direct Business Loans			
Business Loans Receivable	\$ 18,218	\$ 120,151	\$ 138,369
Interest Receivable	2,457	1,077	3,534
Foreclosed Property	3,104	–	3,104
Allowance	(1,595)	(30,646)	(32,241)
Total Direct Business Loans	22,184	90,582	112,766
Direct Disaster Loans			
Disaster Loans Receivable	10,643	7,931,998	7,942,641
Interest Receivable	73	12,191	12,264
Foreclosed Property	–	658	658
Allowance	(740)	(1,475,666)	(1,476,406)
Total Direct Disaster Loans	9,976	6,469,181	6,479,157
Defaulted Guaranteed Business Loans & Other Loans Receivable			
Defaulted Guaranteed Business Loans	51,002	7,763,190	7,814,192
Other Loans Receivable (see note below)	–	583,745	583,745
Interest Receivable	408	48,719	49,127
Foreclosed Property	3,281	37,910	41,191
Allowance	(30,163)	(5,973,336)	(6,003,499)
Total Defaulted Guaranteed Business Loans & Other Loans Receivable	24,528	2,460,228	2,484,756
Total Credit Program Receivables & Related Foreclosed Property, Net			\$ 9,076,679

AS OF SEPTEMBER 30, 2009	Pre-1992 Loans	Post-1991 Loans	Total
Direct Business Loans			
Business Loans Receivable	\$ 22,865	\$ 111,870	\$ 134,735
Interest Receivable	1,945	1,196	3,141
Foreclosed Property	3,104	–	3,104
Allowance	(1,924)	(28,445)	(30,369)
Total Direct Business Loans	25,990	84,621	110,611
Direct Disaster Loans			
Disaster Loans Receivable	13,825	8,424,827	8,438,652
Interest Receivable	103	29,501	29,604
Foreclosed Property	–	933	933
Allowance	(980)	(1,597,336)	(1,598,316)
Total Direct Disaster Loans	12,948	6,857,925	6,870,873
Defaulted Guaranteed Business Loans & Other Loans Receivable			
Defaulted Guaranteed Business Loans	53,790	5,744,177	5,797,967
Other Loans Receivable (see note below)	–	655,911	655,911
Interest Receivable	655	25,754	26,409
Foreclosed Property	3,270	34,374	37,644
Allowance	(28,984)	(4,341,935)	(4,370,919)
Total Defaulted Guaranteed Business Loans & Other Loans Receivable	28,731	2,118,281	2,147,012
Total Credit Program Receivables & Related Foreclosed Property, Net			\$ 9,128,496

Note: Other Loan Receivables include payments advanced by the SBA against future reimbursements in the SBIC and 504 Guaranty Programs.

C. Loans Disbursed and Outstanding Loan Obligations

(Dollars in Thousands)

DIRECT LOANS

New Loans Disbursed During the Year Ending September 30,	2010	2009
Business Direct Loan Program	\$ 31,620	\$ 23,928
Disaster Loan Program	387,058	725,405
Total Direct Loans Disbursed	\$ 418,678	\$ 749,333
Outstanding Loan Obligations as of September 30,	2010	2009
Business Direct Loan Program	\$ 41,547	\$ 38,130
Disaster Loan Program	217,463	211,128
Total Direct Loan Obligations	\$ 259,010	\$ 249,258

GUARANTIED LOANS

New Loans Disbursed During the Year Ending September 30,	2010	2009
Total Principal Disbursed at Face Value	\$ 15,060,123	\$ 12,728,017
Total Principal Disbursed Guaranteed by the SBA	13,150,441	10,665,284
Outstanding Loan Obligations as of September 30,	2010	2009
Business Guaranteed Loan Programs	\$ 10,081,005	\$ 9,717,347
Loans Outstanding as of September 30,	2010	2009
Total Principal Outstanding at Face Value	\$ 76,247,818	\$ 74,856,050
Total Principal Outstanding Guaranteed by the SBA	64,433,140	62,203,856

D. Subsidy Cost Allowance Balances

(Dollars in Thousands)

FOR THE YEARS ENDING SEPTEMBER 30,	2010	2009
Post-1991 Business Direct and Purchased Guaranteed Loans		
Beginning Balance of Allowance Account	\$ 4,370,380	\$ 2,912,506
Current Year's Subsidy (see 6G for breakdown by component)	3,671	2,518
Loans Written Off	(2,425,174)	(1,486,461)
Subsidy Amortization	(2,583)	(2,028)
Allowance Related to Guaranteed Loans Purchased This Year	4,015,052	2,909,644
Miscellaneous Recoveries and Costs	41,835	29,531
Balance of Subsidy Allowance Account before Reestimates	6,003,181	4,365,710
Technical Assumptions/Default Reestimates	801	4,670
Ending Balance of Allowance Account	\$ 6,003,982	\$ 4,370,380
Post-1991 Disaster Direct Loans		
Beginning Balance of Allowance Account	\$ 1,597,336	\$ 1,574,082
Current Year's Subsidy (see 6G for breakdown by component)	47,079	111,638
Loans Written Off	(303,284)	(302,239)
Subsidy Amortization	(64,274)	(62,462)
Miscellaneous Recoveries and Costs	37,516	33,008
Balance of Subsidy Allowance Account before Reestimates	1,314,373	1,354,027
Technical Assumptions/Default Reestimates	161,293	243,309
Ending Balance of Allowance Account	\$ 1,475,666	\$ 1,597,336

E. Loan Guaranty Liability Balances

(Dollars in Thousands)

FOR THE YEARS ENDING SEPTEMBER 30,	2010	2009
Pre-1992 Business Loan Guaranties		
Beginning Balance of Liability for Loan Guaranties	\$ 809	\$ 816
Adjustment to Expected Losses, Guaranties Outstanding	(235)	(7)
Ending Balance of Liability for Loan Guaranties	574	809
Post-1991 Business Loan Guaranties		
Beginning Balance of Liability for Loan Guaranties	3,993,827	1,824,735
Current Year's Subsidy (see 6G for breakdown by component)	574,260	98,459
Loan Modifications	—	13,216
Fees	394,739	402,711
Interest Accumulation Factor	(31,617)	(59,446)
Claim Payments to Lenders	(4,925,476)	(3,913,241)
Adjustment Due to Reestimate & Guarantied Loan Purchases	910,425	1,003,597
Miscellaneous Recoveries and Costs	(64,707)	(61,040)
Balance of Liability for Loan Guaranties before Reestimates	851,451	(691,009)
Technical Assumptions/Default Reestimates	3,614,981	4,684,836
Ending Balance of Liability for Loan Guaranties	4,466,432	3,993,827
Total Ending Balance of Liability for Loan Guaranties	\$ 4,467,006	\$ 3,994,636

F. 2010 Subsidy Rates by Program and Component

LOAN PROGRAMS	Total Subsidy	Financing	Default	Other	Fee
Guaranty					
7(a)	0.46%	0.00%	4.34%	0.00%	-3.88%
7(a) Dealer Floor Plan	0.65%	0.00%	4.70%	0.00%	-4.05%
504 CDC	0.00%	0.00%	4.20%	0.32%	-4.52%
Disaster Gty - Immediate	2.83%	0.00%	2.83%	0.00%	0.00%
Disaster Gty - Expedited	2.14%	0.00%	2.14%	0.00%	0.00%
SBIC Debenture	0.00%	0.00%	4.83%	0.03%	-4.86%
Direct					
Disaster	10.77%	2.90%	11.86%	-3.99%	0.00%
Microloan	12.04%	2.12%	2.77%	7.15%	0.00%
ARRA Guaranty					
7(a)	4.23%	0.00%	6.07%	0.00%	-1.84%
504 CDC	2.05%	0.00%	4.08%	0.33%	-2.36%
504 1st Mortgage	0.00%	0.00%	0.92%	0.00%	-0.92%
ARC	76.15%	18.37%	57.78%	0.00%	0.00%
7(a) Dealer Floor Plan	3.40%	0.00%	4.76%	0.00%	-1.36%
ARRA Direct					
7(a) Broker/Dealer	-0.49%	-4.89%	0.04%	4.36%	0.00%
Microloan	12.04%	2.12%	2.77%	7.15%	0.00%

The subsidy rates in Table F pertain only to loans obligated in the current year. These rates cannot be applied to the loans disbursed during the current year to yield the subsidy expense because loans disbursed during the current year include loans obligated in prior years. Subsidy expenses reported in Table G result from the disbursement of loans obligated in the current year as well as in prior years, and include reestimates.

G. Subsidy Expense by Component

(Dollars in Thousands)

FOR THE YEARS ENDING SEPTEMBER 30,	2010	2009
Business Loan Guaranties		
Interest	\$ 40,675	\$ 2,707
Defaults	757,709	145,749
Fees	(232,850)	(52,746)
Other	8,726	2,749
Subsidy Expense Before Reestimates and Loan Modifications	574,260	98,459
Loan Modifications	-	13,216
Reestimates	3,614,981	4,684,836
Total Guaranteed Business Loan Subsidy Expense	\$ 4,189,241	\$ 4,796,511
Business Direct Loans		
Interest	\$ 1,730	\$ 1,966
Defaults	410	22
Other	1,531	530
Subsidy Expense Before Reestimates	3,671	2,518
Reestimates	801	4,670
Total Business Direct Loan Subsidy Expense	\$ 4,472	\$ 7,188
Disaster Direct Loans		
Interest	\$ 22,663	\$ 85,592
Defaults	42,449	68,446
Other	(18,033)	(42,400)
Subsidy Expense Before Reestimates	47,079	111,638
Reestimates	161,293	243,309
Total Disaster Direct Loan Subsidy Expense	\$ 208,372	\$ 354,947

H. Administrative Expense

The SBA received appropriations to administer its credit programs, including the making, servicing and liquidation of its loans and guaranties. Amounts expensed in the Statement of Net Cost are:

(Dollars in Thousands)

FOR THE YEARS ENDING SEPTEMBER 30,	2010	2009
Disaster Direct Loan Programs	\$ 203,716	\$ 251,999
Business Loan Programs	151,098	138,601
Total Administrative Expense	\$ 354,814	\$ 390,600

I. Credit Program Subsidy Reestimates

Reestimates are performed annually, on a cohort-by-cohort basis. The purpose of reestimates is to update original program cost estimates to reflect actual cash flow experience as well as changes in forecasts of future cash flows. Forecasts of future cash flows are updated based on additional information about historical program performance, revised expectations for future economic conditions, and enhancements to cash flow projection methods. Financial statement reestimates were performed using a full year of performance data for FY 2010 for SBA’s large loan programs and with nine months of actual and three months of projected performance data for the Secondary Market Guaranty and the small loan programs.

BUSINESS GUARANTIED LOAN PROGRAMS

Net subsidy reestimates of business guaranteed loan programs follows:

(Dollars in Thousands)

Guaranteed Loan Program Subsidy Reestimates	2010	2009
7(a)	\$ 1,483,646	\$ 2,030,243
7(a) Star	20,751	17,924
504 CDC	1,597,460	1,565,784
SBIC Debentures	40,407	66,598
SBIC Participating Securities	336,858	960,151
Secondary Market Guaranty Program	(8,208)	(50,803)
All Other Guaranty Loan Programs	(2,702)	(2,730)
7(a) - ARRA	(9,543)	72,430
504 CDC - ARRA	156,312	25,239
Total Guaranteed Loan Program Subsidy Reestimates	\$ 3,614,981	\$ 4,684,836

The 7(a) Loan Guaranty program, SBA’s flagship and largest program had a net upward reestimate in FY 2010 of \$1.5 billion. While the 2009 cohort performed better than expected in FY 2010, many earlier cohorts performed worse. Actual cohort performance, in particular performance of the 2005-2008 cohorts, made up a significant portion of the reestimate. The remainder of the reestimate was mostly due to updated model assumptions and methodologies, which will allow for more accurate projections of future cash flows. These methodology changes resulted in increased purchase projections for the remaining years within the cohorts.

The 504 Certified Development Companies program had a net upward reestimate of \$1.6 billion. While the 2009 cohort performed better than expected in FY 2010, many earlier cohorts performed worse. The majority of the reestimate was due to updated model assumptions and methodologies, which will allow for more accurate projections on future cash flows. These methodology changes resulted in increased purchase projections and decreased recovery projections for the remaining years within the cohorts. The remainder of the reestimate was mostly due to higher than projected purchases in FY 2010, in particular for cohorts 2005-2008.

The SBIC Debentures program had a net upward reestimate of \$40.4 million. The reestimate was mostly due to lower than projected recoveries during FY 2010 and a decrease in projected recoveries for the remaining years within the cohorts.

The SBIC Participating Securities program had a net upward reestimate of \$336.9 million. The reestimate was mostly due to the downturn in the economy that resulted in lower than projected recoveries and higher than projected purchases during FY 2010 and an increase in projected purchases for the remaining years within the cohorts.

The Secondary Market Guaranty program had a net downward reestimate of \$8.2 million. This downward reestimate was due in part to the lower than projected interest rate paid to investors during FY 2010 and a decrease in the projected interest rate paid to investors for the remaining years within the cohorts.

The 7(a) ARRA program had a net downward reestimate of \$9.5 million, due in part to better than projected performance in FY 2010. This includes loans funded from several appropriations during the year providing additional funds under ARRA provisions.

The 504 ARRA program had a net upward reestimate of \$156.3 million despite better than projected performance in FY 2010. The reestimate was due in large part to updated model assumptions and methodologies, which will allow for more accurate projections of future cash flows. These methodology changes resulted in increased purchase projections and decreased recovery projections for the remaining years within the cohorts.

BUSINESS DIRECT LOAN PROGRAMS

Net subsidy reestimates for business direct loan programs follows:

(Dollars in Thousands)

Business Direct Loan Program Subsidy Reestimates	2010	2009
7(m) Microloan	\$ 487	\$ 4,507
7(m) Microloan - ARRA	973	-
SBIC Preferred Stock	(708)	344
All Other Direct Loan Programs	49	(181)
Total Direct Loan Program Subsidy Reestimates	\$ 801	\$ 4,670

The 7(m) Direct Microloan program had a net upward reestimate of \$0.5 million. This reestimate was due in large part to the 2009 cohort that was reestimated for the first time this year. Actual purchase activity during FY 2010 altered the historical purchase curve causing projected purchases for the 2009 cohort to be greater than the original budget estimates.

The 7(m) Direct Microloan Recovery Act program had a net upward reestimate of \$1.0 million. This reestimate was also due in large part to the 2009 cohort that was reestimated for the first time this year. Actual purchase activity during FY 2010 altered the historical purchase curve causing projected purchases for the 2009 cohort to be greater than the original budget estimates.

DISASTER DIRECT LOAN PROGRAM

(Dollars in Thousands)

Disaster Direct Loan Program Subsidy Reestimates	2010	2009
Disaster	\$ 152,945	\$ 231,117
World Trade Center Disaster	8,348	12,192
Total Disaster Direct Loan Program Subsidy Reestimates	\$ 161,293	\$ 243,309

The Disaster program had a net upward reestimate of \$161.3 million primarily in the 2006 cohort, which mostly consists of loans for the Gulf Coast hurricanes of 2005. Loans in the 2006 cohort currently account for about 56 percent of the outstanding portfolio of Direct Disaster loans. The upward reestimate was primarily the result of performance probabilities being updated with actual performance during FY 2010 that resulted in an increase in projected defaults.

NOTE 7. General Property and Equipment, Net

The SBA capitalizes equipment with a cost of \$50,000 or more per unit and a useful life of 2 years or more at full cost and depreciated using the straight-line method over the useful life. The SBA expenses other equipment items not meeting the capitalization criteria when purchased.

Leasehold improvements with modifications of \$50,000 or more and a useful life of 2 years or more are capitalized and amortized using the straight-line method over the useful life of the improvement or the lease term, whichever is shorter. Other leasehold improvement expenditures not meeting the capitalization criteria are expensed.

Software intended for internal use, whether internally developed, contractor developed or purchased, is capitalized at cost if the initial unit acquisition cost is \$250,000 or more and service life is at least 2 years. Costs that do not meet the capitalization criteria are expensed when incurred.

Capitalized software costs include all direct and indirect costs incurred, including overhead, to develop the software. Software for internal use is amortized using the straight-line method over its useful life, not to exceed 5 years. Amortization begins when the software or equipment is put into production. The costs of enhancements are capitalized when it is more likely than not that the enhancements will result in significant additional capabilities.

Assets meeting the capitalization thresholds established at September 30, 2010 and 2009 are detailed below:

(Dollars in Thousands)

	2010	2009
Equipment	\$ 1,787	\$ 1,787
Accumulated Depreciation	(1,049)	(703)
Net	738	1,084
Leasehold Improvements - Construction in Progress	315	75
Leasehold Improvements	1,496	1,496
Amortization of Leasehold Improvements	(249)	(125)
Net	1,562	1,446
Software in Development	-	4,970
Software in Use	30,545	30,546
Amortization of Software in Use	(30,028)	(29,511)
Net	517	6,005
Total General Property and Equipment, Net	\$ 2,817	\$ 8,535

NOTE 8 Liabilities Not Covered by Budgetary Resources

Liabilities not covered by budgetary resources are liabilities for which congressional action is needed before budgetary resources can be provided. These unfunded liabilities at September 30, 2010 and 2009 consisted of:

(Dollars in Thousands)

	2010	2009
Intragovernmental Liabilities - Other		
Employment Taxes Payable	\$ 2,091	\$ 2,870
Federal Employee Compensation Act Payable	5,865	5,843
Total Intragovernmental Liabilities - Other	7,956	8,713
Federal Employee Compensation Act Actuarial Liability	29,960	29,640
Surety Bond Guarantee Program Future Claims	19,539	20,817
Other Liabilities		
Prior Liens on Real Estate Payable	409	409
Accrued Unfunded Annual Leave	26,758	25,314
Total Other Liabilities	27,167	25,723
Total Liabilities Not Covered by Budgetary Resources	\$ 84,622	\$ 84,893

The liability for Surety Bond Guarantees is an estimate of future claims in the SBG program for guaranties outstanding at year-end.

NOTE 9 Debt

Borrowings payable to the Treasury result from loans provided by the Treasury to fund the portion of direct loans not covered by subsidy appropriations and to fund the payment of downward subsidy reestimates and other credit program disbursements (see Note 15). The SBA makes periodic principal repayments to the Treasury based on the analysis of its cash balances and future disbursement needs.

Borrowings payable to the Federal Financing Bank are the result of its financing of SBA Section 503 Debentures issued prior to 1988.

All debt is intragovernmental and covered by budgetary resources. Debt transactions for the periods ending September 30, 2010 and 2009 and resulting balances are:

Intragovernmental Debt

(Dollars in Thousands)

	2010	2009
Department of Treasury		
Beginning Balance	\$ 10,872,754	\$ 9,462,882
New Borrowing	1,578,644	2,594,270
Repayments	(699,804)	(1,184,398)
Ending Balance	\$ 11,751,594	\$ 10,872,754
Federal Financing Bank		
Beginning Balance	\$ 5,529	\$ 10,345
Repayments	(3,249)	(4,667)
Change in Interest Payable	(93)	(149)
Ending Balance	\$ 2,187	\$ 5,529
Total Debt	\$ 11,753,781	\$ 10,878,283

NOTE 10 Net Assets of Liquidating Funds Due to Treasury

Net Assets of Liquidating Funds Due to Treasury is the residual of the book value of assets less liability in the Liquidating Funds for loans made prior to FY 1992. Subsequent to the issuance of its audited financial statements each year, the SBA returns to the Treasury the portion of this balance that is considered to be the unobligated balance for budgetary reporting at fiscal year-end.

