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HOLDING THE SMALL BUSINESS ADMINISTRATION ACCOUNTABLE: WOMEN'S CONTRACTING AND LENDER OVERSIGHT

HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP

UNITED STATES SENATE

ONE HUNDRED TENTH CONGRESS

SECOND SESSION

January 30, 2008

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ONE HUNDRED TENTH CONGRESS

SECOND SESSION

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HOLDING THE SMALL BUSINESS ADMINISTRATION ACCOUNTABLE: WOMEN'S CONTRACTING AND LENDER OVERSIGHT

WEDNESDAY, JANUARY 30, 2008

UNITED STATES SENATE,
COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP,
Washington, D.C.

The committee met, pursuant to notice, at 10:06 a.m., in room 428–A, Russell Senate Office Building, the Honorable John F. Kerry (chairman of the committee) presiding.

Present: Senators Kerry, Levin, and Snowe.

OPENING STATEMENT OF THE HONORABLE JOHN F. KERRY, CHAIRMAN, SENATE COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP, AND A UNITED STATES SENATOR FROM MASSACHUSETTS

Chairman KERRY. The hearing will come to order. I appreciate your patience. We have another hearing in the Finance Committee and then we have a markup this afternoon, and both Senator Snowe and I are on that, so we are sort of trying to juggle things a little bit here. I appreciate it, and Administrator, thanks for being here. We really appreciate it. Happy new year to you and to others we haven't had a chance to say it to.

This is the first hearing of the Small Business Committee for the Second Session of the 110th Congress. Last year, we had a pretty aggressive hearing schedule. We had 14 hearings, 4 roundtables, 4 markups, and in fact, the Committee—I don't know if this is good or bad, but we wound up setting a new mark for the number of meetings in 1 year. I am not anxious to have meetings for the sake of having meetings, and I don't think Senator Snowe is either. But there is a certain amount of business that is just pent up and a necessary amount of oversight that we need to do.

I am very appreciative for the continuous, consistent support of the Ranking Member in these efforts. There is very little that we haven't done that we haven't worked on jointly and in a bipartisan way in the whole committee. It is a great tradition of this committee and I really appreciate her partnership in this effort.

I am also glad to report that the Committee did make significant progress on a number of issues. We reported out six bipartisan small business reauthorization bills. We are going to continue to work to fully reauthorize those programs and the Small Business Innovation Research Program, which expires on September 30.

I am also glad to report that working with other committees of jurisdiction, which we have done, I think, fairly effectively, we have provided the first real increase in funding for small business programs since 2001. We have also cut taxes for small firms. We have increased transparency in contracting at TSA. We have passed legislation to help small firms become more energy efficient. And we have expanded research and development opportunities for small firms.

But as we know, there is still a lot yet to do, and right now, our focus is on trying to help some of these small firms through very tough economic times.

Just last week, Senator Snowe and I each introduced small business stimulus bills. I guess it is an advantage that we both also happen to be on the Finance Committee and we are able to work both sides of that, tax and small business. We are supporting proposals to expand small business expensing and net operating loss carry-back provisions and also to provide significant tax incentives for small business. The Finance Committee is going to be marking that up this afternoon and I am pleased that we will see the inclusion of small business tax provisions in the stimulus that are going to help spur business investment and free up capital to create jobs and expand the economy. The legislation I put forward, cosponsored by Committee Members Levin and Landrieu, will also encourage government-backed lending.

Today, this is an accountability hearing to follow up on the issues from various hearings which we agreed we would come back and revisit, and in which the Administrator and/or representatives of the agency said this would be the time by which certain things would be in place and we would be able to sort of take stock. So I appreciate the opportunity to do that, particularly on matters as diverse as energy guidelines, disaster reform, lender oversight, and contracting. I appreciate the Administrator being here to help us in that process.

One of the central focuses of today's hearing will be the Women's Procurement Program. I think it is fair to say, Mr. Administrator, that we are deeply concerned. I haven't actually had a chance to talk at great length with Senator Snowe about it, but I know through the staff discussions that there is a lot of concern on the Committee about this rule. It really presents some very serious concerns to the Committee, to be honest with you. In fact, some people see it as just a rank affront to the engagement of women in the business world today.

We as a Congress determined some time ago that it was important to make certain that women have an equal opportunity to be able to provide their goods and services to the Federal Government. It is an enormous procurement opportunity, and it has taken 7 years of pushing in a bipartisan manner from this committee, completely bipartisan—this was put in place in the year 2000—asking for a rule to implement the means by which administrators can set aside a specific amount of contracting for women businesses.

Out of the 140 industries, more than 2,300 contracting categories, the SBA is now suggesting that there are only 4—only 4—that are underrepresented by women. Now, women-owned businesses account for over 30 percent of all firms, yet they get only

3.4 percent of Federal contracting dollars, far short of the 5 percent goal that we set. I think we feel very strongly that that goal is not an unachievable goal and it is not a phony goal. It is something that really ought to be achieved. It ought to be exceeded, if not met.

So we really believe here that this ought to go back to the drawing board and we ought to come up with a workable rule that people can get behind. I have written a letter to the administration outlining my objections to the proposed rule in a more formal way. I will make that letter available to the entire committee.

[The letter of Chairman Kerry follows:]

United States Senate

COMMITTEE ON SMALL BUSINESS & ENTREPRENEURSHIP
WASHINGTON, DC 20510-6350

March 31, 2008

The Honorable Steven C. Preston
Administrator
U.S. Small Business Administration
409 Third Street, S.W.
Washington, DC 20416

Dear Administrator Preston:

In the intervening weeks since our initial comments regarding the proposed rule to implement the long delayed Women's Contracting Set-Aside Program many women have voiced their concerns about the direction the SBA has taken with respect to the Program. The intensity that this issue has engendered in the women's business community leads us to submit this substitute letter in order to clarify and amplify our objections to the SBA's Proposed Rule entitled Women-Owned Small Business Federal Contract Assistance Procedures published December 27, 2007 (72 Fed. Reg. 73285). Our previous letter of February 1, 2008 letter is hereby withdrawn with the submission of this new letter.

First, we must emphasize that by proposing a rule that requires agency-by-agency findings of discrimination you have greatly exceeded your rulemaking authority. It is within Congress' prerogative alone to legislate the parameters of the Women's Procurement Program. And in Public Law 106-554 Congress has spoken and we neither require nor contemplate findings of discrimination for implementation of the Women's Contracting Program. We believe that requiring findings of discrimination agency-by-agency is impermissible and clearly exceeds your rulemaking authority.

Secondly, we reiterate our concern that you have applied an incorrect standard of review to a gender based program. We are deeply concerned that the proposed rule requires gender based programs to satisfy a standard of constitutional scrutiny that exceeds the strict scrutiny standard that has been applied to race-conscious contracting programs. While there have been fewer cases examining the question of what standard of constitutional scrutiny applies to gender-conscious contracting programs, the law is absolutely clear that the constitutional standard that applies to women's programs does not exceed the strict scrutiny standard that applies to race-conscious contracting programs. Courts have variously referred to the appropriate standard for gender-conscious programs as "heightened scrutiny" or "intermediate scrutiny."

While the Court in ***United States v. Virginia*, 518 U.S. 515, 533 (1996)** ruled that an "exceedingly persuasive justification" is necessary to meet this standard, there is no doubt that the evidentiary requirements do not exceed the strict scrutiny standard applied in ***Adarand Constructors v. Pena*, 515 U.S. 200 (1995).** Both in its treatment of the RAND study and in its requirement that there be specific findings of discrimination by each government agency desiring to operate the women's procurement program, this rule

The Honorable Steven C. Preston
March 31, 2008
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imposes a standard that clearly exceeds the strict scrutiny standard that has been applied to race-conscious affirmative action programs. In the numerous court cases upholding race-conscious contracting programs, neither national, federal government-wide studies, nor agency-specific findings of discrimination are currently required.