(Dollars in Thousands)

AS OF SEPTEMBER 30,	2010	2009
Pollution Control Equipment Guaranty Fund	\$ 3,996	\$ 5,052
Disaster Loan Fund	14,428	18,489
Business Loan and Investment Fund	49,935	55,043
Total Due Treasury	\$ 68,359	\$ 78,584

NOTE 11 Other Liabilities

Other liabilities at September 30th were:

(Dollars in Thousands)

	2010	2009
OTHER LIABILITIES - INTRAGOVERNMENTAL		
Entity		
Current		
Employment Taxes Payable	\$ 3,977	\$ 3,457
Advances from Other Agencies	2,086	3,580
Total Current	6,063	7,037
Non-current		
Employment Taxes Payable	2,091	2,870
Federal Employee Compensation Act Payable	5,865	5,843
Payable to Federal Financing Bank	209	305
Total Non-current	8,165	9,018
Total Entity	14,228	16,055
Non-entity		
Current		
Payable to Treasury	6	7
Total Other Liabilities - Intragovernmental	\$ 14,234	\$ 16,062
OTHER LIABILITIES - PUBLIC		
Entity		
Current		
Accrued Funded Payroll and Benefits	\$ 19,967	\$ 15,158
Accrued Unfunded Annual Leave	26,758	25,314
Suspense Accounts	275	327
Total Current	47,000	40,799
Non-current		
Prior Liens on Real Estate Payable	409	409
Total Non-current	409	409
Total Entity	47,409	41,208
Non-entity		
Current		
Non-entity Current Payable	6	4
Total Other Liabilities - Public	\$ 47,415	\$ 41,212

NOTE 12 Leases

The SBA leases all of its facilities from the General Services Administration. The SBA enters into an Occupancy Agreement with GSA for each facility. GSA, in turn, leases commercial facilities or provides space in federal buildings. Agreements for space in federal buildings can be vacated with 120 to 180 days notice. However, the SBA anticipates continuing the same or similar facilities leases in the future. These leases with GSA are operating leases and are expensed in the Statement of Net Cost when incurred. FY 2010 and 2009 facilities lease costs were \$42.4 million and \$42.7 million. Future lease payments shown below assume a 3 percent inflation factor from the following years' projected totals as estimated by GSA. The downward trend after 2015 is due to the expiration of a number of leases.

(Dollars in Thousands)

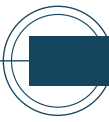
FUTURE FACILITIES OPERATING LEASE PAYMENTS

FY	Lease Pmts
2011	\$ 46,117
2012	47,500
2013	48,925
2014	50,393
2015	51,905
After 2015	39,451
Total	\$ 284,291

NOTE 13 Non-entity Reporting

Non-entity Assets are assets held by the SBA but not available to the SBA. The primary non-entity asset held by the SBA is Fund Balance with the Treasury held in the Treasury general fund accounts specifically established for SBA's downward subsidy reestimates for its discretionary loan programs. Because the loan programs are discretionary, the downward reestimates are not available to the SBA and they are returned to the Treasury in the fiscal year following the accrual of the reestimates. During the year, these general fund accounts contain SBA's prior year reestimates. At year-end, the funds are swept by the Treasury with the exception of one deposit fund. Also at year-end, the SBA accrues the current year's reestimates, including downward reestimates as applicable. For the downward reestimates, in the loan financing funds, the SBA records an accrual adjustment that records a transfer out to the non-entity fund, a reduction of subsidy allowance or loan guarantee liability, and an account payable to the non-entity fund. In the loan program funds the SBA records a reduction of loan subsidy expense and the associated impact on the net cost. The non-entity Treasury general funds contain a corresponding account receivable in anticipation of the receipt of the downward reestimates in the following year and a Downward Reestimate Payable to Treasury.

For consolidated financial statement presentation, the SBA eliminates the payable to the non-entity fund and the non-entity Treasury general fund receivable from the financing funds; since both are included in SBA's reporting entity. The Downward Reestimate Payable to Treasury in the non-entity Treasury general fund is not eliminated and is reflected on the Balance Sheet as a liability line item.



(Dollars in Thousands)

	2010	2009
Entity		
Financing Fund Payable	\$ (130,993)	\$ (64,875)
Non-entity		
Miscellaneous Receipts Fund Receivable	130,993	64,875
Downward Reestimate Payable to Treasury	(130,993)	(64,875)
Balance Sheet Reported Payable	\$ (130,993)	\$ (64,875)

NOTE 14 Consolidated Statement of Net Cost

Federal cost accounting standards require the SBA to report operating costs by strategic goal activity. Full costs include all direct and indirect costs for a strategic goal. Full costs are reduced by exchange (earned) revenues to arrive at net operating cost.

Operating Cost

The full and net operating costs of SBA’s major strategic goals are presented in the Consolidated Statement of Net Cost. Full costs are comprised of all direct costs for the strategic goals and those indirect costs which can be reasonably assigned or allocated to the strategic goals, including employee pension and other retirement benefit costs paid by the OPM and charged to the SBA.

Earned Revenue

Earned revenues arise from exchange transactions, and are deducted from the full cost of SBA’s major strategic goals to arrive at net strategic goals costs. The SBA recognizes earned revenues when reimbursements are payable from other federal agencies and the public, as a result of costs incurred or services performed. A major source of earned revenue includes interest earned on SBA’s outstanding Business and Disaster loan portfolios and interest earned on uninvested funds in the credit reform financing accounts.

Reporting by Strategic Goal

The SBA reports costs consistent with its three strategic goals. The costs of Goal 4, to ensure that all SBA strategic goals operate at maximum efficiency and effectiveness by providing them with high quality executive leadership and support services, are fully allocated to the other three strategic goals. Goal 4 costs are estimated at \$146.3 million and \$121.5 million for FY 2010 and FY 2009. Costs Not Assigned to Strategic Goals on the Statement of Net Cost includes costs of congressionally mandated grant programs and the Office of the Inspector General.

Intragovernmental Gross Cost is cost incurred by the SBA in exchange transactions with other federal agencies. Gross Cost with the Public is cost incurred by the SBA in exchange transactions. Intragovernmental Earned Revenue is revenue earned by the SBA in exchange transactions with other federal agencies. Earned Revenue from the Public is revenue earned by the SBA in exchange transactions.

The classification as Intragovernmental Costs or Gross Cost with the Public relate to the source of goods and services received by the SBA and not to the classification of related revenue. The classification of revenue or cost being defined as “intragovernmental” or “public” is defined on a transaction by transaction basis. The purpose of this classification is to enable the federal government to provide consolidated financial statements, and not to match the public and intragovernmental revenue with costs that are incurred to produce public and intragovernmental revenue.

(Dollars in Thousands)

INTRAGOVERNMENTAL COSTS AND EXCHANGE REVENUE

FOR THE YEARS ENDING SEPTEMBER 30,

2010

2009

STRATEGIC GOAL 1:**Expand America's Ownership Society, Particularly in Underserved Markets**

Intragovernmental Gross Cost	\$ 303,718	\$ 237,923
Gross Cost with the Public	4,693,371	5,172,008
Total Strategic Goal 1 Gross Cost	4,997,089	5,409,931
Intragovernmental Earned Revenue	187,036	113,832
Earned Revenue from the Public	71,313	52,511
Total Earned Revenue Strategic Goal 1	258,349	166,343

STRATEGIC GOAL 2:**Provide Timely Financial Assistance to Homeowners, Renters, Nonprofit Organizations and Businesses Affected by Disaster**

Intragovernmental Gross Cost	\$ 419,946	\$ 479,914
Gross Cost with the Public	394,505	601,318
Total Strategic Goal 2 Gross Cost	814,451	1,081,232
Intragovernmental Earned Revenue	60,803	74,732
Earned Revenue from the Public	306,935	331,172
Total Earned Revenue Strategic Goal 2	367,738	405,904

STRATEGIC GOAL 3:**Improve Economic Environment for Small Business**

Intragovernmental Gross Cost	\$ 3,911	\$ 3,348
Gross Cost with the Public	13,903	11,158
Total Strategic Goal 3 Gross Cost	17,814	14,506

Cost Not Assigned to Strategic Goals

Intragovernmental Gross Cost	\$ 16,232	\$ 14,375
Gross Cost with the Public	57,698	47,919
Total Gross Cost Not Assigned to Strategic Goal	73,930	62,294

Net Cost of Operations

\$ 5,277,197	\$ 5,995,716
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NOTE 15 Statement of Budgetary Resources

The Statement of Budgetary Resources presents information about total budgetary resources available to the SBA and the status of those resources as of September 30, 2010 and 2009. SBA's total budgetary resources were \$8.4 billion and \$5 billion for the years ended September 30, 2010 and 2009. Additionally, \$10 billion and \$7.4 billion of nonbudgetary resources including borrowing authority and collections of loan principal, interest and fees in financing funds were reported for the years ended September 30, 2010 and 2009.

Adjustments to Beginning Balance of Budgetary Resources

The SBA made no adjustments to the beginning budgetary resources during the years ended September 30, 2010 and 2009.

Permanent Indefinite Appropriations

The SBA receives permanent indefinite appropriations annually to fund increases in the projected subsidy costs of loan programs as determined by the reestimation process required by the Federal Credit Reform Act of 1990. The appropriations are received initially in the SBA Program Funds and then transferred to the Financing Funds where they are used to fund obligations. SBA's Liquidating Funds also receive permanent indefinite appropriations to fund obligations. The Financing Funds are used to account for credit program obligations made subsequent to FY 1991. Liquidating Funds are used to account for credit program obligations made prior to FY 1992.

Decreases in projected subsidy costs in the Financing Funds are returned to the Treasury through SBA's annual reestimation process. The prior year's ending unobligated balances in SBA's Liquidating Funds are also transferred to the Treasury annually.

Borrowing Authority and Terms of Borrowing

The SBA is authorized to borrow from the Treasury's Bureau of Public Debt when funds needed to disburse direct loans and purchase guaranteed loans exceed subsidy costs and collections in the non-budgetary loan financing funds. In FY 2010 and 2009, the SBA received \$2.7 billion and \$3.5 billion of borrowing authority from the OMB. The SBA pays interest to the Treasury based on Treasury's cost of funds. The rate at which interest is paid to the Treasury on the amounts borrowed (or received from the Treasury on uninvested cash balances) in a loan financing fund for a particular cohort is a disbursement-weighted average discount rate for cohorts prior to FY 2001 and a single effective rate for cohorts beginning with FY 2001. The SBA calculates and repays borrowings not needed for working capital at midyear for prior year cohorts. The SBA uses the loan principal, interest and fees collected from the borrowers in its loan financing funds to repay its Treasury borrowings. The repayment maturity dates for the borrowing from the Treasury are based on the loan maturities used in the subsidy calculation. The maturities range from 16 years for Direct Business loans, 25 years for Guaranteed Business loans and 30 years for Disaster loans.

Apportionment Categories of Obligations Incurred

During FY 2010 and FY 2009, the SBA incurred \$13.1 billion and \$9.6 billion of direct and reimbursable obligations of which \$0.9 billion and \$0.7 billion was apportioned in category A; \$12.2 billion and \$8.9 billion were apportioned in category B. Category A apportionments are restricted by quarter and program; Category B apportionments are restricted by purpose and program.

Unobligated Balances

Unobligated balances at September 30, 2010 and 2009 are \$5.2 billion and \$2.7 billion which include \$3.0 billion and \$1.3 billion of unavailable unobligated balances. These balances are unavailable primarily because they are unapportioned by OMB. The SBA accumulates the majority of these unobligated balances in its nonbudgetary financing accounts during the fiscal year (\$3.5 billion in FY 2010 and \$1.2 billion in FY 2009) from reestimates that are used primarily to pay default claims in the following fiscal year. In addition, unobligated balances are accumulated in budgetary accounts from appropriations (\$1.8 billion in FY 2010 and \$1.5 billion in FY 2009) that are used to finance SBA's ongoing program operations.

Undelivered Orders

Undelivered orders for the periods ended September 30, 2010 and 2009 were \$0.9 billion and \$0.8 billion.

Differences between the Statement of Budgetary Resources and the Budget of the U. S. Government

There was no material difference between the FY 2009 Statement of Budgetary Resources and the President's FY 2011 budget submission. The President's Budget with actual numbers for FY 2012 has not yet been published. The SBA expects no material differences between the President's Budget "actual" column and the FY 2010 reported results when the budget becomes available in February 2011.

NOTE 16 Reconciliation of Budgetary Obligations Incurred to Net Cost of Operations

The SBA presents the Statement of Net Cost using the accrual basis of accounting. This differs from the obligation-based measurement of total resources supplied, both budgetary and from other sources, on the Statement of Budgetary Resources.

The Federal Financial Accounting Standard No. 7 requires "a reconciliation of proprietary and budgetary information in a way that helps users relate the two." The focus of this presentation is to reconcile budgetary net obligations to the net cost of operations. The objective of this information is to categorize the differences between budgetary and financial (proprietary) accounting.

CONSOLIDATED RECONCILIATION OF BUDGETARY OBLIGATIONS TO NET COST

For the years ended September 30, 2010 and 2009

(Dollars in Thousands)

	2010	2009
RESOURCES USED TO FINANCE ACTIVITIES		
Budgetary Resources Obligated		
Obligations Incurred	\$ 13,113,785	\$ 9,635,132
Less: Spending Authority from Offsetting Collections and Recoveries	8,231,003	4,946,652
Obligations Net of Offsetting Collections and Recoveries	4,882,782	4,688,480
Less: Offsetting Receipts	78,001	489,395
Net Obligations	4,804,781	4,199,085
Other Resources		
Imputed Financing	32,765	25,549
Other Financing Sources	(144,780)	(88,187)
Net Other Resources Used to Finance Activities	(112,015)	(62,638)
Total Resources Used to Finance Activities	4,692,766	4,136,447
RESOURCES THAT DO NOT FINANCE NET COST OF OPERATIONS		
(Increase) Decrease in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered But Not Yet Provided	(74,812)	193,832
Resources that Fund Expenses Recognized in Prior Periods	(4,637,929)	(1,313,301)
Budgetary Offsetting Collections and Receipts that Do Not Affect Net Cost of Operations		
Credit Program Collections	7,823,359	4,042,182
Offsetting Receipts	78,001	489,395
Resources that Finance the Acquisition of Assets or Liquidation of Liabilities	(6,406,831)	(6,189,101)
Other - Current Year Liquidating Equity Activity	760	863
Other Resources that Do Not Affect Net Cost of Operations	(15)	(100)
Total Resources that Do Not Finance Net Cost of Operations	(3,217,467)	(2,776,230)
Total Resources Used to Finance the Net Cost of Operations	1,475,299	1,360,217
COMPONENTS OF THE NET COST OF OPERATIONS THAT WILL NOT REQUIRE OR GENERATE RESOURCES IN THE CURRENT PERIOD		
Components Requiring or Generating Resources in Future Periods		
Change in Annual Leave Liability	1,444	767
Upward Reestimates of Credit Subsidy Expense	3,796,430	4,637,148
Change in Revenue Receivable from Public	(249)	(3,623)
Provision for Losses on Estimated Guaranties	(1,278)	(3,947)
Change in Unfunded Employee Benefits	320	2,579
Total Components Requiring or Generating Resources in Future Periods	3,796,667	4,632,924
Components Not Requiring or Generating Resources		
Depreciation or Amortization	987	987
Change in Bad Debt Expense - Pre-1992 Loans	3,721	2,094
Other (Income) Expenses Not Requiring Budgetary Resources	523	(507)
Total Components Not Requiring or Generating Resources	5,231	2,574
Total Components of the Net Cost of Operations that Will Not Require or Generate Resources in the Current Period	3,801,898	4,635,499
Net Cost of Operations	\$ 5,277,197	\$ 5,995,716

Liabilities Not Covered by Budgetary Resources on the Balance Sheet (Note 8) differs from Components Requiring or Generating Resources in Future Periods in this reconciliation primarily due to reestimated subsidy costs of loan programs. The subsidy costs are shown in the Statement of Net Cost and are to be covered by budgetary resources but these resources, while available under permanent and indefinite authority, were not provided by year-end. Additionally, there will always be a difference for existing liabilities because the Reconciliation of Budgetary Obligations Incurred to Net Cost of Operations reports only current year changes, not balances.

The following table details these differences:

(Dollars in Thousands)

AS OF SEPTEMBER 30,	2010	2009
Current Year Liabilities Not Covered By Budgetary Resources	\$ 84,622	\$ 84,893
Less: Prior Year	84,893	86,918
Change in Liabilities Not Covered By Budgetary Resources	(271)	(2,025)
Upward Reestimates of Credit Subsidy Expense	3,796,430	4,637,148
Change in Revenue Receivable from Public	(249)	(3,623)
All Other	757	1,424
Components (of Net Cost) Generating Resources in Future Periods (Per Reconciliation Above)	\$ 3,796,667	\$ 4,632,924

NOTE 17 Significant Events

Recovery Act Extensions

The President signed the American Recovery and Reinvestment Act on February 17, 2009. The ARRA provided \$730 million to the SBA to alleviate the effect of the economic recession on American small business. Of the ARRA funding, \$375 million was provided to temporarily reduce fees on 7(a) and 504 guaranteed loans and increase the guaranty percentage on 7(a) loans. Although the \$375 million was scheduled to be available until September 30, 2010, the funds were exhausted during November 2009 and ARRA lending was suspended. The U. S. Congress subsequently provided an additional \$305 million through several appropriations to extend ARRA lending. On May 31, 2010 the temporary authority to increase the 7(a) guaranty percentage expired, contributing to a reduction in SBA guaranteed loan volume during the last four months of FY 2010. The President signed the Jobs Bill on September 27, 2010; the bill provides \$505 million of additional funding under ARRA provisions which will be used during FY 2011. The short term ARRA funding extensions during FY 2010 required several changes to SBA's financial management systems to account for these funds. In addition, SBA's funds control system was enhanced in order to control the use of these short term funding extensions of ARRA provisions.

Economic Conditions

While the economy was no longer in a recession during FY 2010 as evidenced by an increase in GDP, unemployment remained high throughout the fiscal year. These macroeconomic factors had an impact on the FY 2010 performance of SBA's loan portfolio. Despite the increase in GDP in FY 2010, the high unemployment rate contributed to an increase in purchases of defaulted guaranties. The Mid-Session Review Economic Assumptions continue to show higher unemployment forecasts as compared to last year's forecasts, which increase projections for future purchases. This factor contributed to the upward reestimate in the SBA loan programs (as discussed in Note 6I). Future updates to economic forecasts that drive model projections may result in large swings in reestimates. Under the Federal Credit Reform Act, upward reestimates are automatically covered by permanent indefinite budget authority. Such authority provides the SBA resources to address losses incurred in its existing portfolio without further action by Congress.

Financial Management System

During FY 2010, in accordance with OMB guidance, the SBA reviewed and subsequently discontinued its ongoing loan and financial system modernization project to develop an integrated Loan Management and Accounting System. As a result, the \$5.2 million accumulated cost to develop LMAS was written off to expense in the FY 2010 results. Instead of LMAS, the Agency plans to focus on migrating its loan and financial systems from its mainframe platform to improve their efficiency and reliability and to continue the upgrade of its Joint Accounting and Administrative Management System administrative accounting system by implementing the latest version of the Oracle Federal Financials software.

*Did
you
know*

It's important to be where your customers are — online! Google and the SBA have partnered to educate local businesses about how to succeed online. Learn more at <http://www.google.com/help/places/partners/sba>.

Required Supplementary Information

Combining Statement of Budgetary Resources

For the year ended September 30, 2010

(Dollars in Thousands)

	BLIF		DLF		SBGRF	PCECGF
	Budgetary	Nonbudgetary Financing	Budgetary	Nonbudgetary Financing	Budgetary	Budgetary
BUDGETARY RESOURCES						
Unobligated Balance						
Brought Forward October 1	\$ 336,149	\$ 556,036	\$ 858,774	\$ 639,275	\$ 49,396	\$ 3,195
Recoveries of Prior Year Obligations	17,052	3,311	11,810	78,293	–	–
Budget Authority						
Appropriations Received	5,576,868	–	315,513	–	1,000	2,000
Borrowing Authority	–	1,736,548	–	1,001,411	–	–
Spending Authority from Offsetting Collections						
Earned	9,785	6,598,773	3,806	1,224,586	10,205	225
Change in Unfilled Customer Orders	–	1,539	–	(7,110)	–	–
Total Budget Authority	5,586,653	8,336,860	319,319	2,218,887	11,205	2,225
Permanently Not Available	(10,485)	(554,488)	(5,575)	(1,304,624)	–	(3,195)
Total Budgetary Resources	\$ 5,929,369	\$ 8,341,719	\$ 1,184,328	\$ 1,631,831	\$ 60,601	\$ 2,225
STATUS OF BUDGETARY RESOURCES						
Obligations Incurred, Net						
Direct	\$ 5,127,072	\$ 5,644,872	\$ 288,335	\$ 870,303	\$ –	\$ –
Reimbursable	153,210	–	86,588	–	4,345	–
Total Obligations Incurred, Net	5,280,282	5,644,872	374,923	870,303	4,345	–
Unobligated Balances, Available	75,950	1,429,802	50,400	631,107	9,856	2,225
Unobligated Balances, Not Available	573,137	1,267,045	759,005	130,421	46,400	–
Total Status of Budgetary Resources	\$ 5,929,369	\$ 8,341,719	\$ 1,184,328	\$ 1,631,831	\$ 60,601	\$ 2,225
CHANGE IN OBLIGATED BALANCES						
Obligated Balance Brought Forward, Net October 1						
Unpaid Obligations Brought Forward	\$ 206,486	\$ 174,960	\$ 32,643	\$ 214,974	\$ 18	\$ –
Uncollected Customer Payments from Federal Sources Brought Forward	–	(203,903)	–	(31,971)	–	–
Total Obligated Balance Brought Forward, Net	206,486	(28,943)	32,643	183,003	18	–
Obligations Incurred	5,280,282	5,644,872	374,923	870,303	4,345	–
Gross Outlays	(5,261,352)	(5,592,264)	(370,406)	(787,655)	(4,257)	–
Recoveries of Prior Year Unpaid Obligations	(17,052)	(3,311)	(11,810)	(78,293)	–	–
Change in Uncollected Customer Payments from Federal Sources	–	(1,539)	–	7,110	–	–
Obligated Balance, Net, End of Period						
Unpaid Obligations	208,364	224,257	25,350	219,329	106	–
Uncollected Customer Payments from Federal Sources	–	(205,442)	–	(24,861)	–	–
Total Obligated Balance, Net, End of Period	\$ 208,364	\$ 18,815	\$ 25,350	\$ 194,468	\$ 106	\$ 0
NET OUTLAYS						
Gross Outlays	\$ 5,261,352	\$ 5,592,264	\$ 370,406	\$ 787,655	\$ 4,257	\$ –
Offsetting Collections	(9,785)	(6,598,773)	(3,806)	(1,224,586)	(10,205)	(225)
Net Outlays Before Offsetting Receipts	5,251,567	(1,006,509)	366,600	(436,931)	(5,948)	(225)
Offsetting Receipts	–	(54,116)	–	(23,775)	–	–
Net Outlays	\$ 5,251,567	\$ (1,060,625)	\$ 366,600	\$ (460,706)	\$ (5,948)	\$ (225)

Combining Statement of Budgetary Resources

For the year ended September 30, 2010

(Dollars in Thousands)

	SE	OIG	BATF	TOTAL	TOTAL	
	Budgetary	Budgetary	Budgetary	Budgetary	Nonbudgetary Financing	Total
BUDGETARY RESOURCES						
Unobligated Balance						
Brought Forward October 1	\$ 243,472	\$ 15,363	\$ 263	\$ 1,506,612	\$ 1,195,311	\$ 2,701,923
Recoveries of Prior Year Obligations	24,065	252	–	53,179	81,604	134,783
Budget Authority						
Appropriations Received	642,438	16,300	–	6,554,119	–	6,554,119
Borrowing Authority	–	–	–	–	2,737,959	2,737,959
Spending Authority from Offsetting Collections						
Earned	369,966	1,014	24	395,025	7,823,359	8,218,384
Change in Unfilled Customer Orders	(116,682)	89	–	(116,593)	(5,571)	(122,164)
Total Budget Authority	895,722	17,403	24	6,832,551	10,555,747	17,388,298
Permanently Not Available	(5,767)	(101)	–	(25,123)	(1,859,112)	(1,884,235)
Total Budgetary Resources	\$ 1,157,492	\$ 32,917	\$ 287	\$ 8,367,219	\$ 9,973,550	\$ 18,340,769
STATUS OF BUDGETARY RESOURCES						
Obligations Incurred, Net						
Direct	\$ 546,779	\$ 19,444	\$ 45	\$ 5,981,675	\$ 6,515,175	\$ 12,496,850
Reimbursable	371,558	1,234	–	616,935	–	616,935
Total Obligations Incurred, Net	918,337	20,678	45	6,598,610	6,515,175	13,113,785
Unobligated Balances, Available	70,508	6,292	242	215,473	2,060,909	2,276,382
Unobligated Balances, Not Available	168,647	5,947	–	1,553,136	1,397,466	2,950,602
Total Status of Budgetary Resources	\$ 1,157,492	\$ 32,917	\$ 287	\$ 8,367,219	\$ 9,973,550	\$ 18,340,769
CHANGE IN OBLIGATED BALANCES						
Obligated Balance Brought Forward, Net October 1						
Unpaid Obligations Brought Forward	\$ 370,986	\$ 3,318	\$ 27	\$ 613,478	\$ 389,934	\$ 1,003,412
Uncollected Customer Payments from						
Federal Sources Brought Forward	–	–	–	–	(235,874)	(235,874)
Total Obligated Balance Brought Forward, Net	370,986	3,318	27	613,478	154,060	767,538
Obligations Incurred	918,337	20,678	45	6,598,610	6,515,175	13,113,785
Gross Outlays	(825,985)	(20,805)	(50)	(6,482,855)	(6,379,919)	(12,862,774)
Recoveries of Prior Year Unpaid Obligations	(24,065)	(252)	–	(53,179)	(81,604)	(134,783)
Change in Uncollected Customer Payments from						
Federal Sources	–	–	–	–	5,571	5,571
Obligated Balance, Net, End of Period						
Unpaid Obligations	439,273	2,939	22	676,054	443,586	1,119,640
Uncollected Customer Payments from Federal						
Sources	–	–	–	–	(230,303)	(230,303)
Total Obligated Balance, Net, End of Period	\$ 439,273	\$ 2,939	\$ 22	\$ 676,054	\$ 213,283	\$ 889,337
NET OUTLAYS						
Gross Outlays	\$ 825,985	\$ 20,805	\$ 50	\$ 6,482,855	\$ 6,379,919	\$ 12,862,774
Offsetting Collections	(253,283)	(1,102)	(24)	(278,430)	(7,823,359)	(8,101,789)
Net Outlays Before Offsetting Receipts	572,702	19,703	26	6,204,425	(1,443,440)	4,760,985
Offsetting Receipts	(110)	–	–	(110)	(77,891)	(78,001)
Net Outlays	\$ 572,592	\$ 19,703	\$ 26	\$ 6,204,315	\$ (1,521,331)	\$ 4,682,984

Required Supplementary Stewardship Information

Stewardship Investments in Human Capital

Five years ending September 30, 2010

Human Capital investments are expenses included in net cost for education and training programs that are intended to increase or maintain national economic productive capacity and that produce outputs and outcomes that provide evidence of maintaining or increasing national productive capacity. The definition excludes education and training expenses for Federal personnel.

Small Business Development Centers deliver management and technical assistance, economic development and management training to existing and prospective small businesses through cooperative agreements with universities and colleges and government organizations.

SCORE is a nonprofit organization which provides small business counseling and training under a grant from the SBA. SCORE members are successful business men and women who volunteer their time to assist aspiring entrepreneurs and small business owners. There are SCORE chapters in every state.

Women's Business Centers provide assistance to women business owners and acts as their advocate in the public and private sectors in a number of locations around the U.S.

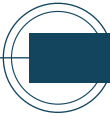
All Other Training and Assistance Programs includes primarily Small Business Training provided by a counselor from a resource partner, district office, or SBA sponsor who delivers a structured program of knowledge, information or experience on a business-related subject. The training lasts for one or more hours and includes an agenda, attendee list, and a trainer evaluation. The session may be for an individual or a class. Training is also available online on a number of subjects of interest to the small business person. Other programs not separately detailed include Native American Outreach and Drug Free Work Place. As additional years of data accumulate, the investments will be presented separately.

Additional information on these programs is provided in the Management Discussion and Analysis section of this Agency Financial Report.

Significant Human Capital investments occur within the following programs:

(Dollars in Thousands)

	2010	2009	2008	2007	2006
Small Business Development Centers	\$ 130,046	\$ 116,909	\$ 98,484	\$ 99,748	\$ 105,743
SCORE	11,134	9,899	10,960	12,267	15,285
Women's Business Centers	16,924	21,504	23,655	16,382	10,382
All Other Training and Assistance Programs	81,057	61,356	41,318	62,787	24,513
Total	\$ 239,161	\$ 209,668	\$ 174,417	\$ 191,184	\$ 155,923



OFFICE OF THE INSPECTOR GENERAL REPORTS

Success Story



Successful Entrepreneur Finds His Own “Land of Opportunity”

ETC Engineers & Architects, Inc., Little Rock, Arkansas

From the day he first set foot in the state, Mizan Rahman knew he'd find success in Arkansas, a state formerly nicknamed the “Land of Opportunity.” The owner and president of ETC Engineers and Architects, Inc., Rahman relied on his engineering instincts: it takes time and teamwork to build something good that will last.

ETC Engineers and Architects, Inc. is one of central Arkansas' foremost civil engineering companies. The company currently employs 13 engineers, architects and support staff specializing in designing roads, water systems and sewage systems.

The successful company has taken years to build. Born in Bangladesh and later graduating from a university there, Rahman applied for and received a United States Agency for International Development in-service training scholarship. His scholarship was canceled in 1971 because of a civil war between Pakistan and Bangladesh, then known as East Pakistan, but Mizan Rahman moved on to a post at the U.S. Geological Survey, and took a job testing water quality at its laboratory in Little Rock.

As the years rolled by, Rahman married, took his first job with an engineering firm, and completed a master's degree in civil engineering and an MBA before he decided to open his own firm. A \$36,000 SBA-backed line of credit was enough to open ETC Engineers and Architects, Inc. in 1978. The company has also benefited from the 8(a) Business Development program and graduated from the program in 1994. The program helped Rahman compete in the American economy and access the federal contracting market.

Summary of OIG Audit Follow-up

Throughout the year, the OIG conducts audits of SBA's processes, procedures and programs, and makes recommendations for improvement. Many of these recommendations are not material, relative to their dollar impact on SBA's financial and administrative operation, but are beneficial to SBA's management. If SBA management disagrees with an OIG recommendation, the OIG may revise the recommendation or refer the issue to a higher level of SBA management. When both SBA management and the OIG agree on the recommendation, SBA management develops a corrective action plan, including a target date for completion. This recommendation is identified as having a "Management Decision." When the corrective action plan is implemented and the recommendation has been fully addressed, the recommendation is identified as having a "Final Action."

The OCFO maintains a database to track the recommendations through to the conclusion, or Final Action. During FY 2010, there were 156 Final Actions, resulting from 12 monetary and 144 non-monetary recommendations. The status of the corrective actions is updated regularly and is available for review on the SBA Intranet. The status of all audit recommendations is reconciled with the OIG to ensure actions are posted promptly and accomplished in accordance with the agreed-upon target dates.

The following two tables reflect SBA's monetary final action activity for FY 2010. Detailed information on the final action activity and the status of corrective action plans not implemented within one year can be found in the CD that accompanies this Agency Financial Report.

TABLE 1.

Final Action on Audit Recommendations with Disallowed / Questioned Costs October 1, 2009 – September 30, 2010		
	Number of Recommendations	Disallowed Costs (Rounded to Thousands)
A. Recommendations with management decisions on which final action had not been taken at the beginning of the period.	5	\$1,826
B. Recommendations on which management decisions were made during the period.	3	1,904
C. Total recommendations pending final action during period.	8	\$3,730
D. Recommendations on which final action was taken during the period.		
1. Recoveries:		
(a) Collections and Offsets	4	1,854
(b) Property		
(c) Other		
2. Write-Offs	3	626
3. Total	7	\$2,480
E. Recommendations needing final action at the end of the period.	1	\$1,250

TABLE 2.

Final Action on Audit Recommendations with Funds Put To Better Use October 1, 2009 – September 30, 2010		
	Number of Recommendations	Funds to be Put to Better Use (Rounded to Thousands)
A. Recommendations with management decisions on which final action had not been taken at the beginning of the period.	5	\$1,550,335
B. Recommendations on which management decisions were made during the period.	0	
C. Total recommendations pending final action during period.	5	\$1,550,335
D. Recommendations on which final action was taken during the period.		
1. Value of recommendations implemented (completed).	4	1,547,644
2. Value of recommendations that management concluded should not or could not be implemented or completed.	1	2,691
3. Total	5	\$1,550,335
E. Recommendations needing final action at the end of the period.	0	\$0

OIG Report on the Most Serious Management and Performance Challenges



U.S. SMALL BUSINESS ADMINISTRATION

OFFICE OF INSPECTOR GENERAL

Report No. 11-01

*Fiscal Year 2011 Report
on the Most Serious Management and
Performance Challenges Facing the
Small Business Administration*

October 15, 2010

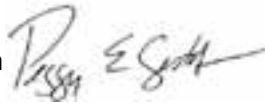
U.S. SMALL BUSINESS ADMINISTRATION
OFFICE OF INSPECTOR GENERAL
WASHINGTON, D.C. 20416

October 15, 2010

MEMORANDUM

TO: Karen G. Mills
Administrator

FROM: Peggy E. Gustafson
Inspector General



SUBJECT: Fiscal Year 2011 Report on the Most Serious Management and
Performance Challenges Facing the Small Business Administration

In accordance with the Reports Consolidation Act of 2000, we are providing you with the Office of Inspector General's (OIG) Fiscal Year (FY) 2011 Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration (SBA). This report represents our current assessment of Agency programs and/or activities that pose significant risks, including those that are particularly vulnerable to fraud, waste, error, mismanagement or inefficiencies. The Challenges are not presented in order of priority, as we believe that all are critical management or performance issues.

Our report is based on specific OIG, Government Accountability Office (GAO), and other official reports, as well as our general knowledge of SBA's programs and operations. Our analysis generally considers those accomplishments that SBA reported as of September 30, 2010.

Within each Management Challenge there are a series of "recommended actions" to resolve the Challenge. Each recommended action is assigned a color "status" score. The scores are as follows: Green for Implemented; Yellow for Substantial Progress; Orange for Limited Progress; and Red for No Progress. An upwards arrow in the color box indicates that the color score improved over last year's report, and a down arrow indicates that it regressed.

As part of the OIG's continuing evaluation of the Management Challenges, certain Challenges have been updated or revised. In addition, actions that were scored Green last year, and which remained Green this year, have been moved up to the "history bar" above the recommended actions. The history bar highlights any progress that the Agency has made on a Challenge over the past four FYs (or as long as the Challenge has existed, if shorter) by showing the number of actions that have moved to Green each year.

We are pleased to report that one Management Challenge in last year's report, *Insufficient and Outdated SBA Controls Contribute to Excessive Risk of the SBIC Program*, has been completed by virtue of both remaining recommended actions receiving Green color scores this year. The OIG determined that SBA (1) was actively monitoring and timely transferring impaired Small Business Investment Companies (SBICs) to liquidations when warranted and (2) had developed performance goals and indicators to evaluate effectiveness of the liquidation process of SBICs and was reporting annually on whether these goals had been met. This Challenge has been shown as "completed" in the attached report and the remaining Challenges have been renumbered accordingly.

The following table provides a summary of the FY 2011 report on the Agency's Most Serious Management and Performance Challenges.

	Topic	Status Score				Improved ¹	Worsened ²
		Green	Yellow	Orange	Red		
1	Small Business Contracts		2	1			
2	IT Security		3	1			1
3	Human Capital		2	1			1
4	Loan Guaranty Purchase	1		1		1	
5	Lender Oversight		4	2		2	
6	8(a) BD Program		3	1			1
7	Loan Agent Fraud		2			2	
8	Loan Management and Accounting System			4		— ³	
9	Improper Payments	1	3	3		— ⁴	
Completed Challenge							
	SBIC Program	2				2	
	TOTAL	4	18	14		7	3

We would like to thank SBA's management and staff for their cooperation in providing us with information needed to prepare this report. We look forward to continuing to work with SBA's leadership team in addressing the Agency's Management Challenges.

Attachment

¹ "Improved" refers to a recommended action that showed progress this year over last year's score (as denoted by an "up" arrow).
² "Worsened" refers to a recommended action that regressed from last year's score (as denoted by a "down" arrow).
³ Management Challenge 8, Loan Management and Accounting System, was new in FY 2010. Consequently, no color scores were shown in last year's report against which to measure progress.
⁴ Management Challenge 9, Improper Payments, was new in FY 2010. Consequently, no color scores were shown in last year's report against which to measure progress.

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Challenge 1. Procurement flaws allow large firms to obtain small business awards and agencies to count contracts performed by large firms towards their small business goals

Challenge 2. Weaknesses in information systems security controls pose significant risks to the Agency

Challenge 3. Effective human capital strategies are needed to enable SBA to successfully carry out its mission and become a high-performing organization

Challenge 4. SBA needs better controls over loan purchase and liquidation processes

Challenge 5. SBA needs to further strengthen its oversight of lending participants

Challenge 6. The Section 8(a) Business Development program needs to be modified so more firms receive business development assistance, standards for determining economic disadvantage are clear and objective, and SBA ensures that firms follow 8(a) regulations when completing contracts

Challenge 7. Effective tracking and enforcement would reduce financial losses from loan agent fraud

Challenge 8. SBA needs to modernize its Loan Accounting System and migrate it off the mainframe

Challenge 9. SBA needs to accurately report, significantly reduce, and strengthen efforts to recover improper payments in the Disaster and 7(a) loan programs

Completed Challenge: Insufficient and outdated SBA controls contribute to excessive risk of the SBIC program

Appendix: Relevant Reports

Challenge 1. Procurement flaws allow large firms to obtain small business awards and agencies to count contracts performed by large firms towards their small business goals.

The Small Business Act establishes a Government wide goal that 23 percent of the total value of all prime contract awards for each fiscal year (FY) be awarded to small businesses. As the advocate for small business, the Small Business Administration (SBA) should strive to ensure that only small firms obtain small business awards and that procuring agencies accurately report contracts awarded to small businesses when representing its progress in meeting small business contracting goals.