Furthermore, we also believe that the SBA's use of the narrowest statistical model from the RAND study to implement the program undermines the intent of this Congress to expand opportunities for the broadest number of women-owned small businesses. Amazingly, the SBA has excluded all but four industries from the program. Given that the RAND study can be fairly read to include as many as 87 percent of all industries as underrepresented with respect to women, it is particularly troubling that you have chosen to read the report as narrowly as possible.

We find it hard to believe that cabinetmaking, engraving, other motor vehicles dealers and national security and international affairs are the only industries in which the SBA has determined that women-owned small businesses are under-represented or substantially under-represented in government-wide federal procurement. As a result, contracting officers can only restrict competition under 8(m) to businesses in these industries.

We cannot emphasize enough the depth of our disappointment with this rule. We have waited seven years for implementation of a program that we believe has the potential to open up opportunities for women business owners for years to come. To put it simply, this rule is not what we envisioned and does not reflect Congressional intent. As this Committee has consistently urged for the last seven years, any rule implementing the Women's Procurement Program must include a significant number of industries and must not require any agency to find itself guilty of discrimination.

If you have any questions or need any additional information, please do not hesitate to contact us or have your staff call Gregory Willis at 202-224-5175.

Sincerely,

John F. Kerry
Chariman

Carl Levin
US Senator

Joseph I. Lieberman
US Senator

Maria Cantwell
US Senator

Jon Tester
US Senator

Chairman KERRY. I hope the Committee will join me in sending a message regarding this rule, and we will come back to that, obviously, in the question period.

We are also going to follow up on the lender oversight issue. The BLX $76 million loan scheme showed that SBA needs oversight—we need to understand where we are in making the oversight process more effective.

The subprime mortgage problem is affecting all aspects of our economy. It is one of the things we are trying to address in the stimulus package today, if we can, with a mortgage revenue bond proposal that Senator Gordon Smith and myself and others have put forward. In my travels around my State, I am talking to mayors who are seeing their property tax base shrink as they go through hundreds of foreclosures. In Brockton, Massachusetts, about 1,200 foreclosures are staring them in the face, and that just rips the community apart. It affects the schools, it affects public safety, and it affects the tax base for all of their efforts.

We need to deal with that. It is an example of why catching lender fraud at the early end is such an important effort, more important even than it was when we met on this issue several months ago. The SBA is responsible for some $50 billion in 7(a) and 504 loan guarantees and we need to make certain that the basic changes that make a difference in protecting the taxpayer are in place.

Also, we want to make a few inquiries about the overall redaction issue that we discussed last time regarding the Inspector General's report on the SBA oversight of BLX based on the basic belief that the public deserves as much transparency as possible to facilitate a legitimate understanding of what is happening. Unnecessary secrecy just thwarts most of the goals of the Congress and the Committee and the country in that regard.

There are several other issues, including the Gulf Coast disaster reform, making sure the SBA is helping small firms to become more energy efficient, and we look forward to talking about the Women's Business Centers Renewal Grants Program. I might add that, Mr. Administrator, everything that I have heard is very positive in that vein and we really want to congratulate you and your Deputy Administrator. We have had tremendous positive feedback from the centers around the country who really feel there has been a terrific take-up on that, so we really congratulate you on that and thank you for that. That sort of represents the good upside that everybody looks for in this kind of effort, but we thank you for that.

I know that the funding issue from Congress last year created some of your own issues, and obviously we hope that that can be improved. The Senate passed a higher amount. The House did not. We wound up with a lower amount from the House. So I think the Senate acted in good faith on it and we hope we can try to upgrade that this year.

This is a particularly important time. In all the years I have been on this committee, I guess about 23 years now, we have had ups, we have had downs. We have been able to weather them. But always, the SBA has been an important leverager in that effort and can be very, very important to whatever recovery efforts we initiate, so we look forward to working with you on that, and again I thank you.

Senator Snowe.

OPENING STATEMENT OF THE HONORABLE OLYMPIA J. SNOWE, RANKING MEMBER, A UNITED STATES SENATOR FROM MAINE

Senator SNOWE. Thank you, Mr. Chairman. Thank you for a very productive year, as you indicated, on issues that are so critical to small business. I also thank you for starting off this year with vigorous oversight on some of the key small business programs that we discussed in our oversight hearings last year. This obviously reflects a strong mutual commitment to ensure accountability on many of these programs.

I welcome the SBA Administrator, Mr. Preston, for being here today before the Committee to answer all the questions and for his commitment to honor those programs that we discussed last year, particularly in the contracting programs, lender oversight, and the issues that the Chairman also cited. Our economy couldn't be more fragile, couldn't be more front and center on our agenda, and that is why I am pleased, Mr. Chairman, that we were able to include the small business expensing provision and extending the net carry-back of operating losses from 2 to 5 years that is in the Chairman's mark that is pending before the Finance Committee today. That is an important way to ignite job creation in this country, by allowing small businesses to have access to more capital for investments and stimulating the economy.

I am concerned about the Small Business Women's Contracting Program, and the implementation of it, through the rulemaking process that is pending. I've had discussions with you, Mr. Administrator, when I addressed that the SBA has an opportunity to hit a home run with respect to this rulemaking process and implementing the contracting program and the set-asides for women's contracts by women-owned businesses.

Frankly, I am concerned that the rule would have little, if any, measurable benefit given the way it has been structured. It is a law that was enacted back in 2000, long before your tenure. We have had numerous hearings. We had two proposed rules, three reports, and it appears that we are no closer today than we were then with respect to developing an equitable approach to contracting for women-owned businesses and helping them to access Federal agencies, contracts and the hundreds of billions of dollars that are available to them.

So I feel that the rule is deficient and unlikely to have any practical impact in helping the government satisfy its 5 percent goal, which is ultimately our purpose. And as you can see here with the chart, it indicates that the gross disparity means that only 1,238 businesses really will be affected by the rule that is now pending, and during this comment period, hopefully we can put forward some of our own suggestions. Hopefully, we can get this modified. Only 2 percent out of the 55,000 businesses, only 1,238 businesses that are women-owned would benefit under this rule, and, in fact, only 2 in my home State, of the hundreds of businesses that are women-owned businesses. I know you discuss some of the issues, and hopefully you can get into the methodology that was utilized, because I think it is important.

[See chart attached:]

But secondly, when this proposed rule goes into effect, Federal agencies must admit to a history of gender discrimination, and I find it difficult if not impossible to envision a scenario where a Federal agency would make such an admission. It certainly isn't required anywhere in the Small Business Act, and again, it could be one other barrier to the full implementation of an equitable rule.

This Women's Contracting Program isn't new. We have repeatedly insisted that it be implemented. It has been seven long years, and unfortunately, through our countless efforts, it isn't until now, and I thank you for at least honoring your commitment as you told this committee that you would propose a rule. But I hope that ultimately we can find some ways to modify that rule and promulgate a final rule that would be far more equitable for women-owned businesses.

It is too limited, as is indicated by this chart, and also I think it just doesn't get the job done in maximizing the effectiveness for women business owners and an entrepreneurial climate that is more conducive to grow. If there is any time to secure new avenues to generate revenue for the economy, that time is certainly now.

And so I hope that we can begin to modify the rule. I am certainly going to submit comments, and hopefully in conjunction with the Chairman, as he indicated, or introduce legislation—that is one step in the process that is a much lengthier process to get that done—so that we make a real difference, not just a 2-percent difference. I think that there were many ways in examining the methodology that was used, there were many more options for measurement that would have delineated the number of industries that are women-owned that are underrepresented in the contracting process.