Office of Inspector General (OIG) audits and other governmental studies have shown widespread misreporting by procuring agencies; many contract awards recorded as going to small firms have actually been performed by larger companies. While some contractors may misrepresent or erroneously calculate their size, most of the incorrect reporting results from errors made by Government contracting personnel. Noted errors include acceptance of questionable size self-certifications and misapplication of small business contracting rules. Also, it is unclear whether contracting officers always review the on-line certifications that contractors enter into the governmental Online Representations and Certifications Application (ORCA) prior to awarding contracts. SBA needs to ensure that contracting personnel are adequately trained on small business procurement procedures and are reviewing ORCA data prior to awarding contracts.

The Agency also needs to address a loophole within General Services Administration Multiple Awards Schedule (MAS) contracts that contain multiple industrial codes. Currently, a company awarded such a contract can identify itself as small on individual task orders awarded under that contract even though it does not meet the size criteria for the applicable task. Thus, agencies may obtain small business credit for using a firm classified as small, when the firm is not small for specific orders under the MAS contract.

While more remains to be done, SBA made some progress on this challenge. For example, SBA co-chaired the President's Interagency Task Force on Federal Contracting Opportunities for Small Businesses and recommended mandatory training on small business contracting, procurement policies and regulations for contracting personnel and program managers. It is also working on an interagency agreement with the Defense Acquisition University, expected to be executed in FY 2011, whereby SBA personnel would serve as adjunct faculty to teach small business related contracting courses; and has worked with the Department of Defense's Office of Small Business Programs to develop two small business courses intended for program managers, contracting officers, and contract specialists. SBA estimated that the courses will be available in FY 2011. Finally, SBA conducted surveillance reviews to assess whether procurement officials confirmed the small business size status prior to contract award.

Challenge History Fiscal Year (FY) Issued: 2005	Actions Accomplished (Green Status) during Past 4 FYs			
	06-0	07-0	08-1	09-0
Remaining Recommended Actions for FY 2011				Status at end of FY 2010
1. Develop and take steps to provide reasonable assurance that agencies are providing adequate basic and continuing education training to contracting personnel on small business contracting procedures.				Yellow
2. Develop and implement a program that promotes accurate contractor certifications and ensures that contracting personnel review contractor certifications.				Yellow
3. Issue regulations that require firms to meet the size standard for each specific order they receive under a GSA schedule and Government-wide Acquisition Contract (GWAC) and show that the regulations are being followed.				Orange

Green-Implemented **Yellow**-Substantial progress **Orange**-Limited Progress **Red**-No progress

Challenge 2. Weaknesses in information systems security controls pose significant risks to the Agency.

The confidentiality, integrity, and availability of SBA's information systems are vital to the continued successful operation of the Agency. While information technology (IT) can result in a number of benefits, such as information being processed more quickly and communicated almost instantaneously, it can also increase the risk of fraud, inappropriate disclosure of sensitive data, and disruption of critical operations and services. SBA's computer security program operates in a dynamic and highly decentralized environment and requires management attention and resources as weaknesses are identified.

SBA continued to improve information system security in several critical areas during FY 2010. SBA issued procedures requiring vulnerability scanning in contract service level agreements and control reviews; implemented physical and administrative access controls over Agency systems; and made progress implementing standard baseline configurations for its Windows operating system servers and improving controls over major applications. SBA now reviews contractor clearances as part of its Security Authorization process and tracks compliance in its Plan of Actions and Milestones (POA&M). To show further progress, SBA needs to address both known and newly-reported information security issues. For example, SBA needs to demonstrate a process that accomplishes timely mitigation of system risks that are identified as "medium" and "high;" further implement enterprise-wide and application-level change control controls for both emergency and normal system changes; and timely implement OIG recommendations related to IT security issues. While SBA has continued to improve its information system security, the FY 2010 Financial Statement Audit has identified new weaknesses in segregation of duty controls within SBA financial systems.

Challenge History Fiscal Year (FY) Issued: 1999	Actions Accomplished (Green Status) during Past 4 FYs			
	06-2	07-2	08-2	09-0
Remaining Recommended Actions for FY 2011				Status at end of FY 2010
1. Access controls are in place and operating effectively, and contractors are not granted system access until they have obtained the required background investigations and/or security clearances.				Yellow
2. System software controls are in place and operating effectively.				Yellow
3. Segregation of duty controls are in place and operating effectively.				Orange ↓
4. The POA&M accurately reports all computer security weaknesses and corrective actions.				Yellow

Green-Implemented **Yellow**-Substantial progress **Orange**-Limited Progress **Red**-No progress

Challenge 3. Effective human capital strategies are needed to enable SBA to successfully carry out its mission and become a high-performing organization.

During the past decade, facing budget constraints at the same time that virtually of all its programs were growing significantly, SBA restructured key Agency operations, reengineered its largest loan programs, and downsized personnel through attrition and directed transfers. While these actions transformed the way SBA does business, the Agency has not adequately analyzed priorities and allocated resources consistent with those priorities and its new business processes. As a result, there is no assurance that sufficient resources—in terms of both number of staff and the knowledge and skills possessed by staff—are available and appropriately deployed to perform critical functions. For example, OIG and GAO reviews have identified training and inadequate staffing of key functions, including oversight of lenders and monitoring of 8(a) program requirements, as critical issues affecting the Agency.

The results of the Office of Personnel Management’s (OPM’s) Federal Human Capital Surveys—now the Federal Employee Viewpoint Survey (FEVS)—have highlighted SBA’s serious human capital challenges. For example, in 2006 SBA ranked near the bottom on all four human capital indices—Leadership and Knowledge Management, Results-Oriented Performance Culture, Talent Management, and Job Satisfaction. SBA was proactive in addressing these results and showed significant improvement in the 2008 survey. In addition, the Partnership for Public Service, in its 2009 rankings of “The Best Places to Work in the Federal Government,” recognized SBA as the most improved agency, although SBA still ranked 26 out of 30 large agencies. However, the 2010 FEVS did not show continued progress—SBA still trailed the government-wide average on the four human capital indices, with the most significant gap (10 percent) being in Talent Management. In addition, SBA was 29 out of 31 large agencies in the 2010 “Best Places to Work” rankings and its scores were lower than in the 2009 rankings for a number of areas, including Employee Skills/Mission Match, Strategic Management, and Training and Development.

While SBA has taken positive steps in some areas, such as performance management and leadership development, it needs to develop a comprehensive workforce planning process that provides a systematic and strategic approach for ensuring that qualified staff are available and appropriately allocated toward mission-critical functions and Agency priorities.

Challenge History Fiscal Year (FY) Issued: 2001 (Revised 2007)	Actions Accomplished (Green Status) during Past 4 FYs			
	06-0	07-0	08-0	09-0
Remaining Recommended Actions for FY 2011				Status at end of FY 2010
1. Allocate appropriate staffing toward Agency priorities – perform an analysis of Agency priorities and develop, communicate, and implement a comprehensive plan (including responsibilities, metrics, and timeframes) for allocating appropriate staffing (in terms of staffing levels and requisite knowledge, skills, and abilities) toward those priorities.				Yellow
2. Take steps to correct problems identified by the Federal Employee Viewpoint Survey (FEVS) – develop, communicate, and implement a corrective action plan (including priorities, responsibilities, metrics, and timeframes) to address the underlying causes of SBA’s poor results on the FEVS.				Yellow
3. Plan for the future of SBA – develop and implement an effective workforce planning program to ensure that there are qualified staff available to perform SBA’s mission-critical functions and meet identified priorities for the foreseeable future.				Orange ↓

Green-Implemented **Yellow**-Substantial progress **Orange**-Limited Progress **Red**-No progress

Challenge 4. SBA needs better controls over loan purchase and liquidation processes.

The majority of loans under the 7(a) loan-guaranty program are made with little or no review by SBA prior to loan approval because SBA has delegated most of the credit decisions to lenders originating these loans. SBA’s review of lender requests for guaranty purchases on defaulted loans is, therefore, the Agency’s primary tool for assessing lender compliance on individual loans and protecting SBA from making erroneous purchase payments. Furthermore, as lenders are delegated the responsibility for servicing and liquidating SBA loans, SBA’s liquidation process, including the comprehensive charge-off review, is the last opportunity to identify lender noncompliance. However, OIG audits of defaulted loans and SBA’s guaranty purchase and liquidation processes have shown that reviews performed by the loan centers have not consistently detected failures by lenders to administer loans in full compliance with SBA requirements and prudent lending practices, resulting in improper payments.

SBA has taken actions to correct many of the deficiencies identified by the OIG. SBA reengineered the 7(a) loan guaranty purchase processes at the National Guaranty Purchase Center (NGPC) and the Little Rock and Fresno Service Centers to improve the efficiency and consistency of the process; increased staffing levels at the centers; developed a comprehensive operations manual for the NGPC; trained individuals responsible for making purchase decisions; and implemented policies and procedures governing the guaranty purchase and liquidation processes to ensure lender compliance before honoring loan guaranties. While improvements have been made, SBA will need to fully implement its Quality Assurance Review Program at the centers and incorporate these procedures into a formal policy.

Challenge History Fiscal Year (FY) Issued: 2001	Actions Accomplished (Green Status) during Past 4 FYs			
	06-0	07-0	08-2	09-0
Remaining Recommended Actions for FY 2011				Status at end of FY 2010
1. Implement a Quality Assurance Program for all SBA loan centers.				Orange
2. Implement policies and procedures governing the guaranty purchase and liquidation processes to ensure lender compliance before honoring SBA loan guaranties.				Green ↑

Green-Implemented Yellow-Substantial progress Orange-Limited Progress Red-No progress

Challenge 5. SBA needs to further strengthen its oversight of lending participants.

Since its inception in 1953, SBA has loaned or guaranteed billions of dollars to finance and spur investment in small businesses. More than 68 percent of loan dollars guaranteed by SBA are made by lenders using delegated authorities with limited oversight. Prior reviews of SBA's Office of Credit Risk Management (OCRM) disclosed that onsite lender examinations did not adequately assess lender risk; reviews were not made of high-risk, medium-sized lenders; and SBA had not effectively implemented enforcement actions. High risk lenders now account for more than 80 percent of SBA's 7(a) outstanding portfolio. The risks inherent in delegated lending require an effective oversight program to: (1) monitor lender compliance with SBA policies and procedures; and (2) take corrective actions when a material noncompliance is detected.

The Agency has made substantial progress in its oversight of lenders in the 7(a) and 504 loan programs, reducing action items within this Management Challenge from 8 in FY 2006 to 3 in FY 2010. With authority to charge fees to cover the cost of on-site lender reviews, SBA expanded the scope of its oversight by more than doubling the number of on-site reviews of large high-risk lenders. It also issued a *Lender Review Standard Operating Procedure (SOP)* to guide the on-site review process and modified the Lender Risk Rating System to further strengthen lender risk assessments. In October 2010, SBA issued its new *Lender Supervision and Enforcement SOP* that establishes oversight and enforcement actions against nonperforming lenders. The SOP is comprehensive and addresses a number of the concerns that the OIG has had with lender oversight issues. In particular, the SOP provides for agreed-upon procedure reviews and corrective action plans that include milestones and timeframes for achieving results. The guidelines established for lender performance will assist the OCRM in establishing goals and target dates for inclusion in lender corrective action plans.

While the SOP took effect on October 1, 2010, SBA will need to demonstrate consistent and reliable adherence to the procedures and corrective action plans to improve the performance of high-risk lenders.

Challenge History Fiscal Year (FY) Issued: 2001	Actions Accomplished (Green Status) during Past 4 FYs				Status at end of FY 2010	
	06-7(a)-2 06-504-1	07-7(a)-0 07-504-1	08-7(a)-2 08-504-2	09-7(a)-0 09-504-0	7(a)	504
Remaining Recommended Actions for FY 2011						
1. Expand the scope of lender oversight and improve the process for reviewing lenders and Certified Development Companies (CDCs) for compliance risks.					Yellow	Yellow
2. Implement guidance providing for effective oversight of lending programs.					Yellow ↑	Yellow ↑
3. Ensure that effective corrective actions are implemented, monitored, and result in improvement in the performance of participants with unacceptable performance.					Orange	Orange

Green-Implemented **Yellow**-Substantial progress **Orange**-Limited Progress **Red**-No progress

Challenge 6. The Section 8(a) Business Development program needs to be modified so more firms receive business development assistance, standards for determining economic disadvantage are clear and objective, and SBA ensures that firms follow 8(a) regulations when completing contracts.

The SBA 8(a) Business Development (BD) program was created to assist eligible small disadvantaged business concerns to compete in the American economy through business development.

Previously, the Agency did not place adequate emphasis on business development to enhance the ability of 8(a) firms to compete, and did not adequately ensure that only 8(a) firms with economically disadvantaged owners in need of business development remained in the program. Companies that were “business successes” were allowed to remain in the program and continue to receive 8(a) contracts, causing fewer companies to receive most of the 8(a) contract dollars and many to receive none.

The Agency has made considerable progress in addressing issues that challenge its ability to deliver an effective 8(a) program. The Office of Business Development has developed a Business Development Assessment Tool, as well as a plan to provide 8(a) firms with individualized business development assistance. In addition, the Office of Business Development has strengthened its policies and procedures and revised its regulations to ensure that companies that are “business successes” are graduated from the program. Also, the Agency issued proposed regulations in 2009 to establish clear and objective standards to address the definition of “economic disadvantage,” but has not taken further action. SBA has further addressed the need to identify the skills necessary for Business Development Specialists to adequately evaluate a company’s business plan and assess a participant’s competitive potential. Although the Agency has taken steps to ensure that procuring agencies enforce contractor compliance with 8(a) BD program regulations, significant improvements are still needed. The Agency also needs to finalize regulations necessary to complete applicable recommended actions.

Challenge History Fiscal Year (FY) Issued: 2003	Actions Accomplished (Green Status) during Past 4 FYs			
	06-1	07-1	08-1	09-1
Remaining Recommended Actions for FY 2011				Status at end of FY 2010
1. Develop and implement a plan, including SOP provisions, which ensures that the 8(a) BD program identifies and addresses the business development needs of program participants on an individualized basis.				Yellow
2. Develop and implement Regulations and SOP provisions to ensure that participants are graduated once they reach the levels defined as business success.				Yellow
3. Establish objective and reasonable criteria that effectively measures “economic disadvantage” and implement the new criteria.				Orange ↓
4. On a regular basis, conduct surveillance reviews of procuring agencies to ensure they are effectively monitoring and enforcing compliance with specified 8(a) BD regulations on the contracts they administer. (Previously action #5)				Yellow

Green-Implemented Yellow-Substantial progress Orange-Limited Progress Red-No progress

Challenge 7. Effective tracking and enforcement would reduce financial losses from loan agent fraud.

For more than a decade, OIG investigations have revealed a pattern of fraud in the 7(a) business loan guaranty program by loan packagers and other for-fee agents. Fraudulent schemes have involved hundreds of millions of dollars, yet SBA oversight of loan agents has been limited, putting taxpayer dollars at risk. The Agency could reduce this risk by establishing effective loan agent disclosure requirements, a database or equivalent means to track loan agent involvement with its loans, and a more effective agent enforcement program.

Tracking Loan Agent Data -- Over the years, in response to this Management Challenge, SBA has proposed various methods of tracking loan agent activity. At one point, SBA proposed to revise its E-Tran system (which collects loan data electronically from participating lenders) to collect information on loan agent involvement. The Agency ultimately concluded, however, that this approach was not feasible. At the end of FY 2007, SBA proposed a new approach to integrate information from the Form 159 (which asks for information about loan agents) into the Form 1502 electronic data collection process by SBA's Fiscal and Transfer Agent (FTA). The OIG revised recommended action #1 below, but SBA made no progress on this action during FY 2008, in part due to a protest of the award of the FTA contract. At the end of FY 2009, SBA presented a succinct plan for implementing the 1502 approach. However, during FY 2010, SBA again changed its position, and advised that it would capture the data by having the Form 159 faxed in to the FTA. At the end of FY 2010, SBA issued a notice with directions on how this data was to be submitted.

Loan Agent Enforcement Procedures -- In FY 2007, the Agency made progress by issuing its Lender Oversight SOP and by previously revising the guaranty purchase checklist (which lists the records that lenders need to provide when requesting SBA to pay a guaranty) to include the submission of the Form 159. However, the Agency also needs to establish a more effective enforcement program to deter fraudulent loan agent activity. Effective October 1, 2010, SBA issued a Lender Supervision and Enforcement SOP with provisions for loan agent enforcement actions and a delegation of authority to the Director of the Office of Credit Risk Management.

Challenge History Fiscal Year (FY) Issued: 2000	Actions Accomplished (Green Status) during Past 4 FYs			
	06-0	07-1	08-1	09-0
Remaining Recommended Actions for FY 2011				Status at end of FY 2010
1. Develop an effective method of disclosing and tracking loan agent involvement in the SBA business loan programs.				Yellow ↑
2. Implement procedures for enforcement actions against loan agents for improper and fraudulent conduct.				Yellow ↑

Green-Implemented Yellow-Substantial progress Orange-Limited Progress Red-No progress

Challenge 8. SBA needs to modernize its Loan Accounting System and migrate it off the mainframe.

In November 2005, SBA initiated the Loan Management and Accounting System (LMAS) project to update the Agency’s Loan Accounting System and migrate it off of the mainframe. Previous OIG reports noted that the system is close to the end of its expected useful life, relies on obsolete technology, contains major security vulnerabilities that cannot be addressed until the system is moved to a new operating platform, and is costly to operate. Additionally, the OIG reported concerns about SBA’s management of the project; the project’s noncompliance with the Agency’s System Development Methodology (SDM) in key areas, which impacts SBA’s ability to control project costs and quality; and the lack of an enterprise-wide or project-level Quality Assurance (QA) function to ensure that LMAS deliverables meet SBA’s requirements and quality standards. Finally, the OIG reported that the LMAS QA contractor had not performed all of the activities stipulated in its contract and that none of the issued LMAS task orders have undergone Independent Validation and Verification (IV&V) testing.

In 2009 SBA contracted with McKinsey & Company to conduct a review of the LMAS project. This review identified multiple weaknesses in SBA’s LMAS project management activities and recommended: (1) focusing on core mainframe legacy platform replacement; (2) strengthening project governance; (3) increasing project team resources; 4) focusing on COTS capabilities while minimizing customization; and 5) improving vendor management.

In 2010 OMB issued Memorandum 10-26, recommending that Federal agencies split large-scale modernization efforts into smaller, simpler segments with clear deliverables. In response, SBA changed its strategy for LMAS going forward to accelerate the migration of user interfaces from the mainframe legacy platform to the Agency’s current architecture, and convert batch COBOL systems from the mainframe to a more current and platform-independent environment. To show further progress, SBA needs to develop detailed project plans for implementing its new LMAS strategy; implement a QA/IV&V process that encompasses all of the requirements of its enterprise SDM; and provide sufficient evidence that all LMAS work products undergo IV&V activities in accordance with the Agency’s *Enterprise Quality Assurance Plan*.

Challenge History Fiscal Year (FY) Issued: 2010	Actions Accomplished (Green Status) during Past 4 FYs			
	N/A	N/A	N/A	N/A
Recommended Actions for FY 2011				Status at end of FY 2010
1. Migrate LAS to a new operating platform before the current mainframe contract expires in 2012.				Orange
2. Modify the LMAS QA/IV&V contract and establish an effective Quality Assurance (QA) process which provides senior management independent assurance that LMAS development activities and related project deliverables meet SBA Quality standards.				Orange
3. Establish a process for reviewing and accepting LMAS deliverables that complies with Systems Development Methodology requirements.				Orange
4. Implement a Quality Assurance process in LMAS in accordance with SBA’s Enterprise Quality Assurance Plan.				Orange

Green-Implemented **Yellow**-Substantial progress **Orange**-Limited Progress **Red**-No progress

Challenge 9. SBA needs to accurately report, significantly reduce, and strengthen efforts to recover improper payments in the Disaster and 7(a) loan programs.

OIG audits of SBA's Disaster and 7(a) Loan Programs determined that the improper payment rates reported for these programs were significantly understated. SBA estimated that improper payments in the Disaster Loan Program were about \$4.5 million, or 0.55 percent of loans approved in FY 2007, while the OIG reported that it was at least 46 percent, or approximately \$1.5 billion. SBA also reported that the improper payment rate for the 7(a) program was 0.53 percent of FY 2008 program outlays, although the OIG estimated the rate to be 27 percent, or approximately \$234 million. SBA's improper payment rates were understated because the Agency did not adequately review sampled loans, used flawed sampling methodologies, and did not accurately project review findings for both programs. Additionally, the OFA inappropriately overturned improper payments identified by reviewers.

OIG audits in prior years have also identified high percentages of disaster and business loans that were made to borrowers who were ineligible, lacked repayment ability, or did not provide the required support for loan disbursement. In 2009, we reported that over 30 percent of reviewed disaster loans were disbursed for properties that were not the applicant's primary residence and identified an estimated \$30 million in improper loan guaranty purchases in the 7(a) program. SBA also has not aggressively pursued recovery of improper payments. SBA has not yet collected more than \$2 million of FY 2008 improper payments identified by the OIG.

SBA has taken actions to correct many of the deficiencies identified by the OIG. For example, the Agency has determined that a secondary market purchase will be considered improper to the extent that SBA failed to identify and/or collect the improper payment during its post purchase review process. The Agency also established clear policies for offsetting outstanding ongoing guaranty fees from amounts paid to the lenders. Also, the Agency has implemented a corrective action plan for the disaster loan program that addresses OMB requirements. A QAR team of experienced loan officers and legal personnel was established to perform the improper payment reviews. However, additional actions are needed to accurately report, significantly reduce, and recover improper payments. SBA needs to incorporate the improper payment review processes; a denial, repair and improper payment dispute resolution process; and an improper payment recovery process into formal policy.

Challenge History Fiscal Year (FY) Issued: 2010	Actions Accomplished (Green Status) during Past 4 FYs			
	N/A	N/A	N/A	N/A
Recommended Actions for FY 2011	Status at end of FY 2010			
	Disaster	7(a)		
1. Ensure that processes used to calculate the improper payment rate for disaster and 7(a) loans are designed to effectively identify improper payments as defined by Office of Management and Budget (OMB) Circular A-123.	Yellow	Orange		
2. Reassign responsibility for final approval of disputed denial, repair, and improper payment decisions from the Office of Financial Assistance to the Office of Risk Management to ensure an adequate and timely resolution of disputes.	N/A	Orange		
3. Develop a process to ensure that reviewers are properly trained to perform improper payment reviews.	Green	N/A		
4. Develop and implement corrective action plans to reduce improper payments in the 7(a) and Disaster Loan programs.	Yellow	Yellow		
5. Establish a process and time standards to expeditiously recover improper payments identified during Agency reviews and OIG audits.	N/A	Orange		

Green-Implemented **Yellow**-Substantial progress **Orange**-Limited Progress **Red**-No progress

Completed Challenge

Insufficient and outdated SBA controls contribute to excessive risk of the SBIC program.

The Small Business Investment Company (SBIC) program is designed to stimulate and supplement the flow of private equity capital and long-term debt to small business concerns. SBA uses both guaranteed debt (debentures) and equity interest (participating securities) to provide government-backed financing to SBICs. Effective October 2004, SBA discontinued the licensing of SBIC participating securities due to the over \$2 billion in unprecedented losses experienced by the program. While existing participating securities SBICs continue to operate in the program, the last funds will expire by 2014 upon the maturity of their 10-year life cycle.

As of August 2010, SBA had about \$6.4 billion of outstanding leverage in both debenture and participating securities financings at risk. As of August 2010, 138 SBICs were in liquidation with outstanding leverage of nearly \$2 billion, most of which were in Participating Securities. Prior OIG reports determined that: (1) existing guidance did not provide a systematic approach for transferring capially-impaired SBICs into liquidation status and (2) better performance goals and indicators were needed to show how well and how timely recoveries were maximized for liquidated SBICs.

Our review of the Investment Division’s management reports and discussions with division officials disclosed that management was actively monitoring and timely transferring impaired SBICs to liquidations when warranted. Also, management transferred one longstanding problematic SBIC into liquidation in September 2010, after the principals conceded that they could not raise the additional capital to cure the fund’s impairment. Management has also developed performance goals and indicators to evaluate effectiveness of the liquidation process of SBICs and reports annually on whether these goals have been met.

Challenge History Fiscal Year (FY) Issued: 2004	Actions Accomplished (Green Status) during Past 4 FYs			
	06-1	07-1	08-1	09-2
Remaining Recommended Actions for FY 2011				Status at end of FY 2010
1. Develop systematic criteria and implement a timely approach for transferring SBICs to liquidation status.				Green ↑
2. Develop and implement performance goals and indicators that address the efficiency, cost-effectiveness, and timeliness of the SBIC liquidation process. (Previously action #3)				Green ↑

Green-Implemented **Yellow**-Substantial progress **Orange**-Limited Progress **Red**-No progress

Appendix: Relevant Reports

Most of the SBA OIG Reports listed can be found at www.sba.gov/ig.

Challenge 1:

- SBA Advocacy, Analysis of Type of Business Coding for the Top 1,000 Contractors Receiving Small Business Awards in FY 2002, December 2004.
- The Center for Public Integrity, The Big Business of Small Business: Top defense contracting companies reap the benefits meant for small businesses, September 29, 2004.
- The Center for Public Integrity, The Pentagon's \$200 Million Shingle: Defense data shows billions in mistakes and mislabeled contracts, September 29, 2004.
- SBA OIG, Audit of SBA's Administration of the Procurement Activities of Asset Sale Due Diligence Contracts and Task Orders, Report #4-16, March 17, 2004, pp. 8-9.
- GAO, Contract Management: Reporting of Small Business Contract Awards Does Not Reflect Current Business Size, GAO-03-704T, May 7, 2003.
- The Small Business Committee, U.S. House of Representatives Hearing, Are Big Businesses Being Awarded Contracts Intended for Small Businesses? Testimony of Mr. Fred C. Armendariz, Associate Deputy Administrator, SBA, May 7, 2003.
- The Small Business Committee, U.S. House of Representatives Hearing, Are Big Businesses Being Awarded Contracts Intended for Small Businesses? Testimony of Mr. Felipe Mendoza, Associate Administrator, Office of Small Business Utilization, U.S. General Services Administration, May 7, 2003.
- SBA OIG, SBA Small Business Procurement Awards Are Not Always Going to Small Businesses, Report #5-14, February 24, 2005.
- SBA OIG, Review of Selected Small Business Procurements, Report #5-16, March 8, 2005.
- SBA OIG, SBA's Planning and Award of the Customer Relationship Management Contracts, ROM 10-16, June 29, 2010.
- Interagency Task Force on Federal Contracting Opportunities for Small Businesses Report, September 2010.

Challenge 2:

- SBA OIG, Audit of SBA's FY 2009 Financial Statements, Report #10-04, November 13, 2009
- SBA OIG, SBA's FY2008 Financial Statements, Report #9-03, November 14, 2008
- SBA OIG, Audit of SBA's Financial Statements for FY 2006, Report #7-03, November 15, 2006.
- SBA OIG, Audit of SBA's Information System Controls for FY 2004, Report #5-12, February 24, 2005.

Challenge 3:

- Partnership for Public Service, Best Places to Work in the Federal Government 2010, <http://bestplacestowork.org/BPTW/rankings/>
- OPM, 2010 Federal Employee Viewpoint Survey (FEVS), <http://www.fedview.opm.gov/2010/>
- SBA OIG, The Colorado District Office's Servicing of 8(A) Business Development Program Participants, Report #10-15, September 30, 2010
- SBA OIG, Adequacy of Procurement Staffing and Oversight of Contractors Supporting the Procurement Function, ROM 10-13, April 9, 2010
- SBA OIG, SBA's Administration of the Microloan Program under the Recovery Act, ROM 10-10, December 28, 2009
- Partnership for Public Service, Best Places to Work in the Federal Government 2009
- OPM, 2008 Federal Human Capital Survey (FHCS)
- GAO, Agency Should Assess Resources Devoted to Contracting and Improve Several Processes in the 8(a) Program, GAO-09-16, November 2008

- GAO, Opportunities Exist to Build on Leadership's Efforts to Improve Agency Performance and Employee Morale, GAO-08-995, September 2008
- SBA OIG, Non-Native Managers Secured Millions of Dollars from 8(a) Firms Owned by Alaska Native Corporations through Unapproved Agreements that Jeopardize the Firms' Program Eligibility, Report #8-14, August 7, 2008
- GAO, Opportunities Exist to Improve Oversight of Women's Business Centers and Coordination Among SBA's Business Assistance Programs, GAO-08-49, November 2007
- SBA OIG, Audit of Two 8(a) Sole-Source Contracts Awarded to Contractors in SBA's Mentor Protégé Program, Report #7-19, March 30, 2007
- SBA OIG, Management Advisory Report on the Transfer of Operations to the National Guaranty Purchase Center, Report #4-39, August 31, 2004
- GAO, Small Business Administration: Progress Made, but Transformation Could Benefit from Practices Emphasizing Transparency and Communication, GAO-04-76, October 2003
- GAO, Results Oriented Cultures: Implementation Steps to Assist Mergers and Organizational Transformations, GAO-03-699, July 2003
- GAO, Small Business Administration: Workforce Transformation Plan is Evolving, GAO-02-931T, July 16, 2002
- SBA OIG, Modernizing Human Capital Management, Report #2-20, May 31, 2002
- GAO, Small Business Administration: Current Structure Presents Challenges for Service Delivery, GAO-02-17, October 2001
- GAO, Small Business Administration: Steps Taken to Better Manage its Human Capital, but More Needs to be Done, GAO/T-GGD/AIMD-00-256, July 20, 2000
- SBA OIG, A Framework for Considering the Centralization of SBA Functions, November 1996

Challenge 4:

- SBA OIG, Material Deficiencies Identified in Early-Defaulted and Early-Problem Recovery Act Loans, #10-19, September 24, 2010
- SBA OIG, SBA's Management of the Backlog of Post-purchase Reviews at the National Guaranty Purchase Center, #9-18, August 25, 2009
- SBA OIG, , The Small Business Administration's Fiscal Year 2008 Improper Payment Rate for the 7(a) Guaranty Loan Program #9-16, July 10, 2009
- SBA OIG, Review of Key Unresolved OIG Audit Recommendations in Program Areas Funded by the American Recovery and Reinvestment Act and Related Activities Need to Safeguard Funds, #ROM 09-1, April 30, 2009
- SBA OIG, Audit of the Liquidation Process at the National Guaranty Purchase Center, #9-08, January 30, 2009
- SBA OIG, Audit of Six SBA Guaranteed Loans, #8-18, September 8, 2008
- SBA OIG, Audit of Loan Classifications and Overpayments on Secondary Market Loans, #8-09, March 26, 2008
- SBA OIG, Audit of UPS Capital Business Credit's Compliance with Selected 7(a) Lending Requirements, #8-08, March 21, 2008
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- SBA OIG, Audit of an SBA Guaranteed Loan, Report #7-17, March 12, 2007
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Agency Response to the OIG Report on Management and Performance Challenges



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

Date: November 10, 2010

To: Peggy E. Gustafson
Inspector General

From: Marie C. Johns
Deputy Administrator 

Subject: FY 2011 OIG-Identified Major Management Challenges

On October 15, 2010, the OIG submitted to SBA its report entitled: "Fiscal Year 2011 Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration." The Management Challenge Report, which is published in the Agency's Annual Financial Report (AFR) each November, provides an OIG assessment of major Agency management challenges that pose significant risks, including those that are particularly vulnerable to waste, fraud, error, or mismanagement.

SBA is pleased to report the following results in this year's Report:

1. Achieved four green ("fully successful") ratings on 36 OIG-recommended actions, 18 yellow ("substantial progress"), 14 orange ("limited progress"), and no reds ("no progress");
2. Eliminated one challenge completely, i.e., "Insufficient and Outdated SBA Controls Contribute to Excessive Risk in the SBIC Program," by successfully implementing the two OIG-recommended actions;
3. Improved ratings in seven of the 36 OIG-recommended actions;
4. Achieved progress in two additional Challenges that included "new" OIG-recommended actions last year; and
5. Reduced the overall number of recommended actions to address the Challenges from 36 to 32, down from 136 actions recommended in FY 2004.

One of the Agency's core management priorities is to ensure effective program oversight and execution of its fiduciary responsibility to safeguard taxpayer resources. SBA appreciates the cooperation and work done by the OIG in helping the Agency to continue to address successfully its major management challenges. Instituting sound internal management processes leads to reduced government risk; lower cost to the taxpayer; and reduced potential for waste, fraud and abuse.

Thank you and your staff for your continued commitment in helping us to improve our management environment.

APPENDICES

Success Story



SBA Programs Help Dental Center Serve Neighborhood Jackson's Dental Center, Atlanta, Georgia

After being on Martin Luther King Jr. Drive for several decades, Dr. Montina Jackson and her husband Jerome Jackson realized it was time to upgrade and expand their dental center and laboratory. They were committed to providing their services to the local neighborhood, but at the same time they needed a larger facility to replace the small building they had occupied in the area for over 30 years.

Dr. Jackson says doors really started to open for their expansion in the fall of 2008. She enrolled in SBA's first "Emerging 200" management training course in Atlanta. "My training really helped me to critically analyze my business," said Dr. Jackson. "When I was in dental school, there was very little instruction about operating a business." Dr. Jackson was introduced to SBA's 7(a) lending program after she presented her strategic plan to a panel of business specialists that included Rosemarie Drake, a regional account manager for CIT Small Business Lending. Ms. Drake's company made a \$1.2 million SBA 7(a) loan to Dr. Jackson and her husband. They used the funds to acquire and rehab a 10,000 square-foot building just a few blocks west of their old location. "The SBA guaranteed loan was critical to getting our expansion underway," said Dr. Jackson. "And having to put only 10 percent down on the loan was a key to getting it done." The Jacksons also saved over \$25,000 in lending fees which were waived since the loan was made under provisions of the American Recovery and Reinvestment Act. Over half of the structure was transformed into a modern dental center with seven dental examination rooms. Another half of the renovated building was made into four suites that can be rented to other tenants.

Dr. Jackson practices both preventive and family dentistry. She also does cosmetic and emergency dental work and was the first female dentist to treat patients at the Fulton County Jail.

Appendix 1 - Improper Payments

As required by the Improper Payments Information Act the SBA reviewed its payment programs for improper payments during FY 2010.

I. Risk Assessment

The SBA's four major credit programs are included in our Improper Payments program as they were previously identified in the former Section 57 of Circular A-11.

- (1) 7(a) Business Loan guaranty approvals and defaulted loan purchases
- (2) 504 Certified Development Company guaranty approvals
- (3) Small Business Investment Company financings
- (4) Disaster Loans

The first three are loan guaranty programs and Disaster is a direct lending program. No other SBA programs meet the dollar thresholds in OMB guidance for improper payment reporting. There have been no changes in SBA's risk assessment process since the last improper payment report.

II. Statistical Sampling

The statistical sampling process used in FY 2010 is practically unchanged from that used last year. In accordance with OMB guidance a brief statement of the process follows.

7(a) Guaranty Purchase statistical sampling used Probability Proportional to Size with replacement in FY 2010. This method was used because large loans in the sample can skew the result. The sampling period was the 12 months ended March 31, 2010. The sample was stratified based on service center, purchase process and early default. Using PPS, the SBA determined the appropriate total sample size to be 211 loans with aggregate purchase outlays of \$90,507,176, and improper payments of \$2,112,111 were identified within the sample. Using the Hansen-Hurwitz estimation method, the estimated improper payment rate for the 7(a) guar-

anty purchase population is 1.87 percent compared to a 3.81 percent rate last year.

7(a) Approval reviews also used PPS Sampling with replacement for all loan guaranties approved during the 12 month period ended March 31, 2010. The approval population was divided into six strata based on the loan delivery method. The SBA determined the appropriate total sample size to be 115 loans from the population. The estimated improper payments rate for the annual period ending March 31, 2010 was calculated as zero percent based on the aggregate net approval amount of \$98,084,100 on the approved loans with no improper payments found.

504 CDC Approval used PPS sampling with replacement from all loan guaranties approved during the 12 month period ended March 31, 2010. The approval population was divided into three strata based on the loan delivery method. The SBA determined the appropriate total sample size to be 50 loans from the population. The estimated improper payments rate was calculated as zero percent based on the aggregate net approval amount of \$64,524,000 on the approved loans with no improper payments found.

SBIC used a random sample of 95 SBIC financings by SBIC's having SBA guaranteed leverage during the 12 month period ended March 31, 2010 (last year the period was 12 months ended June 30th.) Improper payments were identified when an SBIC examination (either regularly scheduled or a special examination) found a discrepancy with SBIC program regulations in the sampled financings. The examinations identified three potential improper payments where excessive prepayment penalties were not approved by SBIC program officials as required (although they may have been approved if the SBIC had requested approval.) The three financings constituted \$848,896 of the \$85,942,350 in financings sampled, or 0.99% of the total.

Disaster Quality Assurance Review included 252 disbursed disaster loans made during the 12 months ended June 30, 2010 found a 34.2 percent improper payment rate. The scope of the QAR covers three compliance areas: (1) basic eligibility, (2) adherence to relevant laws, rules, regulations

and standard operating procedures and (3) creditworthiness. The high rate of improper payments is generally the result of paperwork errors, not eligibility or creditworthiness errors.

III. Corrective Action

The 7(a) guaranty purchase improper payments program identifies and tracks the reasons for any improper payments discovered in the reviews, and then appropriate adjustments to the guaranty purchase process are made to reduce future errors. Improper payments arise from the failure of a purchase processor to identify material lender deficiencies in the handling of an SBA guaranteed loan. Primary reasons for errors in purchases reviewed this year were:

- Improper use of loan proceeds (not fully in accordance with loan authorization).
- Failure to obtain equipment appraisal and required liens on collateral.
- Loan made to an ineligible franchise.
- Appraisal of collateral did not meet loan authorization requirement.
- Minor under/overpayments to secondary market due to incorrect interest rates.
- Payment of undocumented lender expenses.
- Overpayment as a result of lender billing twice for the same expense.
- Failure to verify borrower financial information using IRS tax transcripts.

Corrective action procedures followed for the 7(a) guaranty purchase process involve advising the purchase processing team of improper payment determinations and clarification of the issues to avoid possible improper payments in the future through a newly structured quality assurance review (QAR) process. A fully documented guaranty purchase procedure handbook is updated when needed. Remedial actions taken by the QAR team include:

- identify and analyze error patterns,
- communicate error patterns to the staff processing purchases,

- review current policies and procedures to ensure that any error patterns are appropriately addressed in current guidance,
- revise policies and procedures where necessary,
- issue guidance to the purchase staff on specific issues,
- provide training, and to
- supplement center resources where possible to ensure ongoing quality assurance review programs that will identify any emerging patterns or potential problem areas that might result in future improper payments, as well as take action to mitigate these potential problem areas.

7(a) loan guaranty approvals and 504 CDC loan approvals had no improper payments.

There appear to be sufficient safeguards in place to prevent improper payments in 7(a) loan processing and 504 loan originations because of multiple reviews that take place when a loan is being processed.

SBIC financings had only three potential erroneous payments. This minimal number of erroneous payments will continue in the future due to rigorous program standards. The following procedures ensure fiscally prudent managers in the SBIC program.