Frankly, we should modify the test. I am talking about this past discrimination as a prerequisite for participation. And we also should substantially broaden the range of applicable business industries for women across this nation and eliminate the unnecessary barriers that have been recently proposed under this contracting rule.

It is important and incumbent upon the Small Business Administration to satisfy this commitment that was made to our committee through the five oversight hearings with respect to this rule and to the other lender oversight issues that have been raised. One was the implementation of the Women's Business Centers Renewable Grant Programs that the Chairman and I along with Senator Sununu made permanent last year as part of the emergency supplemental.

We also heard testimony from the SBA's Inspector General and former SBA staff regarding the problems surrounding the SBA Office of Disaster Assistance, and so we are anxious to hear what progress has been made on those questions.

And also, the Energy Policy Act of 2005 directed the SBA, working with the EPA and other agencies, to develop the Small Business Energy Clearinghouse to assist small businesses in becoming more energy efficient, and it has been more than 3 years since this requirement went into effect, and yet additional energy legislation had to be passed last month to compel SBA to fulfill its obligation under law.

So I think that these are some of the issues that we need to address here this morning and to follow through in implementation and to make sure that it is consistent with the spirit of the law and the intent of the law. Some of these issues are long overdue, and as I said, it certainly predated your tenure. But hopefully we can work together as partners to mitigate some of these issues and to resolve the litany of issues that we are going to discuss here today, which are hindering our nation's small businesses at a difficult and challenging economic time.

And so I hope that we can be more collaborative in that process and trying to make sure that small businesses are able to thrive and increase access to capital through the loan programs, which have also seen a decline in that respect, and the number of lenders have declined, as well. So there are an array of issues that I think that we have to address here this morning and hopefully that we can forge a partnership for this year in addressing these issues, and most especially, first and foremost, is to modify this rule during this comment period, which is scheduled to close, I gather, on February 25.

So I thank you, Mr. Chairman, and I sincerely hope this will be a turning point for working out these issues and becoming a partnership and making substantive differences on these and other issues that are important to small businesses. Thank you.

Chairman KERRY. Thank you very much, Senator Snowe. I appreciate your comments enormously.

Well, Mr. Administrator, I think you have got it sort of outlined, some of the concerns, and we welcome your testimony.

STATEMENT OF THE HONORABLE STEVEN C. PRESTON, ADMINISTRATOR, U.S. SMALL BUSINESS ADMINISTRATION, WASHINGTON, D.C.

Mr. PRESTON. Thank you very much. Thank you for inviting me. I have reiterated it many times, but Senator Snowe, I appreciate your request for a partnership. Any time we can come up and brief you, work through these issues, we are happy to do it, and I know recently we had our team up here briefing the Committee staff on lender oversight.

The proposed rule that will implement the Women-Owned Small Business Federal Contracting Procedures has been published in the Federal Register. It is currently in the 60-day comment period. SBA has been and remains committed to implementing the statutorily authorized set-aside for the program.

I would also like to take this opportunity to discuss SBA's ongoing efforts to improve lender oversight in our loan processing centers in Herndon as well as Sacramento.

Let me start by discussing the Women's Procurement Program. Based on nonpartisan guidance that we received from the National Academy of Sciences, the RAND Corporation conducted a statistical review to determine underrepresentation for women-owned small businesses in Federal contracting. RAND recommended—or, excuse me, NAS recommended considering a variety of data sources and methodologies in order to gain a broad perspective, but in addition, they provided much more specific guidance based on solid reasoning that weighed heavily in our thinking.

First, NAS indicated that greater weight should be given to measures based on contracting dollars going to women-owned small businesses rather than the numbers of contracts. In addition, NAS emphasized the importance of considering more detailed industry information, which is represented by four-digit North American Industry Classification System codes, NAICS codes, rather than the very broad industry classifications. They also highlighted the need to demonstrate that businesses were ready, willing, and able to perform in Federal contracting.

To determine underrepresentation and substantial underrepresentation, RAND identified 28 possible approaches that considered data in the Central Contractor Registry, the Federal Procurement Data System, as well as the Survey of Business Owners from the 2002 Census. After careful consideration of the remaining approaches and in keeping with the direction of NAS and RAND, SBA adopted the approach that we believe best captured the most appropriate measures based heavily on the guidance we received from those institutions.

First, based on the NAS comments and the need to align our findings with Federal policy, we did use measures that considered contract dollars going to businesses rather than numbers of contracts. Clearly, the goal of the statute is to achieve 5 percent for women-owned businesses in terms of contract dollars. Getting revenue from contracts is what creates business value. The entire appropriations budgeting contract and the accounting process in the Federal Government is also based on dollars.

Second, NAS guidance is clear that SBA should use NAICS code levels that more clearly disaggregate between industries performing similar activities. SBA determined that the four-digit NAICS code level best met these criteria. Only the CCR data provided the detail at the four-digit level. SBO data was only available at the two-digit level. In addition, only the CCR data base gave us women-owned small businesses. SBO data compiled them with businesses that didn't meet the small business standard. NAS also questioned whether SBO data would be characterized as ready, willing, and able since it represented all companies in the economy rather than those signed up to do contracting through the CCR.

Frankly, I and many people on my team were surprised by the results of the study. We learned that those women-owned small businesses registered in the CCR actually generally receive a higher percentage of revenue from Federal contracting dollars than other businesses and that the data only showed underrepresentation in four NAICS codes, and that is four out of the 140 that they studied, and I want to avoid any confusion with 2,000 industries. This is four out of 140. The 2,000 relates to some different issue.

According to the study, once women in small businesses register to do business with the Federal Government, they received a higher percentage of their gross receipts from the Federal Government compared with others in their industry sector. The study indicates that the real issue, we believe, is an increase in the number of women-owned small businesses who compete for government contracts. Our goal at the SBA is not only to develop regulations implementing these procedures, but also to help women-owned small businesses so that they can compete both in the private marketplace as well as for Federal contracts.

In 2007, SBA began an initiative to more effectively assist small businesses interested in doing business with the Federal Government. We have realigned our field staff. We provided them with additional training so that they are better equipped to help advise, train, and counsel small businesses so that they are then, in turn, equipped to do the marketing necessary to find procurement opportunities. I think we have made a tremendous amount of progress.

In 2006, contract dollars going to women-owned small business reached a record level, \$11.6 billion. In addition, women-owned small businesses experienced the largest growth in history in any single year since the goal was established at \$1.5 billion. The amount of contracting dollars going to women-owned small businesses is more than 2.5 times what it was in 2005 and has grown almost 17 percent per annum since that period of time. Subcontracting dollars were over \$10 billion and represented about 6 percent of subcontracting dollars.

We are taking a forward-looking approach. First, our programs are all tasked with growing the universe of women-owned businesses and encouraging these businesses to register in the CCR, which makes these businesses eligible to contract with the Federal Government. In addition, the role of the SBA is to help those businesses become ready, willing, and able to undertake and build a successful track record, and we have done a number of things. We have provided our entire field organization this past summer with a full week of training to help them become more effective in outreach and training. We have rolled out a new technology to help other agencies easily find women-owned small businesses to help them meet their contracting needs. We have established outreach goals for all of our offices throughout the country and we are holding Federal agencies accountable through the scorecard.

We also have a number of exciting initiatives planned for the next year. We expect to participate in over 500 procurement-related activities, additional training and matchmaking events in the field, additional online courses on Federal procurement, realigning our field staff to focus on business development and identifying contracting opportunities, as well as continue to increase accountability for Federal agencies.

You know, I think our view here is that there is no one single approach that is going to expand participation of women-owned small businesses but rather a combination of initiatives that take into account the individual needs of the businesses and the best approach to provide those opportunities to women-owned small businesses.

Let me briefly now discuss SBA's progress on improving lender oversight. Obviously, effective lender oversight is foundational to the quality of our programs and our responsibility to the taxpayer. When I appeared before this committee on November 13 last year, I discussed SBA's efforts in managing credit risk, in monitoring lender performance, and in enforcing lender program requirements. We are engaging in an ongoing dialog with the IG on the implementation of their recommendations. Where it makes sense, we implement their recommendations or we take actions to address the issue giving rise to them. Where we don't concur with the recommendation, we explain those conclusions to the IG.

There are a number of steps we have taken and are currently taking to improve oversight that deserve particular attention. We dramatically improved the quality and expanded the scope of our onsite and offsite reviews. We provided greater transparency on our processes to our lenders and giving them access to data on their portfolios and on the portfolio in general. We have issued proposed regulations that would clarify the lender oversight process and lend a level of clarity to our oversight activities. We have implemented training, expanded staffing, and are driving reengineering initiatives at our Herndon processing center that will improve its capacity, responsiveness, and quality in rolling those out to all of our other centers.

We are revamping the SBA Express and Community Express procedures, and we have implemented a process for replacing our loan account system. The new system will contain more information that lenders can see and that we can leverage for future oversight.

I think the agency is well, well ahead of where it was just a couple of short years ago. We clearly have more room to go and I would be happy to report out on that, as well.

But thank you for the opportunity to testify today and I look forward to any questions you might have.

[The prepared statement of Mr. Preston follows:]

Administrator Steven C. Preston
U.S. Small Business Administration
U.S. Senate Small Business and Entrepreneurship Committee
Holding SBA Accountable: Women's Contracting and Lender Oversight

Thank you for inviting me to testify today on behalf of the U.S. Small Business Administration (SBA) regarding the Federal Government efforts in contracting with women-owned small businesses as well as the SBA's activities in small business lending oversight.

I would like to address the contracting issue first. The proposed rule that will implement the Women-Owned Small Business Federal Contracting Procedures set-forth in P.L. 106-554 has been published. Public comments on the proposed rule are due by February 25. SBA has been, and remains, committed to implementing the statutorily-authorized set-aside for women-owned small businesses and intends to do so in a constitutionally valid manner, while at the same time meeting the specific directives provided in the legislation.

History

In 1994, through the Federal Acquisition Streamlining Act (FASA), Congress established a statutory goal of not less than 5 percent of the total value of all Federal Government prime contract and subcontract awards for each fiscal year going to women-owned small businesses (WOSBs). The Federal Government has made consistent progress toward reaching the prime goal. Federal prime contract dollars going to WOSBs increased from \$2.4 billion in FY 1994 to \$11.6 billion in FY 2006 (3.4 percent of contracting dollars). Subcontracting dollars have increased from \$3.6 billion in FY 2000 to over \$10.1 billion in FY 2006, representing 6 percent of subcontracting dollars. SBA's Office of Government Contracting and Business Development (GCBD) is working closely with Offices of Small Disadvantaged Business Utilization (OSDBUs) in the major Federal procuring agencies to promote the use of WOSBs and encourage the Agencies to reach the 5 percent goal.

In December of 2000, Congress passed legislation creating the framework for Women-Owned Small Business Federal Contracting Procedures.

Consistent with the requirement in the legislation for SBA to determine the underrepresentation of WOSBs in the Federal contracting marketplace, SBA itself conducted a study to establish the necessary findings. Once completed, an independent panel of experts at the National Academy of Sciences (NAS) reviewed the study to assess the sufficiency and validity of SBA's methodology. Ultimately, NAS concluded that the original SBA study was flawed. NAS recommended a methodology for performing a study that would more effectively withstand legal and statistical scrutiny.

RAND Report

On February 21, 2006, SBA awarded a contract to the RAND Corporation and it commenced work on a study, in accordance with the methodology recommended by NAS, to determine those industries in which WOSBs are underrepresented and substantially underrepresented in Federal procurement. The RAND study was completed in April 2007 and since then SBA has been engaged in a government-wide effort to complete this proposed rule in a manner that will satisfy both statutory and constitutional requirements.

Following SBA guidelines which were approved by NAS, RAND defined underrepresentation as a disparity ratio of 0.80 or less, while substantial underrepresentation was defined as a ratio of 0.50 or less. NAS recommended applying this analysis to data found in the 2004 Central Contractor Registration (CCR) and the 2005 Federal Procurement Data System / Next Generation (FPDS-NG) cross-referenced with the North American Industry Classification System (NAICS) industry codes at the four-digit level based on either contract dollar amounts or the number of contracts. With the disparity thresholds of 0.50 and 0.80 established, RAND examined 28 different approaches that looked at a wide range of data collected by the Federal Government including data in the CCR, the Federal Procurement Data System/Next Generation (FPDS/NG) and the 2002 Survey of Business Owners (SBO) from the five-year economic Census. Relying on the guidance offered by NAS and the actual results of parsing the data, RAND then began to zero-in on those methods that most accurately measured underrepresentation and substantial underrepresentation. After very careful analysis of the four remaining approaches, SBA adopted the approach that best captured the most appropriate measures. NAS guidance is clear that SBA should use the NAICS code level that most clearly disaggregates between industries performing similar activities. SBA determined that the four digit NAICS code level best meets this criteria. The methodology utilizing the dollar amount was also found to be the most justifiable measure of WOSB contract representation because:

- Most importantly, the very goal (5 percent WOSB participation based on "total value" of contract awards) the statute was intended to support is based on contracting dollars, and thus using contract dollars as the primary measure of representation is most consistent with the statutory framework;
- In addition, Congress appropriates federal funding in dollars;
- The Federal budget is allocated in dollars;
- All government contracts are awarded in dollars;
- The accounting and auditing processes focus on how dollars are spent; and
- Contract numbers do not allow for an accurate accounting of the financial benefits of business development that occur when small businesses receive Federal contracts.

Based on the determined methodology, four industries were identified where WOSBs were either underrepresented or substantially underrepresented:

- National Security and International Affairs;
- Coating, Engraving, Heat Treating, and Allied Activities;

- Household and Institutional Furniture and Kitchen Cabinet Manufacturing; and
- Other Motor Vehicle Dealers.

Constitutional Concerns

While the role of SBA is to aid, counsel and assist small businesses, it is not the role of the Agency to advise on questions of constitutional law. Therefore, SBA worked closely with the Department of Justice in drafting a proposed rule that is cognizant of the exacting constitutional requirements that apply in implementing a gender-specific set-aside. According to Supreme Court precedent, the Equal Protection Clause requires "skeptical scrutiny of official action denying rights or opportunities based on sex," and any gender-based preference program must be supported by an "exceedingly persuasive justification." *United States v. Virginia, 518 U.S. 515, 533 (1996)*. As applied to the Federal Government, the constitutional standards prohibit Federal agencies from discriminating on the basis of gender in awarding of Federal contracts unless the preference furthers important governmental objectives and the means employed are substantially related to the achievement of those objectives. *Id.* at 533.

The Department of Justice advised that in order to conform to these constitutional standards, simply finding underrepresentation generally will not suffice to sustain the set aside of contracts for WOSBs. Consequently, the soundest means of assuring constitutional compliance is for the procuring agency to determine that setting aside those contracts solely for WOSBs is substantially related to remedying gender discrimination in the relevant industry or contracting sector.