- Licensing standards require knowledgeable fund managers and this reduces the likelihood of program errors and fraud.
- All fund managers must undergo training on SBIC regulations as a condition for receiving leverage and therefore almost all SBICs are very knowledgeable service providers that have extensive experience in the program.
- Licensing includes extremely detailed background checks on fund managers by both the Office of the Inspector General and the Federal Bureau of Investigation.
- Credit checks are performed on all potential fund managers as part SBIC licensing.
- Licensees are audited on a periodic basis to determine ongoing compliance with regulatory requirements.

Disaster improper payment rate was greater than was projected. The increased rate does not reflect greater risk in the portfolio, but does indicate a need to adhere to the documentation requirements of our Standard Operating Procedures. The following steps will reduce future Improper Payment rates.

- Additional training has been instituted to ensure that staff is aware of all paperwork requirements and waiver procedures when appropriate.
- A dedicated team that reports directly to SBA HQ will complete the annual Improper Payment review and continuously review the work of the Production and Disbursement Center.
- Areas of concern will be identified and corrected in a timely manner.

Disaster improper payments identified thru annual Quality Assurance Reviews indicate minimal findings of unauthorized and/or ineligible loans. Disaster program internal controls include the following:

- Disaster related damages are verified onsite by SBA staff. The cost to repair and/or replace the disaster damaged property is determined by SBA construction analysts.
- Disaster procedures include credit checks, verification of income, verification of ownership and checks with FEMA to ensure that federal assistance is not duplicated during loan processing and disbursement of all disaster loans.
- Every secured disaster loan is reviewed by disaster staff attorneys for legal sufficiency and the use of electronic funds transfer is utilized to prevent lost and stolen checks.

Grant Programs

The SBA does not have any reportable grant programs under OMB risk susceptible guidance. As a result, this report does not include a discussion of fund stewardship in its grant programs.

Improper Payment Reduction Outlook (\$ in millions)															
Program	FY09 ¹ \$ Outlays	FY09 IP %	FY09 IP \$	FY10 ¹ \$ Outlays	FY10 IP %	FY10 IP \$	FY11 ¹ \$ Outlays	FY11 IP %	FY11 IP \$	FY12 ¹ \$ Outlays	FY12 IP %	FY12 IP \$	FY13 ¹ \$ Outlays	FY13 IP %	FY13 IP \$
7(a) Guaranty Purchases ¹	1,805.4	3.81 ⁵	68.8	2,392.2	1.87	44.8	1,523.6	1.8	27.4	1,296.8	1.7	22.0	1,223.0	1.6	19.6
7(a) Guaranty Approvals ¹	8,934.7	0.0	0.0	11,638.7	0.0	0.0	12,500.0	0.0	0.0	14,000.0	0.0	0.0	15,500.0	0.0	0.0
CDC Debentures ²	3,820.6	0.0	0.0	4,500.2	0.0	0.0	5,000.0	0.0	0.0	5,500.0	0.0	0.0	6,000.0	0.0	0.0
CDC Loans Guarantied ¹	3,820.6	0.0	0.0	4,500.2	0.0	0.0	5,000.0	0.0	0.0	5,500.0	0.0	0.0	6,000.0	0.0	0.0
SBIC Guaranties ³	1,856.0	1.1	20.4	1,475.0	0.99	14.6	1,400.0	1.0	14.0	1,400.0	1.0	14.0	1,400.0	0.90	12.6
Disaster Loan Disbursements ⁴	806.0	20.9 ⁵	168.5	372.1	34.2	127.1	800.0	20.0	160.0	800.0	17.0	136.0	800.0	15.0	120.0

1. Outlays in this report represent the base amount of the program activity related to SBA improper payments; and this amount will differ from the amount reported as outlays in SBA's President's Budget submissions because they include reestimates of subsidy cost, reimbursements to SBA administrative funds and other costs. Outlays for 7(a) Guaranty Purchases are the amount of disbursements for the purchase of defaulted guaranteed loans. Outlays for 7(a) Guaranty Approvals are the amount of new guaranty approvals by banks and other SBA lending partners. Outlays for CDC Debentures and CDC Loans Guarantied are approvals irrespective of disbursement, net of approval increases, decreases, reinstatements and cancellations for the current year. Outlay figures for Disaster are loan disbursements on current year approvals. All improper payments in this report are overpayments, not underpayments.

2. SBA has zero improper payments assumed for CDC debentures.

3. SBIC Guaranties include SBA guaranties of SBIC investments in small business for SBICs having SBA leverage.

4. Disaster Loan Outlays projected for FY 2011 thru FY 2013 reflects a historical average level.

5. The SBA Inspector General issued audit reports on the 7(a) and Disaster Improper Payment programs in July and March 2009. As a result of findings and recommendations in these reports the SBA changed its methodology used in both of these programs for sampling and testing improper payments. As a result the improper payment rates and dollars increased in FY 2009 reflecting these changes.

IV. Improper Payment Reporting

The table on the previous page presents the SBA's Improper Payment program results for FY 2010.

Recovery of Improper Payments

7(a) guaranty purchase recovery has target of 85% of the aggregate amount of improper payments identified by March 30th of the following year. Litigation may be necessary in some instances with uncooperative lenders and additional information may be presented which could indicate that all or a portion of a disbursement is not actually improper. Also, reasonable settlements of improper payment claims may be made rather than to pursue protracted recovery proceedings. SBA will make formal written demand upon and/or engage in discussions with 7(a) lenders having received improper payments. If a lender refuses to return a payment, litigation or other cost effective action will be explored to promote a reasonable chance of recovery. The litigation office in SBA's Office of General Counsel will conduct this analysis.

SBIC program recovery is very effective. SBA's current recovery efforts are very effective and are resolved quickly. The reported improper payment may be determined to not be a violation of regulations after further study. Or the SBIC may be asked to change the terms of the investment to resolve the issue. If necessary, the SBIC may be asked to divest its interest in the portfolio concern. In very rare instances, the SBIC might be found to be in default of its covenants and transferred to the Office of SBIC Liquidations, where recovery efforts will be implemented. This has not been necessary for the most part.

Disaster improper payments are generally the result of loan documentation errors and do not result in a disaster victim receiving funds that they are not eligible to receive. Further, the disaster loan program operation has a built in recovery system in that the majority of loans made are collateralized and all loans have to be repaid, and SBA's loan servicing and liquidation operation attains maximum recovery.

V. Recovery Auditing

Recovery auditing is a control technique to identify improper contractor payments and initiate recovery actions where appropriate. Even though SBA does not meet the OMB threshold for recovery auditing, SBA does employ internal control measures to address improper contract payments.

Disaster program internal controls (checks and balances) have always been a part of loan making and disbursement and they are responsible for the relatively minimal amounts of unauthorized and/or ineligible loans. In addition, the Disaster loan legally obligates the recipient of any disaster loan to pay back all the loan amount whether or not the loan contains any Improper Payments. Not only is there a legally binding contract to repay the loan, the contract is usually secured by real estate collateral which further strengthens the government's recovery position. Accordingly, an ODA recovery auditing effort is *not applicable* because each loan contract legally assures recovery of the entire loan (with interest) as soon as the loan agreement is signed – notwithstanding the circumstances.

Agency Component	Amount subject to Review for CY Reporting	Actual Amount Reviewed and Reported CY	Amount Identified for Recovery CY	Amount Recovered CY	Amount Identified for Recovery PYs	Amount Recovered PYs	Cumulative Amount Identified for Recovery (CY + PYs)	Cumulative Amount Recovered (CY + PYs)
N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

VI. Improper Payment Accountability

The SBA's Strategic Goal Three is to assure SBA programs operate efficiently and effectively, including compliance with federal regulations on improper payments. The SBA's strategic goals are included in annual performance plans for all of its programs as business objectives, and these business objectives are included in employee performance plans. SBA management monitors accomplishment of its business objectives in its performance plan using its performance management process, and action is taken when progress is not on target.

Executive and management bonuses are based on the accomplishment of business objectives included in employee annual performance plans. This management process assures accountability of improper payment administration.

SBIC operations analysts are evaluated, in part, on the resolution of regulatory violations in a timely manner. They are also evaluated, in part, on responding to requests for clarification on regulations by licensees. Although examiners are not evaluated on the number of violations they uncover, they are evaluated on the number of exams they perform. We believe the assistance provided by the Operations analysts and the approximately annual exams for leveraged SBICs provide an incentive to perform within the framework of the regulations.

VII. Information Systems and other Infrastructure and Improper Payments

7(a) loan purchase is supported very well by the Guaranty Purchase Tracking System. It is continually updated to enhance the overall integrity of the purchase process.

504 CDC software used by the Central Servicing Agent is owned by the SBA. Therefore the Agency has a higher level of control over that software than would typically exist with contractor owned systems. In addition the contractor provides audited financial statements and a SAS 70 report to verify its system.

SBIC financings are supported very well by a data system that tracks exams, exam findings and resolution of exam findings. All individuals are empowered to refer any case of suspected fraud to the Inspector General.

Disaster does have the information systems and other infrastructure it needs to reduce improper payments to targeted levels. Disaster is engaged in an ongoing process of developing and has already implemented an integrated, electronic loan processing system to streamline, enhance and improve the loan-making process. This system will support workflow management, electronic file

management and document generation functions. The newly formed Quality Assurance Team is working with the Disaster Credit Management System development team to improve the Quality Assurance process with a goal to minimize future Improper Payments events as much as possible. Many of the business rules that govern the programming of this system have been designed to help improve the Quality Assurance process.

Information System Resources Budget Request

Although the SBA's existing systems provide adequate support to its programs to avoid improper payments, the SBA has included funding in its FY 2012 budget request to upgrade its financial systems. During FY 2010, in accordance with OMB guidance, SBA reviewed and subsequently discontinued its ongoing loan and financial system modernization project to develop an integrated Loan Management and Accounting System. Instead of LMAS, the Agency plans to focus on migrating its loan and financial systems from its mainframe platform to improve their efficiency and reliability and to continue the upgrade of its Joint Accounting and Administrative Management System administrative accounting system by implementing the latest version of the Oracle Federal Financials software. These system improvements will provide support to the SBA's Improper Payment program.

VIII. Statutory or Regulatory Barriers

The SBA does not have any statutory or regulatory barriers limiting improvement to its performance on improper payments initiative.

IX. Additional Comments

The SBA provided additional staff during FY 2010 to support its internal controls over financial management activities in accordance with OMB Circular A-123 requirements. These resources will be applied to future improvement of the SBA's Improper Payment program.

Appendix 2 - Contact SBA: Useful Sites and Numbers

The SBA home page is www.sba.gov. Information on SBA programs may be accessed from this site. Several of the more frequently visited sites are listed below:

SBA INFORMATION	
Who We Are and What We Do	www.sba.gov/aboutsba
Find Your Local Office	www.sba.gov/localresources/index.html
SBA's Plans and Reports	www.sba.gov/aboutsba/budgetsplans/index.html
Advocacy	www.sba.gov/advo
SBA Resource Partners	www.sba.gov/services/counseling
Online Resources	www.sba.gov/tools
Small Business Jobs Act of 2010	www.sba.gov/jobsact
Inspector General	www.sba.gov/ig
FOR START-UP BUSINESSES	
What is a Small Business?	www.sba.gov/contractingopportunities/officials/size
Starting Your Business	www.sba.gov/starting
SBA Direct	www.sba.gov/direct
On Line Training	www.sba.gov/services/training/index.html
SCORE	www.score.org
FOR ESTABLISHED BUSINESSES	
Financing Your Business	www.sba.gov/services/financialassistance
Contracting	www.sba.gov/services/contractingopportunities
Surety Bond	www.sba.gov/services/financialassistance/suretybond/index.html
Business Opportunities	http://business.sba.gov/financing/grants
Exporting	www.sba.gov/aboutsba/sbaprograms/internationaltrade
CONTRACTING WITH THE GOVERNMENT	
Government Contracting	www.sba.gov/GC
Central Contractor Registration	www.bpn.gov/ccr/default.aspx
DISASTER ASSISTANCE	
Disaster Assistance	www.sba.gov/services/disasterassistance
Disaster Area Office Locations	www.sba.gov/services/disasterassistance/officelocations
FEMA Information	www.fema.gov

Facebook: www.facebook.com/sbagov **Twitter:** www.twitter.com/sbagov
YouTube: www.youtube.com/sba

SBA National Answer Desk (Toll Free) (800) 827-5722
Disaster Customer Service Center (Toll Free) (800) 659-2955

Appendix 3 - Glossary of Acronyms and Abbreviations

(Available at: “Current Agency Financial Report“ <http://www.sba.gov/aboutsba/budgetsplans/index.html>)

504	504 Certified Development Loan Program Provides small businesses with long-term, fixed-rate financing for the purchase of land, buildings and long-life capital equipment	ARC	America’s Recovery Capital Loan Program A new temporary guaranty loan program authorized by the American Recovery and Reinvestment Act of 2009.
7(a)	7(a) Loan Guaranty Program SBA’s primary loan program. It provides general loan financing for a wide variety of purposes.	ARRA	American Recovery and Reinvestment Act of 2009 Most often referred to as the Recovery Act in SBA documents.
8(a)	8(a) Business Development Program Assists firms owned and controlled by socially and economically disadvantaged individuals to enter and succeed in the economic mainstream.	BATF	Business Assistance Trust Fund A trust fund in the U.S. Treasury maintained to receive and account for donations made by private entities for activities to assist small business.
A-123	Designation for OMB Circular on “Internal Control Systems.” It prescribes policies and procedures to be followed by executive departments and agencies in establishing, maintaining, evaluating, improving, and reporting on internal controls in their program and administrative activities.	BD	Business Development The Office of Business Development uses SBA’s statutory authority to provide business development and federal contract support to small disadvantaged firms.
AA	Associate Administrator	BDMIS	Business Development Management Information System The system that automates the certification and annual review process for the 8(a) program.
AFMAC	Audit and Financial Management Advisory Committee Assists the Administrator in overseeing SBA’s financial operations	BLIF	Business Loan and Investment Fund Fund operated by the Treasury Department to maintain the accounting records of loans approved prior to 1992.
AFR	Agency Financial Report The name of one of the annual PAR reports.	CA	Capital Access (See OCA)
APR	Annual Performance Report A report required by the Government Performance and Results Act that presents a federal agency’s progress in achieving the goals in its strategic plan and performance budget.	CDC	Certified Development Company Refers to the Section 504 Certified Development Company debenture program.
		CFO	Chief Financial Officer The CFO is responsible for the finan-

cial leadership of the Agency. This includes responsibility for all Agency disbursements, management and coordination of Agency planning, budgeting, analysis and accountability processes.

CFR **Code of Federal Regulations**
The codification of the general and permanent rules published in the Federal Register by the executive departments and agencies of the federal government.

CIO **Chief Information Officer**
The CIO is responsible for the management of information technology for the Agency, including the design, implementation and continuing successful operation(s) of information programs and initiatives.

CLA **Office of Congressional and Legislative Affairs**
The CLA assists in the development and enactment of SBA legislative proposals and serves as the liaison for SBA's communications on all legislative and congressional activities.

COO **Chief Operating Officer**

COOP **Continuity of Operations Plan**
A predetermined set of instructions or procedures that describe how an organization's essential functions will be sustained for up to 30 days following a disaster and then return to normal operations.

CRC **Civil Rights Center**
The CRC administers and enforces various federal statutes, regulations and Executive Orders that relate to nondiscrimination and equal opportunity.

CY **Current Year**

DAP **Disaster Assistance Plan**
Executive Order 13411 mandates that federal agencies create a single application that fulfills the information requirements of all applicable federal disaster assistance programs.

DCMS **Disaster Credit Management System**
The electronic system used by the SBA to process loan applications for all new disaster declarations.

DCIA **Debt Collection Improvement Act**
A federal law to maximize collections of delinquent debts owed to the government.

DFP **Dealer Floor Plan**
A small pilot program authorized by the Recovery Act to make revolving loans to retail dealerships including automobile dealers that began in July 2009

DLF **Disaster Loan Fund**
Assists eligible small businesses impacted by disasters.

ECCB **Enterprise Change Control Board**
The ECCB is in charge of the administration of the centralized network accounts for the SBA.

EEO **Equal Employment Opportunity**

ELA **Electronic Loan Application**
Simplifies the application process by providing electronic loan applications.

FASAB **Federal Accounting Standards Advisory Board**
Promulgates accounting principles for federal government reporting entities.

FBCI **Faith-Based and Community Initiatives**
The office promotes SBA partnerships with faith-based and neighborhood organizations to help people receive training and credit assistance.

	In accordance with an Executive Order issued in February 2009, the name will change to the Center for Faith-Based and Neighborhood Partnerships.		
FCRA	Federal Credit Reform Act A law enacted to provide a more realistic picture of the cost of U.S. government direct loans and loan guaranties.	FMFIA	Federal Managers Financial Integrity Act A law Act that primarily requires ongoing evaluations and reports on the adequacy of the internal accounting and administrative control systems of executive agencies.
FECA	Federal Employees Compensation Act Provides compensation benefits to federal civilian employees for work-related injuries or illnesses and to their surviving dependents.	FPDS	Federal Procurement Data System
FEMA	Federal Emergency Management Agency The agency that is tasked with responding to, planning for, recovering from and mitigating against disasters.	FRIS	Financial Reporting Information System SBA's consolidated general ledger system.
FERS	Federal Employees' Retirement System A three-tiered retirement plan for federal employees hired after 1984, composed of Social Security benefits, a basic benefit plan, and contributions to a TSP.	FTA	Fiscal and Transfer Agent
FEVS	Federal Employee Viewpoint Survey	FY	Fiscal Year The SBA fiscal year begins October 1 and ends the following September 30.
FFMIA	Federal Financial Management Improvement Act A law that requires each agency to implement and maintain financial management systems that comply substantially with federal financial management systems requirements, applicable federal accounting standards, and the USSGL.	GAO	U.S. Government Accountability Office The audit, evaluation and investigative arm of Congress.
FHCS	Federal Human Capital Survey A survey administered by OPM to measure federal employees' perceptions about how effectively agencies have managed their workforces.	GC/BD	Office of Government Contracting and Business Development GC/BD works to create an environment for maximum participation by small, disadvantaged and woman-owned business in federal government contract awards and large prime subcontract awards.
		GDP	Gross Domestic Product
		GSA	General Services Administration
		GWAC	Government-wide Acquisition Contract
		HUBZone	Historically Underutilized Business-Zone Encourages economic development by the establishment of federal contract award preferences for small businesses located in historically underutilized business zones.
		IP	Improper Payments (See IPIA)
		IPA	Independent Public Accountant A firm or person, other than the agency's IG, who meets the independence standards specified in GSA, and is

	engaged to perform the audit of a federal agency or for other purposes.		
IPIA	Improper Payment Information Act A federal law, enacted in 2002 to identify and reduce erroneous payments in the government's programs and activities.	MRA	Master Reserve Account SBA's fiscal agent maintains this escrow fund to facilitate the operation of the Certified Development Company program.
IT	Information Technology Refers to matters concerned with the design, development, installation and implementation of information systems and applications.	MRF	Master Reserve Fund SBA's fiscal and transfer agent maintains this reserve fund to facilitate the operation of the 7(a) secondary market program.
LAS	Loan Accounting System SBA's loan origination servicing and disbursement system.	NAICS	North American Industry Classification System NAICS is the standard used by federal statistical agencies in classifying business establishments for the purpose of collecting, analyzing, and publishing statistical data related to the U.S. business economy.
LLG	Liability for Loan Guaranties Net present value of expected future cash flows for outstanding guaranties.	NGPC	National Guaranty Purchase Center SBA's centralized loan guaranty purchase processing center.
LMAS	Loan Management and Accounting System Financial Management System that supports loan accounting.	NIST	National Institute of Standards and Technology An agency of the U.S. Department of Commerce
LMS	Loan Monitoring System Aids the SBA in managing its core loan guaranty programs and serves as one of the building blocks in the overall systems modernization project.	NPV	Net Present Value
MAS	Multiple Awards Schedule	NWBC	National Women's Business Council A bi-partisan federal advisory council created to serve as an independent source of advice and policy recommendations to the President, Congress, and the SBA on economic issues of importance to women business owners.
MAX	Budget Information System OMB uses the MAX Budget Information System to collect, validate, analyze, model and publish budget Information.	OCA	Office of Capital Access The office responsible for small business program loans, lender oversight, the investment company program, the surety bond program and the international trade program.
MD&A	Management's Discussion and Analysis The MD&A is considered required supplementary information for federal financial statements and is designed to provide a high level overview of the Agency.	OCFO	Office of the Chief Financial Officer The office responsible for the finan-

cial activity of the Agency, including Agency disbursements, management and coordination of Agency planning, budgeting, analysis and accountability processes.