Summary of the Regulation

The proposed rule will assist WOSBs in procuring contracting opportunities with the Federal Government by providing procedures for certifying a business as an eligible WOSB, protesting eligibility determinations and awards, as well as providing a framework for agencies to make the determination that WOSB underrepresentation is related to gender discrimination. In addition, the rule sets forth when contractors can restrict competition to WOSBs.

Women's Procurement Goal

SBA's goal is not only to develop regulations implementing these procedures, but to help WOSBs so they can compete both in the private market place and for Federal contracts.

In analyzing the data found in the RAND study, we recognized that the real issue is that there are not enough WOSBs registered in CCR. As a result, we are analyzing what we have done in the past and what additional steps we can take to increase the number of WOSBs able to pursue Federal contracts.

In addition, SBA has been working with its resource partners to educate women entrepreneurs not only on how to contract with the Federal Government, but on how to establish and grow their businesses. Currently, SBA provides business counseling and events including business matchmaking and networking opportunities through SBA field offices located around the country and through SBA resource partners, including Small Business Development Centers (SBDCs), SCORE and Women Business Centers (WBCs), that counsel prospective business owners on elements necessary to start a business.

SBA is taking a forward-looking approach. First, our programs are tasked with growing the universe of WOSBs and encouraging these businesses to register with the CCR, thus making these businesses eligible to contract with the Federal Government. Second, the role of SBA is to help those businesses become ready, willing and able to undertake and build a successful track record working with the Federal Government.

These initiatives will help WOSBs to achieve the congressionally-established goal. We must remember that there is no single magical approach that will expand the participation of women-owned small businesses in Federal procurement; rather a combination of initiatives that take into account the individual needs of businesses is the best approach to provide opportunities for women small business owners to do business with the Federal Government.

The WOSB rule submitted by the SBA represents careful analysis which culminated in a proposed rule utilizing the most justifiable measures and methodology. SBA fully supports WOSBs and will take all necessary steps to implement this rule.

Lender Oversight

On November 13, 2007, I appeared before the Senate Small Business and Entrepreneurship Committee to discuss SBA's ongoing efforts in managing credit risk, monitoring lender performance and enforcing lending program requirements. I detailed to the Committee SBA's progress in putting measures in place to manage risk in loan programs while increasing access to business loans. SBA continues to consider ways to improve its oversight ability while maintaining an environment where lenders want to continue their participation in the program.

The Office of Inspector General (OIG) has made multiple recommendations to improve lender oversight. Many of those recommendations are directed to preventing fraud or excessively risky lending. As the OIG has noted, however, it is not always possible to prevent fraud or risky lending. The fact that it took OIG and the U.S. Secret Service agents over five years before arrests could be made against the individuals involved in the Business Loan Express (BLX) loan fraud scheme demonstrates that point. The OIG reports and recommendations have been valuable in pointing out some areas where SBA could improve oversight and SBA has taken concrete steps to make improvements that address many of the recommendations. While SBA continues to make programmatic improvements including progress on the IG's recommendations, any changes must be in accordance with applicable law and must consider the needs of the small business community. Such changes also must allow for the flexibility required in our oversight role. We continue to press for improvements and to work with the IG.

SBA continually updates its lender oversight procedures to adapt to an ever-changing business environment and Congressionally mandated program responsibilities. There are a number of steps we are taking right now that we expect will improve our oversight function:

- We have implemented a process for replacing our loan accounting system. This new system will contain more information on loans and lenders, that can be leveraged for oversight purposes. Recently we re-initiated the procurement process. This will facilitate a faster implementation of the system replacement.
- We issued proposed regulations that would clarify the lender oversight process and add a level of clarity to the Agency's oversight activities.
- We have implemented a training and staffing reengineering initiative at our Herndon and Sacramento processing centers that will improve their capacity and responsiveness.
- SBA is revamping the SBAExpress and Community Express procedures and their purchase and liquidation processes.

Mr. Chairman, Ranking Member Snowe, and Committee members, we are making progress in lender oversight while increasing access to small business loans in underserved communities. A recent study by the Urban Institute, a nonpartisan economic and social policy research organization, found that SBA backed loans are more effective than conventional loans in reaching minorities, women and start-ups and that SBA loans are a useful financing tool for creditworthy small businesses that do not meet conventional underwriting standards. SBA is pleased to have confirmation that we are providing credit solutions to this underserved population and has rolled out several initiatives to further increase participation in our lending programs so creditworthy entrepreneurs have access to capital. It is this access to capital that is so vital to our economy. We at SBA will continue to make progress in both reaching America's small businesses while managing program risk.

Thank you for the opportunity to testify today. I look forward to any questions that you may have.

Chairman KERRY. Thank you very much, Mr. Administrator. I appreciate it.

I think for somebody just tuning in, all this code stuff is probably pretty confusing and doesn't have a clue what you have just said, but I want to try to follow up on a little bit if we can here. First of all, it is accurate, is it not—let me ask Senator Levin, who just came in, if he has any opening comment that he wants to make.

Senator LEVIN. No, I will hold off. Thank you.

Chairman KERRY. All right. Thanks.

It is accurate, is it not, that there was an original study done by SBA with respect to underrepresentation of women businesses, correct?

Mr. PRESTON. Yes.

Chairman KERRY. And that original study that was done by SBA was then reviewed by NAS, the National Academy of Sciences?

Mr. PRESTON. That is correct.

Chairman KERRY. And the National Academy of Sciences in its review essentially found that the study by the SBA was inadequate.

Mr. PRESTON. Yes, two things. They found that our study was inadequate, and then they laid out a methodology under which a study would be adequate.

Chairman KERRY. And RAND came along in order to fill the void and provide the study that hopefully would be adequate, correct?

Mr. PRESTON. They took the NAS methodology and then they did the study, pulled the data and all the analysis.

Chairman KERRY. And in that methodology, what they did, what the RAND folks did was find that anywhere from 87 percent of industries to a range of zero percent, depending on what statistical model you used, would be underrepresented. If you used one statistical model, you could have 87 percent underrepresentation, is that correct?

Mr. PRESTON. They looked at a variety of methodologies. That is the correct range. They did not in any way imply that those methodologies would all be appropriate for consideration——

Chairman KERRY. I understand that. They did provide a range of statistical models——

Mr. PRESTON. Yes.

Chairman KERRY [continuing]. Which you could then adopt to say, wow, this is very reasonable. Let us use this——

Mr. PRESTON. Correct.

Chairman KERRY [continuing]. Correct?

Mr. PRESTON. Yes.

Chairman KERRY. And in May of last year, I wrote you urging you to choose the statistical model that would create the broadest possible program, correct?

Mr. PRESTON. Yes.

Chairman KERRY. And on October 17 of last year, Senator Snowe joined me and we wrote a letter to you urging you to implement the broadest possible program. You chose the narrowest possible. Help us understand that. Why would you not want to at least fall mid-way or as close as you could to meeting what we feel was the intent of Congress, which is try to broaden this?

Five percent is not a ceiling, it is a floor. It could be much higher. And when you start looking through the range of these codes, which I will go into in a minute, it is incomprehensible to me that you can find areas—that you can't find underrepresentation in those areas, that you wouldn't want to say, wow, let us get some women-owned firms into more procurement in food manufacturing or in—you know, I can run through the list. Why would you not?

Mr. PRESTON. Well, I think because the approach we took was to look at the methodology that we thought was most appropriate given the issues we were considering, to advance the policy to fulfill the legislation as well as fulfill constitutional issues that we thought may be an issue——

Chairman KERRY. Well, before we get to constitutional issues, you will acknowledge it was your discretion as to which statistical model you choose, correct?

Mr. PRESTON. I would acknowledge that it was our discretion to determine the statistical method, understanding, however, that we wanted to choose the most defensible method, given what we were trying to achieve.

Chairman KERRY. Well, you are here to defend it. We want to understand why a broader, or if not the broadest statistical model which RAND offered you would not meet the goal of the intent of Congress to try to broaden the participation of women-owned businesses Federal procurement, the $6 billion at minimum that could be spread out among women-owned businesses.

Mr. PRESTON. Yes. Let me make a couple of points. First of all, let me highlight that we are in a rulemaking process right now and we are in the public comment period, so obviously we are looking at all the comments and—to ensure that we understand that people concur—dispute with these methodologies and the basis upon which that occurs.

I think there are two fundamental concepts to understand, because to get away from codes and all the confusion, there are two fundamental concepts to understand. Number one, do you do an analysis based on the dollars going to women-owned small businesses or based on the numbers of contracts?

Chairman KERRY. Let me just stop you right there for a minute.

Mr. PRESTON. Okay.

Chairman KERRY. If you do dollars, you can take a pack of dollars and give it to one person, leaving out a whole bunch of other people who could also be procuring, and then you measure dollars and you say, wow, aren't we doing great because we just gave a $3 million contract here? But you could be giving maybe 10 or 15 or 20 additional smaller contracts. Do you follow us?

Mr. PRESTON. I think when you look at the numbers of firms in Federal contracting, you are less likely to find that, but——

Chairman KERRY. Sixty-three-thousand.

Mr. PRESTON. Well, let me draw the other analogy——

Chairman KERRY. There are 63,000, Mr. Administrator.

Mr. PRESTON. Okay. Let me——

Chairman KERRY. Senator Snowe has pointed out there are only about 1,200 that are getting helped here.

Mr. PRESTON. Okay, but if you use numbers of contracts, I can make a couple of analogies, I think, that would be appropriate here. First of all, if you are looking at a $1 million firm and a $10 billion firm, they are considered equal, so if the $1 million firm gets a $500,000 contract from the Federal Government and the large firm gets a $500,000 contract from the Federal Government, they are considered at parity now. If the very large firm gets two $500,000 contracts with the Federal Government, which is a minuscule percentage of their base, it doesn't take into consideration capacity to perform, Okay, the small firm is considered underrepresented even though 50 percent of their revenues are coming from the Federal Government.

Using numbers doesn't right size the business that they are getting to the size of the company. You can have a $5 million company that has five $1 million contracts, gets 100 percent of their revenue from the Federal Government. You could have GE getting ten $1 million contracts. It is inconsequential to them.

Chairman KERRY. I agree with you. I mean, I am not arguing about that. You are the one who suggested that the dollar amount——

Mr. PRESTON. What I am telling you, those ten contracts going to GE and the five contracts going to the small business would result in that small business being considered underrepresented, even though 100 percent of their business is coming from the government. So what this methodology does is it says what percentage of the revenues are these firms getting from the Federal Government relative to the private sector, and the analysis shows that women-owned businesses in most of these categories get a higher percentage of their revenue from the Federal Government than non-women-owned small businesses.

Chairman KERRY. Well, that may be, but that is not a measurement of whether or not they are capable of getting the procurement level that we set as a target or of even growing into their ability to get a larger percentage of the private sector——

Mr. PRESTON. I agree 100 percent.

Chairman KERRY. This is the whole point.

Mr. PRESTON. It is a measure of underrepresentation, and the legislation, the statute and then bolstered by constitutional precedent, which I unfortunately am not going to be able to wax eloquent on, and I would be happy to follow up with questions for the record or bringing other colleagues before you, requires us to show underrepresentation as a basis for setting up a preference program, and that is the reason that we had to do it that way.

Now, the dollar value—so the dollar value allows us to look at companies based on their capacity to perform. It gives us a measure that is based on something that confers value to them. You could have ten $100 contracts or ten $1 million contracts. Those would be considered equal if you had a numerical measure. So there are a lot of flaws with the numerical measure and that is——

Chairman KERRY. I agree. There are sometimes some flaws, which is why the instinct ought to be not to be arbitrary. The instinct ought to be to exercise discretion in a way that tries to meet a public policy standard, if you will. I mean, speaking as a lawyer, and I know Senator Levin is a lawyer, on the constitutional issue, and so the bar you have to get over with respect to the measurement of an underrepresentation to qualify you legitimately for a preference is pretty hard when you have a range of 87 percent to zero, and when you look at just the raw statistics of 1,200 versus 63,000 to, under any reasonable test standard believe you are arriving at a place that is comfortable. I mean, does your gut tell you you are comfortable with that?

Mr. PRESTON. My gut——

Chairman KERRY. You designed the study. Does your gut say this is the right level——

Mr. PRESTON. My gut tells me we should be working to bring more women-owned businesses into the contracting registry because once——

Chairman KERRY. Why wouldn't you create a rule that helps to do that when you have a statistical basis given you by RAND on which you could do that?

Mr. PRESTON. Because, Senator, the rule—the statute requires us to go out and base our decision on underrepresentation in Federal contracting.

Chairman KERRY. Well, I understand that, but let me—I mean, you are running through the list here. I mean, you have got tobacco manufacturing; fiber, yarn, and thread mills; fabric mills. I mean, you have got subcategories in every single one of these—textile furnishing, cut and sewing apparel manufacturing. I can take you down in New Bedford and Fall River and show you some folks who are underrepresented in that, not to mention, I am sure, in Portland and in some other places. You have men's and boys' cut and sew trousers, men's and boys' cut and sew work clothing manufacturers, men's and girls' dress manufacturing. These are all areas where you say they are not underrepresented. I just find that stunning on its face.

Mr. PRESTON. Well——

Chairman KERRY. I can run through a lot of others. I mean——

Mr. PRESTON. Certainly, we would be happy to have—ask the RAND people——

Chairman KERRY. Printing, commercial lithographic printing——

Mr. PRESTON [continuing]. Who did the analysis to come and talk with you——

Chairman KERRY [continuing]. Digital printing. I mean, you can run down—pharmaceutical, small electrical appliance. I mean, wood kitchen cabinets. This is the one area, kitchen cabinetry, you found them unrepresented. I——

Mr. PRESTON. Well, let me just make——

Chairman KERRY. How about mattress manufacturing? You got a sense of that?

Mr. PRESTON. I don't think that one is in there, but——

[Laughter.]

Chairman KERRY. Well, it is in here.

Mr. PRESTON. If you would like to follow up on it——

Chairman KERRY. It is a category.

Mr. PRESTON. If it is a category, then——

Chairman KERRY. It is a category which you found.

Mr. PRESTON. If it is a category, it has an underrepresentation figure based on the mathematical analysis. But I think it is important for us to understand that, you know, and I said in the opening we were surprised when we saw the results, too. But I will also say we didn't go in there saying, What is the number we want at the end of the day? We went in there and said, What is the methodology we need to choose to align it with what the statute is asking us to do and to make it consistent with the fact that we are trying to help women-owned businesses get contracting dollars? And so it was based on trying to get that alignment in place and try to have a defensible methodology that will result in a sustainable program.

Chairman KERRY. Well, here is the problem. We have an awful lot of women-owned businesses that we are in touch with who come across the transom here who claim underrepresentation and they are not getting their fair share. So on its face, you have got a problem here in terms of this rulemaking period for public comment. Here is some public comment right here on this committee, part of the record, and we will submit it as part of the record, that we don't think that this statistical method chosen adequately addresses the intent of Congress or provides the ability to meet the goal.