OCIO	Office of the Chief Information Officer Supports and provides guidance for SBA's nationwide computer automation and information technology efforts.	OIG	Office of Inspector General Conducts and supervises audits, inspections and investigations relating to SBA programs and operations.
OCRM	Office of Credit Risk Management SBA office that manages program credit risk, monitors lender performance, and enforces lending program requirements.	OMB	U.S. Office of Management and Budget Presidential office that oversees preparation of the federal budget and supervises its administration in Executive Branch agencies.
ODA	Office of Disaster Assistance SBA office that promotes economic recovery in disaster ravaged areas. SBA loans are the primary form of federal assistance for non-farm, private sector disaster losses for individuals and businesses.	OPM	U.S. Office of Personnel Management The federal government's human resources agency.
OFA	Office of Financial Assistance SBA office that administers various loan programs to assist small businesses.	ORACLE	The Accounting program used by SBA's Administrative Accounting Division
OFO	Office of Field Operations SBA office that represents field offices, including regional and district offices, at headquarters.	ORCA	Online Representation and Certification Application an e-Government initiative that was designed to replace the paper based Representations and Certifications process.
OGC	Office of General Counsel Provides legal advice for senior management, as well as legal support for all Agency programs, initiatives and administrative responsibilities.	OVBD	Office of Veterans Business Development The SBA office that works to enhance and increase successful small business ownership by veterans.
OHCM	Office of Human Capital Management Supports the strategic management of human capital in the accomplishment of the Agency's mission.	PAR	Performance and Accountability Report Reporting that presents financial, budgetary and performance information to OMB, Congress and the public.
OIC	Office of Internal Control Is part of the SBA Office of the Chief Financial Officer, and is the office	PCECGF	Pollution Control Equipment Contract Guaranty Fund Supports costs associated with the credit portfolio of pre-October 1991 pollution control equipment loans and guaranties being liquidated by the SBA.

APPENDICES

PIA	Privacy Impact Assessment Part of the Privacy Impact Statement from the Privacy Act.				
PII	Personally Identifiable Information Any information that can identify a person.		SBDC	Small Business Development Center Program SBDCs deliver management and technical assistance, economic development and management training to existing and prospective small businesses through cooperative agreements with universities and colleges and government organizations.	
PLP	Preferred Lender Program Covers certified or preferred lenders that receive full delegation of lending authority.				
POA&M	Plan of Action and Milestones				
PPS	Probability Proportional to Size		SBG	Surety Bond Guarantee Program Provides guaranties, bid, performance and payment bonds for contracts up to \$2 million for eligible small businesses that cannot obtain surety bonds through regular commercial channels.	
PY	Prior Year				
QA	Quality Assurance — Function to assure that project deliverables meet SBA's requirements and quality standards.				
QAR	Quality Assurance Review		SBGRF	Surety Bond Guaranty Revolving Fund All of the contractor and surety fees collected by SBA are deposited in the SBG Revolving Fund at the US Department of Treasury, which is used to pay claims.	
Recovery Act	American Recovery and Reinvestment Act of 2009 Most often referred to as the Recovery Act in SBA documents, may also be referred to as ARRA.				
SAS	Statement on Auditing Standards Establishes standards and provides guidance on the design and selection of an audit sample and the evaluation of the sample results.		SBIC	Small Business Investment Company Provides equity capital, long-term loans, debt-equity investments and management assistance to small businesses, particularly during their growth stages.	
SAT	Senior Assessment Team		SBLC	Small Business Lending Company Non-depository small business lending companies listed by the SBA Office of Capital Access.	
SBA	Small Business Administration A federal agency of the Executive Branch whose mission is to aid, counsel and protect the interests of small businesses and help families and businesses recover from disasters.		SBPRA	Small Business Paperwork Relief Act of 1992	
SBAExpress	Provides selected lenders with a 50 percent guaranty on their loans in exchange for the ability to primarily use their own application and docu-		SBREFA	Small Business Regulatory Enforcement Fairness Act	
			SCORE	A volunteer organization, sponsored by the SBA that offers counseling and	

	training for small business owners who are starting, building or growing their businesses.		
SDB	Small Disadvantaged Business Small business owned and controlled by individual(s) who are socially and economically disadvantaged.	TOP	Treasury Offset Program A centralized debt collection program developed by the Treasury Department's FMS to assist agencies in the collection of delinquent debts owed to the Federal Government.
SFFAS	Statements of Federal Financial Accounting Standards Agreed upon specific standards and concepts published in the Federal Register.	VAT	Vulnerability Assessment Team Performs monthly scans of network-attached devices to identify and remedy network vulnerabilities.
SOP	Standard Operating Procedure SOPs are the primary source of the Agency's internal control.	WBC	Women's Business Center WBCs provide long-term training and counseling to women owning or managing a business, including financial, management, marketing and technical assistance, and procurement.
SOX	Sarbanes-Oxley Act 2002 The law introduced major changes to the regulations of financial practice and corporate governance.		
SSBIC	Specialized Small Business Investment Company Provides equity capital, long-term loans, debt-equity investments and management assistance to socially or economically disadvantaged small businesses.		

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Rory Berges
Debra Braswell
Jeffrey Brown
Joshua Bull
Jonathan Carver
Ashok Chaudhry
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Mary Dam
Gayle Daugherty
Tamara Dollarhite
Leon Fleischer
Jananne Garl
Michelle Gierwatoski
Leslie Godsey
Gordon Goeke
Timothy Gribben
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Joseph Henry
Malene Hernandez
Blake Hoing
Jonathan Jones
Laura Kennedy
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John Kushman
Luan Loerch-Wilson
Theresa Lucero
Valerie Meadows

Robert Montgomery
Maureen Moore-Vellucci
JoAnn Mueller
Rosemary Ngwiri
Sarada Parthasarathy
Mathew Pascarella
Mike Peterson
Janette Porter
Anthony Powell
Tong Qin
Steve Ramey
Ann Marie Schaefer
Ashley Schiller
Charles Sensensey
Rebecca Shoustal
Rodney Simoneau
Katrina Sterling
Bruce Swartz
Sylvia Thornton
LaNae Twite
Darrell White
Donna Wood
Petrina Worthington
Uma Yanamandra

PROGRAM OFFICES

Monique Allen
Michael Avant
Charles Brinkley
Dennis Bumpass
Martin Conrey
Jeanne Crepeau
Paul Christy
Eugene Donaldson
Alan Escobar
Roger Garland
Martin Gold
Grady Hedgespeth
Terrance Hetherington
Walter Intlekofer
Cyril Jones
Gene Lambey
Nina Levine

Dionna Martin
Nathan Osburne
Bruce Purdy
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SBA

**U.S. Small Business Administration
Office of Performance Management
and Chief Financial Officer
409 Third Street, S.W.
Washington, DC 20416**

Attached CD – Supplementary Information

SI 1 – SBA Programs and Offices

(In alphabetical order)

Center for Faith-based and Neighborhood Partnerships

Faith-based and community organizations can play an important role in helping the SBA reach, train, and finance the entrepreneurs whose businesses will bring jobs and hope to economically distressed communities all across the nation. The Center for Faith-based and Neighborhood Partnerships promotes SBA partnerships with faith-based and community organizations to help build awareness of SBA's programs that can transform neighborhoods and change lives. Additionally, the office informs faith-based and neighborhood organization of SBA's loan programs that require non-profit intermediary participation and actively encourages qualified faith-based and neighborhood organizations to apply for certification as microloan intermediaries.

Executive Secretariat

The Office of the Executive Secretariat works with senior management officials to formulate the Administrator's and Deputy Administrator's written correspondence. Under the leadership of the associate deputy administrator for management and administration, ExecSec reviews, edits, and manages correspondence, rules, and regulations. ExecSec also reports products to and from the Office of the Administrator, Deputy Administrator and chief of staff. Together with CLA, OGC, and program offices, ExecSec ensures that correspondence and written products are delivered in the most timely and efficient manner, while providing useful, reliable information, and advice to Congress, other federal agencies, and small business owners nationwide.

Office of Advocacy

The Office of Advocacy is an independent voice for small business within the federal government. It represents the interests of small entities including small businesses, small organizations, and small governmental jurisdictions. Appointed by the President and confirmed by the U.S. Senate, the Chief Counsel for Advocacy directs the office. The Chief Counsel advances the views, concerns, and interests of small business before Congress, the White House, federal agencies, federal courts, and state policymakers. Economic research, policy analyses, and small business outreach help identify issues of concern. Regional advocates and an office in Washington, D.C. support the Chief Counsel's efforts. The Office of Advocacy's economic research, regulatory interventions, and model state legislation initiative reduce regulatory barriers that impede small business growth and development.

Office of Business Operations

The Office of Business Operations plans, directs, and executes all administrative management functions within SBA headquarters, and monitors administrative programs in field offices. It develops policies and procedures for the procurement of supplies, equipment, and non-personnel services. This office also implements and manages approved grants and cooperative agreements.

Office of Capital Access

The Office of Capital Access assists small businesses in obtaining the loans necessary for growth by being a gap lender, providing assistance to small businesses that would otherwise would not qualify for un-guaranteed financing, obtaining equity, or taking advantage of procurement opportunities. Programs include the following:

- The 7(a) loan program requires the SBA's lending partners to certify that the applicant was unable to qualify for loans elsewhere on reasonable terms.
- The 504 program, which has a statutorily mandated job creation component, fills another lending gap by providing long term, fixed rate financing for major assets such as real estate and heavy equipment.
- The Surety Bond Guarantee is a program that serves as a gap surety bond credit provider, expanding the bond credit and capacity of small contractors that would not otherwise be able to compete for public and private work.
- Small Business Investment Center financings generally support smaller transactions that may not otherwise receive funding from private venture firms or financial institutions.
- **The Office of International Trade enhances the ability of small businesses to compete in the global marketplace; facilitates access to capital to support international trade; ensures the interests of small business are considered and reflected in trade negotiations; and supports and contributes to the U.S. government's international commercial and economic agenda.**
- The Office of Credit Risk Management provides risk management based on monitoring, reviewing, and oversight of the 7(a) and 504 lenders and microloan intermediaries; and monitoring and analysis of the 7(a), 504, microloan and disaster portfolios.

Office of the Chief Financial Officer and Performance Management

The Office the Chief Financial Officer conducts and promotes effective financial management activities for the SBA including budget, credit subsidy, financial operations, financial systems and internal controls. It develops and maintains integrated accounting and financial management systems; directs, manages, and provides policy guidance and oversight of all Agency financial management personnel, activities, and operations; approves and manages financial management systems design and enhancement projects; develops budgets for financial management operations and improvements; implements Agency asset management systems; and monitors the financial execution of the Agency budget in relation to actual expenditures.

The Office of the Chief Financial Officer and Performance Management provides tools and guidance to assist the Agency in expanding its capacity to conduct and utilize the results of program evaluations. It also helps the Agency develop better performance measures in order to facilitate the SBA's continued movement from measuring activity outputs to measuring programmatic and Agency outcomes. It builds Agency capacity for results-based management through training and outreach to program offices and supports the Agency's strategic planning. The office also prepares annual accountability and/or performance reports, and establishes and implements Agency-wide policies for management integrity and audit follow-up, including internal controls.

Office of the Chief Information Officer

The Office of the Chief Information Officer provides information technology leadership, products, services and operational support for the SBA. The chief information officer is the principal advisor to the Administrator on information technology matters and has overall responsibility for developing, managing and monitoring SBA-wide IT systems, projects, personnel and expenditures. The office provides information technology governance support to the Agency, ensuring that the SBA manages its current and prospective IT investment portfolio in accordance with the laws, regulations and policies applicable across government.

The OCIO manages the SBA's functional IT units encompassing systems development, operations, voice and data communications and user support. Directly or through contractors, the OCIO has responsibility for over 80 current, mission oriented IT systems that support SBA program delivery and enable the Agency to equip and outfit its employees with current hardware, software and computing tools, such as email, wireless capabilities and remote access for telecommuters. This office manages and maintains the SBA's web presence on www.sba.gov.

The OCIO is also the Agency's lead office for information security, data privacy, electronic identity protection and incident reporting, including information technology aspects of *COOP*, continuity of operations planning.

Office of Communications and Public Liaison

The Office of Communications and Public Liaison has the principal responsibility for developing and implementing effective communications strategies to ensure that the SBA's mission, programs, services and initiatives are articulated clearly and consistently to the American public in general and the small business community in specific. It supports field and program offices with planning and implementation of effective communications strategies. OCPL plays the chief role in articulating, explaining and promoting Agency policy and goals to the national news media.

Through Community Relations and the Office of Strategic Alliances within OCPL, the SBA forms alliances with for-profit corporations, small businesses, non-profit organizations, trade and professional associations, academic institutions, and public-sector agencies. The alliances offer opportunities to network on areas of common interest.

This office manages the web content on www.sba.gov and is also the federal managing partner for *Business Gateway*, www.business.gov, a program integrating web resources to provide small businesses and aspiring entrepreneurs with information services that save time and money, engage citizens to participate, and enable collaboration across all levels of government.

Office of Congressional and Legislative Affairs

The Office of Congressional and Legislative Affairs assists in the development of SBA legislative programs and serves as the communications focal point on legislation and congressional activity. The CLA monitors legislation and policies introduced by Congress and government agencies to determine their effects on the SBA and small business. It furthers the goals of the SBA and enables Members of Congress to best serve their small business constituencies by promptly providing accurate, current, and continuous information to Members of Congress, congressional committees, and others interested in SBA programs. It also devises and implements legislative strategy and has primary responsibility for all matters relating to the congressional and legislative functions of the SBA. It provides liaison with legislative personnel at the White House, the Office of Management and Budget, and various federal departments and agencies. It coordinates with program offices and field offices to ensure continuity and consistency in the SBA's communications with Congress.

Office of Disaster Assistance

The Office of Disaster Assistance plays a vital role in the aftermath of disasters. Through ODA, the SBA is responsible for providing affordable, timely, and accessible financial assistance to homeowners, renters, and businesses of all sizes affected by disaster. Financial assistance is available in the form of low-interest, long-term loans. The SBA's disaster loans are the primary form of federal assistance for the repair and rebuilding of non-farm, private sector disaster losses. For this reason, the disaster loan program is the only form of SBA assistance not limited to small businesses. ODA makes two types of disaster loans:

- Physical disaster loans are for permanent rebuilding and replacement of uninsured or underinsured disaster-damaged privately-owned real and/or personal property. The SBA's physical disaster loans are available to homeowners, renters, businesses of all sizes and nonprofit organizations.
- Economic injury disaster loans provide necessary working capital until normal operations resume after a disaster. Economic injury disaster loans are restricted to small businesses and non-profit organizations.

Office of Disaster Planning

The Office of Disaster Planning reports directly to the SBA Administrator and is responsible for integrating disaster planning, preparedness activities and disaster response programs for all SBA offices.

The office provides direction and oversight to the Agency's Office of Disaster Assistance in coordinating the utilization of SBA resources to assist citizens, communities and businesses in response to disaster occurrences and long term recovery needs. It also represents the SBA on various inter-governmental bodies related to disaster response and recovery and works to ensure that the Agency and its resource partners coordinate effectively to help serve disaster victims. The Agency's disaster training operations, exercises and simulation programs also fall under the purview of the Office of Disaster Planning as does the responsibility for monitoring internal and external communications in times of disaster.

Office of Entrepreneurial Development

The Office of Entrepreneurial Development serves the small business community through outreach and public/private sector collaborative ventures and other creative mechanisms with the purpose of providing management and technical assistance through counseling and training to America's small businesses that otherwise would not be able to locate or afford trained and professional assistance. OED provides entrepreneurs with free and low-cost education and training, topical information, and management assistance critical for sound decision-making in the start-up and growth phases of the business cycle. The tools used to accomplish this are OED's SCORE, Small Business Development Center, and Women's Business Center programs; the SBA's online training portal; Emerging Leaders; and delivery systems such as the SBA's district offices.

Office of Equal Employment Opportunity and Civil Rights Compliance

To advance Agency-wide diversity at all levels, and equal access to programs and activities receiving SBA financial assistance, this office works to prohibit discrimination against all SBA employees and applicants based on: race, color, sex, age, religion, disability, national origin, and retaliation for opposition to discriminatory practices or participation in the EEO process. The office of EEO and CRC also works to achieve equal employment opportunity for all qualified employees consistent with the nation's workforce diversity. The office ensures that no person in the United States is denied the benefits of, excluded from participation in, or subjected to discrimination under any program or activity receiving SBA financial assistance, based on race, color, sex, age, disability, national origin, and marital status (extension of credit). In addition, the office ensures that individuals with disabilities have equal access to the SBA conducted or co-sponsored programs and activities.

Office of Field Operations

The Office of Field Operations represents SBA field offices at headquarters. This office:

- Provides policy guidance and oversight to regional administrators and district directors in implementing Agency goals and objectives, and in solving problems in specific operational areas;
- Establishes and monitors performance goals for district offices;
- Provides associate administrators, program heads and the general counsel with a vehicle for overseeing field office program and policy implementation;
- Provides feedback to headquarters management regarding the performance of their programs;
- Ensures that field offices have adequate input into all policy formation and participate in policy deliberations at headquarters;
- Organizes reviews of field offices;
- Informs the SBA Administrator of field activity; and
- Provides coordination with the Office of Disaster Assistance when necessary.

Office of General Counsel

The Office of General Counsel provides legal advice in support of all SBA programs and initiatives. The office helps to minimize the Agency's legal risks and costs, reduce litigation exposure, and ensure compliance with the applicable statutes, regulations, Executive Orders and other legal requirements. OGC provides the legal support necessary to defend the SBA's interest in judicial and administrative actions, and proactively represent the Agency in all legal matters that arise in the context of its financial assistance, procurement and contracting programs, as well as labor and employment disputes.

Office of Government Contracting and Business Development

The Office of Government Contracting and Business Development promotes increased small business participation in the federal procurement market for goods and services. The office fulfills the SBA's statutory mission to ensure that a fair share of federal procurement goes to small businesses.

Working with federal agencies, the SBA negotiates procurement goals, monitors performance, encourages the use of small business sources, provides procurement training and technical assistance to small firms, and provides policy direction and guidance to federal agencies. Several of the government-wide goals are statutory, including small businesses, small disadvantaged businesses, women-owned small businesses, HUBZone small businesses, and service disabled veterans-owned small businesses.