And you do have a number that you were supposed to go in there with. It is 5 percent. That is the number. It is statutory. It is the law of the land, at 5 percent——

Mr. PRESTON. Five percent is——

Chairman KERRY [continuing]. And you are at 3.41, so you have got to go in there and find the statistical analysis, and you were given an 87 percent underrepresented capacity——

Mr. PRESTON. Well, you know——

Chairman KERRY [continuing]. Which meant you could have met the 5 percent.

Mr. PRESTON. I just have to say, and I think you all probably understand this better than I do, when you are dealing with issues like this, having the right foundation to have a rule that is sustainable, that aligns with what you are trying to achieve——

Chairman KERRY. Let me go back for a minute. Did RAND or did RAND not give you a range of 87 percent underrepresentation down to zero?

Mr. PRESTON. RAND gave us a variety of methodologies that——

Chairman KERRY. Did they not give you——

Mr. PRESTON. They did not imply, or they did not support——

Chairman KERRY [continuing]. Which to take, but they gave you the range.

Mr. PRESTON. They also said specifically—but let me just mention something. They said specifically in the study that they did not opine on whether or not all these methodologies were appropriate for any type of policy.

The other thing is, the NAS study, which was really the foundation we needed to use because the NAS is the one that threw out the original study that the SBA did, said two things. They strongly supported using dollar numbers because that is how value is conveyed and that is what is aligned with the goal, and they strongly supported using industry information that was detailed enough to look into smaller industry segments.

Chairman KERRY. The dollar numbers were——

Mr. PRESTON. And those are the two things we——

Chairman KERRY [continuing]. You don't know how many people are available, how many people are in a particular sector, how many available companies are there. If there are 63,000 registered, have you done a break-down of those 63,000? Do you know how many fit into which category in those 63,000? If you can't take——

Mr. PRESTON. Yes.

Chairman KERRY. You do?

Mr. PRESTON. We do. It is all part of the study, yes.

Chairman KERRY. Well, you ought to be able to tell, it seems to me, whether or not they are getting, on that basis, a share of a combination of sort of numbers of contracts and amounts of money. Anyway, let me cede to Senator Snowe. She is going to probably follow up on the same thing, I assume.

Senator SNOWE. Correct assumption. Mr. Administrator, so the RAND report made no policy recommendation with respect to the methodology. They looked at 28 measurements, 14 in contract dollars, 14 in the number of contracts, correct?

Mr. PRESTON. Yes. RAND basically took all this stuff, plugged it into their models, and didn't make any value judgments on what was right or wrong.

Senator SNOWE. Okay, but out of the 14 contract dollars that the SBA chose to focus on, it eliminated four measurements, as I understand it, that found the highest level of underrepresentation.

Mr. PRESTON. Yes. Let me——

Senator SNOWE. And those four found that women contracting was underrepresented between 27 to 55 percent. So why would you have eliminated those four measurements in that category?

Mr. PRESTON. Okay, so that is the other piece of the puzzle. We talked about dollars versus numbers, and we can go back some more if you want, but the other piece—there are basically two concepts—the other piece is do you look at all companies in America or do you look at companies that are signed up to do contracting with the Federal Government, okay? So that is the other piece.

When you look at the data on companies across the industry, we cannot get women-owned small businesses to any degree of detail in the industry codes. Women-owned small and large businesses are combined. The data is old. And we used that data in our first study that was thrown out and the NAS said that it was difficult to substantiate that those businesses were ready, willing, and able since they weren't even signed up to do contracting.

The other piece of data we had is the Federal Contracting Registry, so they clearly qualify as willing and able and we are assuming readiness. We were able to get detailed industry information. Let me pause on that for a second. If you look at the national data, it would say all retailers, okay. If you look at the detailed data, you could break out auto dealerships, apparel, jewelry stores, grocery stores. If you don't get to that level of specificity in your analysis, you are comparing auto dealerships with grocery stores. So you had to look at representation in those more detailed categories. Those detailed categories were not available in any of the other measures that you are citing.

Senator SNOWE. So we are down to four categories, really only three if I understand it, because the national security-international affairs has no women-owned business. So really, you are down to three categories.

Mr. PRESTON. Right.

Senator SNOWE. Is that correct?

Mr. PRESTON. Yes.

Senator SNOWE. Okay. So we are down to coating and engraving, heat treating and allied activities; household institutional furniture; kitchen cabinet manufacturing; and other motor vehicle dealers, and that is it.

Mr. PRESTON. That is right.

Senator SNOWE. I think you have just gone to the lowest common denominator and it is one thing to choose contract dollars, it is quite another to break it down into these very narrow subsectors of an industry rather than using broader categories.

Mr. PRESTON. That was——

Senator SNOWE. And you talk about the National Academy of Sciences, they cited their sources, the same information. So what we are talking about is a de minimis level here——

Mr. PRESTON. Right.

Senator SNOWE [continuing]. When it comes to helping women out. Ninety-nine percent of all women-owned businesses are small.

Mr. PRESTON. Yes.

Senator SNOWE. So that is where we are at. So really, when you are talking about four categories, we are now down to three because one doesn't have any private firms—and can't have any, if I understand it, according to the law——

Mr. PRESTON. Yes, I——

Senator SNOWE. National security and international can't be a private sector organization.

Mr. PRESTON. Right. No, I understand what you are saying, and I think when we look at the two pieces, the two factors that we considered with getting detailed information, looking at dollar information, I just want to remind you, these were strong recommendations that came to us from the National Academy of Sciences. I will also concede——

Senator SNOWE. They didn't dictate it, though.

Mr. PRESTON. They didn't dictate it.

Senator SNOWE. The SBA chose—you chose these——

Mr. PRESTON. We chose the approach based on the strong recommendations.

Senator SNOWE. And of the 14 options, you eliminated 4 measurements, is that correct, that had the highest underrepresentation of women. It ranged from 27 to 55 percent. So you even eliminated measurements under the options of contract dollars of 14 measurements.

Mr. PRESTON. The contract dollar measurements that you talk about are ones that included very, very broad industries, and it gets to this issue that I mentioned before where you would be mixing IT contractors with lawyers. It just—it didn't provide the level of specificity for us to understand where representation truly occurs, and it is at that level of specificity that Federal contracts take place.

Senator SNOWE. Well, you dissected it to the lowest common denominator in order to reach the goal. You just cut up the sectors in order to achieve that goal. This is what has happened. We have been driving this for 7 years. It is ludicrous. I don't even think the public could believe that it would be 7 years trying to have something implemented, and it is especially frustrating to reach this point and you get a de minimis, the lowest common denominator standard, by choosing the lowest possible result that ultimately is going to affect women. Women-owned businesses is the fastest-growing segment of our economy.

Mr. PRESTON. It is——

Senator SNOWE. Yes.

Mr. PRESTON. But Senator, I also want to highlight it is the fastest-growing sector of Federal contracting and women-owned small businesses are growing faster than any of the set-aside categories.

Senator SNOWE. Well, given the rate in which we are achieving the 5 percent goal, it will take until 2019 to get 5 percent, according to our calculations, at the rate at which we are going. In Fiscal Year 2006, the SBA is one of only a few agencies that achieved the 5 percent goal. Even the Department of Defense with hundreds of billions of dollars, over $20 billion did not achieve the goal. We have been in the low single digits, only recently achieved 3.4 percent of women-owned businesses accessing Federal contracts. So we have a long ways to go and I don't see this rule galvanizing this process to achieve the ultimate 5 percent goal. It should have been long ago achieved——

Mr. PRESTON. I can't argue with that.

Senator SNOWE. It is going to take 11 years to get to 5 percent at this rate.

Mr. PRESTON. I think we can get there faster than that——

Senator SNOWE. I hope so.