Office of Hearings and Appeals

The Office of Hearings and Appeals was established in 1983 to provide an independent, quasi-judicial appeal of certain SBA program decisions. OHA formally adjudicates disputes rising in numerous jurisdictional areas. These include appeals regarding SBA formal size determinations; appeals from contracting officer designations of North American Industry Classification System codes for procurements government-wide; appeals regarding certain SBA determinations relating to development companies; and appeals from Agency and private certifier small disadvantaged business determinations, all of which, by regulation, may be decided either by an Administrative Judge or an Administrative Law Judge. OHA's jurisdiction also includes 8(a) BD program eligibility, suspension, and termination appeals, and salary offset appeals, all of which, by statute, must be decided by an administrative law judge.

Office of Human Capital Management

The Office of Human Capital Management develops and provides innovative human capital strategies. The OHCM advises SBA management with respect to selecting, developing and managing a high-quality, productive workforce. This office sets the SBA's workforce development strategy; assesses current workforce characteristics and future needs based on the SBA's strategic plan; aligns human resources policies with organization mission, strategic goals, and performance outcomes; develops and advocates a culture of continuous learning to attract and retain employees with superior abilities; identifies best practices and benchmarks studies; and creates systems for measuring intellectual capital and identifying links of that capital to organizational performance and growth. This office also implements laws, rules and regulations governing the civil service.

Office of the Inspector General

The Office of Inspector General is an independent office created by law within the SBA to conduct and supervise audits, investigations, and other reviews relating to SBA programs and supporting operations; detect and prevent waste, fraud, and abuse; and promote economy, efficiency, and effectiveness in the administration and management of SBA programs. The inspector general keeps the SBA Administrator and the Congress fully informed of any problems, recommends corrective actions, and monitors progress in the implementation of such actions. The two operating components of the OIG are the Auditing Division and the Investigations Division. The Auditing and Investigations Divisions each administer their respective activities through staff located in various locations around the country. The Management and

Policy and Counsel Divisions support both the inspector general and the operating divisions by providing policy, planning, administrative, and legal services, respectively.

Office of the National Ombudsman

The Office of the National Ombudsman fosters a more small-business–friendly federal regulatory enforcement environment by assisting small businesses when they experience excessive federal regulatory enforcement actions, such as repetitive audits or investigations, excessive fines, penalties, threats, retaliation, or other unfair enforcement action by a federal agency. It does this by evaluating how federal agencies treat small businesses during enforcement or compliance actions.

Office of the National Women’s Business Council

The Office of the National Women’s Business Council undertakes a variety of programs and initiatives in support of women-owned businesses. The council holds two public council meetings and other public roundtable events. It publishes research study reports, *Issue in Brief* reports (which synthesize and summarize federal and other research information for women business owners and policy makers on topics such as health care and federal procurement), and fact sheets on the numbers and growth of categories of women-owned firms. The council manages two web sites, www.nwbc.gov and www.womenbiz.gov, plus a bimonthly e-newsletter, *Engage!*

Office of Native American Affairs

The SBA, through its Office of Native American Affairs, coordinates Native American initiatives and develops policies and procedures to ensure that SBA assistance is made available to American Indians, Native Alaskans, and Native Hawaiians. The initiative consists of three major components: marketing, outreach, and training to enhance business opportunities.

Office of Policy and Strategic Planning

The Office of Policy and Strategic Planning is responsible for evaluating the existing policies and programs of the Small Business Administration as well as translating economic, social and demographic trends that have an impact on small business competitiveness into policy prescriptions that will allow the Agency to be more proactive in addressing the needs of small business.

Office of Veterans Business Development

Statutes direct the Office of Veterans Business Development to conduct comprehensive outreach on behalf of the Agency and to be responsible for the formulation, execution, and promotion of policies and programs of the Administration. To accomplish these tasks, OVBD operates its national outreach initiative and provides direct service delivery through utilization of funding agreements with resource partners, coordination of outreach and service delivery with other federal agency partners, and development of Agency program initiatives.

SI 2 – Strategic Plan FY 2008-2013 — This document can be found at
<http://collab.sba.gov/sites/ocio/PMO/Strategic%20Plans/SBA%20Strategic%20Plan/SBA%20Strategic%20Plan%20FY%202008-2013.pdf>

SI 3 – Strategic Plan FY 2011-2016 — This document can be found at
http://www.sba.gov/idc/groups/public/documents/sba_homepage/serv_strategic_plan_2010-2016.pdf

SI 4 – Detail of OIG Audit Follow-up Activity

Disallowed / Questioned Costs

Report # 4-40, SBA Guaranteed Loan To Elatec Technology Corporation And HK Equipment, Inc.

Summary: The audit objective was to determine if the lender and borrowers materially complied with SBA's requirements in originating, closing and liquidating the loan. The audit recommended the Agency recover the payment made to purchase a guaranty.

Final Action: \$0.00 collected / \$246,640.00 written off

Report # 8-09, Loan Classifications and Overpayments on Secondary Market Loans

Summary: The objectives of the audit were to determine whether SBA classified secondary market loans appropriately, purchased loans from the secondary market in a timely manner and pursued lenders for overpayments it made. The audit recommended the Office of Financial Assistance ensure that guarantees are purchased within 30 days and that the Fiscal and Transfer Agent's transcript is used when the lender's transcript is incomplete.

Final Action: \$1,300,000.00 collected / \$0.00 written off

Report # 8-18, Audit of Six SBA Guaranteed Loans

Summary: The audit report identified six loans that warranted immediate Agency attention during an ongoing audit of the liquidation process at the National Guaranty Purchase Center in Herndon, Virginia. The audit recommended the Office of Financial Assistance seek recovery, plus interest, of the guaranty paid by SBA to two banks.

Final Action: \$0.00 collected / \$379,643.00 written off

Report # 9-12, Review of SBA's National Guaranty Purchase Center Furniture Contract

Summary: The review was conducted in response to an anonymous complaint that a prime contractor received an advance payment for furniture that was never delivered. The audit recommended the Office of Management and Administration determine whether invoices were paid under the proper contract or purchase order and recover any funds, if necessary. And, to determine whether the contractor performed the work and seek reimbursement if it was not.

Final Action: \$239,030.00 collected / \$0.00 written off

Report # 10-03, Application of Insurance Offsets for Gulf Coast Disaster Loans

Summary: The audit objective was to determine whether SBA properly reduced Gulf Coast Hurricanes loan balances to reflect flood and hazard insurance offsets. The audit recommended the Office of Disaster Assistance resolve two over-disbursements.

Final Action: \$314,363.00 collected / \$0.00 written off

Funds Put To Better Use

Report # 8-09, Loan Classifications and Overpayments on Secondary Market Loans

Summary: The objectives of this audit were to determine whether SBA classified secondary market loans appropriately, purchased loans from the secondary market in a timely manner and pursued lenders for overpayments it made to secondary market investors. The audit recommended the Office of Financial Assistance (OFA) to require lenders request guarantee purchase when interest is 120 days or more days past due. It also recommended that OFA reduce servicing fees owed by the amount of fees owed SBA from the lender.

Final Action: \$7,200,000.00 implemented / \$0.00 not implemented

Report # 9-08, The Liquidation Process At The National Guaranty Purchase Center

Summary: The audit objectives were to determine if the Center's liquidation process addressed lender noncompliance to mitigate losses and adequately managed loans in liquidation status. The audit recommended the Office of Financial Assistance recover improper payments and liquidation proceeds from lenders identified in the audit report.

Final Action: \$0.00 implemented / \$2,690,427.00 not implemented

Report # 9-09, Borrower Eligibility for Gulf Coast Disaster Loans

Summary: The objective of the audit was to determine whether the SBA had controls in place to prevent ineligible applicants from receiving disaster loans. The audit recommended the Agency instruct loan officers to follow SOP requirements for residency verification.

Final Action: \$683,200.00 implemented / \$0.00 not implemented

Report # 9-10, SBA's FY 2007 Improper Payment Rate for the Disaster Loan Program

Summary: The objective of this audit were to determine whether SBA was properly identifying improper disaster loan payments and correctly estimating the improper rate for the program. The audit recommended the Executive Office of Disaster Strategic Planning and Operations direct the Office of Disaster Assistance to recalculate the FY-2008 estimate of improper payments.

Final Action: \$1,539,761,288.00 implemented / \$0.00 not implemented

**Final Action on Audit Recommendations Not Completed Within 1 Year
October 1, 2009 – September 30, 2010**

Report # 0-14, 7(a) Service Fee Collections

Program: OCFO

Date Issued: 03/30/2000

Management Decision Date: 08/22/2000

Explanation: The recommendation is to establish receivable accounts for 7(a) loan service fees. This final action cannot be completed until October 2011 when the LMAS receivable calculation function has been implemented.

Report # 3-08, SBA's Oversight of the Fiscal Transfer Agent For The 7(a) Loan Program

Program: CA

Date Issued: 01/30/2003

Management Decision Date: 10/15/2003

Explanation: The recommendation is to the Office of Capital Access to develop SBA procedures and regulations governing the proper operation of the Master Reserve Fund. An SOP has been delayed in internal clearance. This final action is expected by 06/30/2011.

Report # 3-26, Microloan Program: Moving Toward Performance Management

Program: Microloan

Date Issued: 05/13/2003

Management Decision Date: 08/28/2003

Explanation: Three recommendations remain open to the Office of Financial Assistance. 1) Work with the Office of Field Operations to establish a task force to develop a system for district office marketing and oversight of the Microloan program. A task force is underway. The final action is expected by 03/31/2011. 2) Ensure the development of a comprehensive Microloan program SOP. This SOP is in clearance and is expected to be issued by 12/31/2010. 3) Ensure program goals are set and require outcome-oriented data. Principal program goals are set forth in the SBA microloan regulations and these can only be modified by a regulatory change. This recommendation is tied to three recommendations in the FY-2010 audit report, "SBA's Administration Of The Microloan Program Under The Recovery Act." These recommendations are expected to be completed at the same time, by 06/30/2011.

Report # 4-34, SBA's Process for Complying With the FMFIA Reporting Requirements

Program: OCFO

Date Issued: 07/29/2004

Management Decision Date: 09/09/2004

Explanation: The two recommendations remaining open are to the Office of the Chief Financial Officer to revise, clear and issue the draft SOP 00 02 3 and clearly define material weakness as it relates to SBA and at the different levels of management within the Agency. The current draft SOP needs some rewriting. A recent change in key staff requires additional time for familiarization with the existing internal control structure before the SOP can be effectively updated. These final actions are expected to be completed by 03/31/2011.

Report # 6-10, SBA's FY 2005 Financial Statements Management Letter

Program: OCFO

Date Issued: 01/18/2006

Management Decision Date: 03/06/2006

Explanation: There is one open recommendation to the Office of the Chief Financial Officer to update the accounting SOP to include SBA's policies and procedures for processing detailed accounting transactions. The draft SOP has been revised and is being placed into Agency clearance again. SBA continues to use online tables to document its accounting transactions policy and procedures. The recommendation is expected to have final action by 02/28/2011.

Report # 6-25, SBA's Implementation of The Improper Payments Information Act (IPIA)

Program: OCFO

Date Issued: 06/21/2006

Management Decision Date: 07/19/2006

Explanation: The recommendation is to the Office of the Chief Financial Officer to develop Procedure Notices or SOPs as internal guidance when changes to IPIA requirements are issued by OMB. A draft SOP was developed, but needs some rewriting. A recent change in key staff requires additional time for familiarization with the existing internal control structure before the SOP can be effectively updated. This final action is expected to be completed by 03/31/2011.

Report # 6-34, Policies and Procedures For the SBAExpress and Community Express Loan Programs

Program: OCA

Date Issued: 09/29/2006

Management Decision Date: 09/30/2009

Explanation: There are five open recommendations to the Office of Capital Access (OCA).
1) Promulgate regulations to govern the SBAExpress Program in order to ensure that the Agency has sufficient legal authority. OCA has developed a schedule to issue SBAExpress Regulations. This recommendation is expected to have final action by 06/30/2012.
2) Revise the Guide to establish criteria as to when lenders are permitted to use credit scores. This will be addressed in the next rewrite of SOP 50 10. Other general guidance on determining credit worthiness may be developed in the meantime. This recommendation is expected to have final action by 09/30/2011.
3) Promulgate regulations to exempt the SBAExpress Program from existing regulations that conflict with the SBAExpress Program Guide. OCA has developed a schedule to issue SBAExpress Regulations. This recommendation is expected to have final action by 06/30/2012.
4) Amend the Guide to set forth loan portfolio performance standards for lenders with no 7(a) Program lending experience that seek admission to the SBAExpress Program. This will be addressed in the next rewrite of SOP 50 10. This recommendation is expected to have final action by 09/30/2011.
5) Revise the Community Express Program Guide to address the recommendations set forth in Concerns 1-4, as applicable. A resolution has been delayed since the future of the Community Express Program is uncertain. This recommendation is expected to have final action by 09/30/2011.

Report # 7-03, SBA's FY-2006 Financial Statements**Program:** M&A**Date Issued:** 11/15/2006**Management Decision Date:** 01/04/2007

Explanation: The recommendation is to the Chief Operating Officer, in conjunction with appropriate program officials, to ensure that policies are implemented regarding segregation of duties for FRIS, JAAMS, DCMS and LAS. The Office of the Chief Information Officer has developed a generic roles matrix and distributed it to systems owners for education, review and customization for their environments. This final action is expected to be completed by 06/30/2011.

Report # 7-28, SBA's Oversight of Business Loan Center, LLC**Program:** Office of the Administrator**Date Issued:** 07/11/2007**Management Decision Date:** 09/16/2008

Explanation: The recommendation is to the Office of Capital Access to mitigate risk posed by Business Loan Center, LLC (BLX) and promote consistent and uniform enforcement actions by developing SOPs that provide an integrated system of enforcement activities. BLX is no longer an active SBA lender. To avoid undue future risk to the Agency, SBA will publish a lender enforcement SOP to promote consistent and uniform actions. The final action is expected to be completed by 12/31/2010.

Report # 7-29, Quality Assurance Reviews of Loss Verifications**Program:** ODA**Date Issued:** 07/23/2007**Management Decision Date:** 09/30/2009

Explanation: The two open recommendations are to the Office of Disaster Assistance (ODA).

1) Recommend the Deputy Administrator of ODA pursue a reassignment of Quality Assurance Reviews (QAR) responsibilities to an SBA organization outside of ODA. QAR agreed that the responsibilities related to loss verification would be performed by the Most Efficient Organization A76 vendor. However, the performance period for this MEO effort ended on September 30, 2010 and the ODA will not be recompeting this function. ODA believes the responsibilities rest within ODA and has established a multi-layered approach within ODA. 2) Recommend the Deputy Administrator of ODA ensure QAR guidance is developed that requires responsible QAR officials to document the reasons for exceptions and any changes to initial QAR results. ODA will initiate a multilayer approach to ensure quality control. Quality control will be performed and documented in the field by the team leader or designee with results reported to the Production Manager on a real time basis. These recommendations are expected to have final action by 06/30/2011.

Report # 7-32, Advisory Memorandum: Surety Bond**Program:** OSG**Date Issued:** 09/28/-2007**Management Decision Date:** 11/27/2007

Explanation: The recommendation is to the Office of Surety Guarantees to require a surety to perform specific actions before hiring a replacement contractor. A regulation addressing this situation is in clearance. This final action is expected to be completed by 01/31/2011.

Report # 8-06, SBA's FY 2007 Financial Statements Management Letter**Program:** OFA**Date Issued:** 12/14/2007**Management Decision Date:** 12/18/2007

Explanation: There are three open recommendations to the Office of Capital Access. 1) To mitigate potential risks regarding the guaranteed loan purchase process, issue the updated SOP 50 51, Loan Liquidation and Acquired Property. 2) Implement procedures regarding the evaluation of lenders. 3) Implement an action plan for timely updating, reviewing and approving of SOPs. Revisions to SOP 50 51 has been cleared and the comments are being addressed. The SOP will be issued before the end of this calendar year. All final actions are expected to be completed by 12/31/2010.

Report # 8-12, Oversight of SBA Supervised Lenders

Program: CA

Date Issued: 05/09/2008

Management Decision Date: 06/26/2008

Explanation: One recommendation remains open to the Office of Capital Access to establish risk mitigation goals applicable to each loan program and the entire lending portfolio. SBA executed a contract in September 2010 to provide consulting services on OCA's risk management practices. The contractor will assist OCRM in developing the measures. This final action is expected to be completed by 06/30/2011.

Report # 8-13, Planning For The Loan Management And Accounting System Modernization And Development Effort

Program: CA

Date Issued: 05/14/2008

Management Decision Date: 08/11/2008

Explanation: There is one remaining open recommendation to the Office of Financial Assistance to make cost-effective remediation of mainframe vulnerabilities a priority and ensure that migration of LAS occurs before the current mainframe contract expires in 2012. The objectives of the former LMAS project will be incorporated under the new Incremental Improvements Project (IIP) initiative. The mainframe contract will be extended through March, 2013. This final action is expected to be completed by 03/31/2013.

Report # 9-05, SBA's FY 2008 Financial Statements - Management Letter

Program: OFA

Date Issued: 12/17/2008

Management Decision Date: 02/18/2009

Explanation: The two open recommendations are to the Director of the Office of Financial Assistance to reinforce the importance of the collateral analysis in an updated SOP and ensure the revised Disaster Loan SOP identifies procedures related to the disposition of collateral. The SOP is on track and will be in clearance during the first quarter of FY-2011 and issued during the second quarter. These recommendations are expected to have final actions by 02/28/2011.

Report # 9-15, Participants In The 8(a) Program By Firms Owned By Alaska Native Corporations (ANCs)

Program: GC/BD

Date Issued: 07/10/2009

Management Decision Date: 08/04/2009

Explanation: The recommendations are to Government Contracting & Business Development to determine whether 8(a) firms owned by ANCs and tribes should continue to be exempt from the cap on total sole source awards, expedite the implementation of BDMIS, and finalize regulations necessary to fully implement GAO's recommendations. Proposed 8(a) regulations were published in the Federal Register for comment. These recommendations will be closed when SBA issues the final 8(a) regulations by 12/31/2010.

Report # 9-16, SBA's FY 2008 Improper Payment Rate For The 7(a) Guaranty Loan Program

Program: OCA

Date Issued: 07/10/2009

Management Decision Date: 08/27/2009

Explanation: There are two open recommendations to the Office of Capital Access. 1) Seek recovery of \$2.3 million from lenders on the loans listed in the audit report. These loans are under various states of review. Three need OGC opinions, and recovery is not warranted for another three. 2) Fully implement the corrective action plan to reduce improper payments. The Agency has a plan to reduce improper payments. However, a major component of this plan has not yet been fully implemented. These recommendations are expected to have final actions by 12/31/2010.

Report # 9-17, Review of Allegations Concerning How the LMAS Modernization Project Is Being Managed

Program: OCIO

Date Issued: 07/30/2009

Management Decision Date: 09/03/2009

Explanation: The recommendation is to the Office of Capital Access to fully implement the corrective action plan to reduce improper payments in the 7(a) Guaranty Loan Programs. A major component of the corrective action has not yet been fully implemented. This recommendation is expected to have final action by 04/30/2011.

Report # 9-18, SBA's Management of the Backlog Of Post-Purchase Reviews At The National Guaranty Purchase Center

Program: OFPO

Date Issued: 08/25/2009

Management Decision Date: 09/11/2009

Explanation: The recommendation is to the Office of Financial Program Operations to include detailed scopes of work, measurable performance metrics, deliverables and adequate acceptance criteria in service contracts. The measurement standards still must be completed for the contract employees in each Center. This recommendation is expected to have final action by 12/31/2010.