Mr. PRESTON. I would love to work with you——

Senator SNOWE. We should have been there yesterday, though. That was the point. This is 7 years since this law was passed——

Mr. PRESTON. I understand——

Senator SNOWE [continuing]. Anybody—you wouldn't be that patient in the private sector, would you, for results? Nor should we in the public sector.

Mr. PRESTON. I hope you know I wouldn't be that patient in the public sector, either, given what we are doing, but——

Senator SNOWE. We wouldn't wait 7 years to achieve a result. We have to achieve a bottom line. It is no different in the public sector. We all should be aggressively pursuing the bottom line here, because ultimately it means fairness and equity, which is the essence of the Small Business Act of 1953, it was to make sure that there was a fair proportion——

Mr. PRESTON. Yes——

Senator SNOWE [continuing]. And now it is access to Federal contracts and doing business with the Federal Government. This is not equitable and it certainly isn't fair.

Mr. PRESTON. Well, we are—I think our outreach efforts, I think our education efforts are effective. I think we are driving this number forward without the set-aside. I do totally agree with you that this is not going to be a significant measurement of the needle. It is not affecting enough industries or businesses. But I think we are showing good progress and I think the SBA is leading by example. This year, we are going to show 25 percent of our revenue from——

Senator SNOWE. We have all the Federal agencies, and that is where the SBA plays a vital role, as you well know. And I realize these weren't all of your problems. You inherited many. But the question is now, you are in a position to be able to do something about it here and now.

Mr. PRESTON. Let me——

Senator SNOWE. Well, certainly we can start with this rule that is 7 years old. There is no reason to pursue the path that you are recommending in the rulemaking process. So I just hope that we can find a different path in this process and submitting our comments and recommendations to change it so that we can significantly modify this approach to more broadly represent women-owned businesses. It ultimately means jobs and it means fairness. Women-owned businesses ought to access Federal contracts. That is what it is all about, because we are now down to three categories. That is just astonishing.

Mr. PRESTON. Right——

Senator SNOWE. That is not fairness.

Mr. PRESTON. Although I just want to pause for a second, because the language that you are using, I feel compelled to make a point, which is I think women-owned small businesses do compete effectively today based on the results we saw. This is about giving them a preference program, and the reason we have to do all this detailed work is when you do have a preference program, you have to be able to justify how you determine the underrepresentation and look at all sorts of precedents and make sure that it withstands scrutiny, because the last thing you want is for a program like this to be overturned.

Senator SNOWE. I just don't see why you couldn't have chosen other options using all the 14 measurements. It was highly selective. We have had 50 procuring Federal agencies that failed to meet the standards, 50 agencies, including the Department of Defense, that has more than $234 billion of procurement dollars and we can't meet a goal of 5 percent. That is a principle that was enshrined in law, that we wanted a 5-percent standard for women-owned small businesses, and rightfully so, and we have got 50 agencies that have failed to meet that challenge. It has been 7 years.

Mr. PRESTON. Right.

Senator SNOWE. So you can understand the frustration, and there was another path to take that could have withstood constitutional scrutiny and public accountability. So I just hope that we can find a way to do it differently in the days ahead.

Mr. PRESTON. Okay.

Senator SNOWE. Thank you, Mr. Chairman.

Chairman KERRY. Thank you very much, Senator Snowe.

Senator Levin.

Senator LEVIN. I want to get back to the discretion question. Is it clear from your testimony, as I understand it, that you could have selected categories that showed underrepresentation in terms of dollars, which would have led to a greater number of categories? Is that correct? You could have?

Mr. PRESTON. Not if we followed the advice of the research group that laid out the pathway to do the study.

Senator LEVIN. In other words, the only way that you could achieve a larger representation in terms of dollars was to pick these narrow categories? The other ways would not have led to a greater representation in terms of dollars? Is that what you are saying?

Mr. PRESTON. What I am saying is if we had looked at data, okay, that looked at all women-owned businesses in the economy, looked at very broad industry categories, all retailers, all service providers, very broad, data that was 5 years old and data that commingled women-owned small business with women-owned large businesses, all of which was against the advice of the NAS, we would have found more categories.

Senator LEVIN. That is not my question. Could you have adopted a larger number of categories which still would have shown underrepresentation of women in terms of dollars?

Mr. PRESTON. No.

Senator LEVIN. This is it? You are saying there are only three categories——

Mr. PRESTON. Right.

Senator LEVIN [continuing]. That show underrepresentation of women in terms of the amount of dollars?

Mr. PRESTON. That is correct. That is what the study shows.

Senator LEVIN. And there is not——

Mr. PRESTON. I want to highlight two things——

Senator LEVIN. That is not the way I read these. I mean, that, to me, is the key issue. You are saying there is no other way you legally could have done it. On the other hand, when the Chairman asked you the question, you said you had discretion.

Mr. PRESTON. We had discretion. We had the discretion to choose. If we had chosen differently, we would——

Senator LEVIN. No, you had the discretion to choose legally. I mean, the question isn't whether you had discretion to do something illegal. The question is whether or not you had discretion to do something. Discretion means legally to act in a way which would have raised the number of categories which would have added dollars in terms of contracts for women.

Mr. PRESTON. We had the discretion to choose the methodology. The methodology we chose was based on factors that were laid out by the National Academy of Sciences.

Senator LEVIN. I understand. Was that the only one you could have chosen?

Mr. PRESTON. Theoretically, we could have done anything, but its defensibility is something that would have been up for grabs, potentially.

Senator LEVIN. Is it a matter that the others that you could have chosen would not have been defensible, or would have in your judgment been less defensible?

Mr. PRESTON. I think the latter. They would have been less defensible.

Senator LEVIN. So it is not the only ones you could have chosen——

Mr. PRESTON. But——

Senator LEVIN [continuing]. It is the one which, in your judgment, was the most defensible?

Mr. PRESTON. Right, and I think——

Senator LEVIN. It is not the only one which was defensible.

Mr. PRESTON. Yes, and I think——

Senator LEVIN. Wait, wait, wait. One at a time. Is that correct?

Mr. PRESTON. That is correct, and I think—and I appreciate the distinction you are making because what I do not want anybody to think is that we looked at the numbers we got at the end of the day and then decide the methodology based on the number. We were surprised by the number. But as we vetted this within our agency and throughout other people who are experts in this area, this is where we landed.

Senator LEVIN. No, I understand your conclusion. It is now a lot clearer in my mind that there are other categories that you could have chosen that were——

Mr. PRESTON. Other methodologies.

Senator LEVIN [continuing]. Other methodologies which would have led to defensible—you said less defensible or more defensible. They still would have been defensible, but in your judgment, less defensible.

Mr. PRESTON. Defensibility doesn't imply that at the end of the day you win the argument. The defensibility—if we are putting in place a law, a program, rather, we want to make sure it withstands scrutiny.

Senator LEVIN. Of course. Look, you can have ten different options, all of which are defensible. Number one is the most defensible, but numbers two through ten are also defensible, but not as defensible in someone's judgment as number one.

Mr. PRESTON. Right.

Senator LEVIN. But they are still defensible, but two through ten would lead to a much better result in terms of policy. That is where it seems to me you have failed——

Mr. PRESTON. Right.

Senator LEVIN [continuing]. It seems clear to me that those other approaches are legally defensible, even though you can argue less defensible, they are nonetheless——

Mr. PRESTON. Right.

Senator LEVIN [continuing]. Defensible legally, but you chose one which you thought was the most defensible technically, but from a policy perspective doesn't achieve the results which we clearly intended. That is what troubles me a great deal.

Mr. PRESTON. Right. There are two things I would mention that I am sure you appreciate the degree to which these types of programs have come under attack, legal attack. There has been all sorts of—I am sure you all understand this better than I do, since you have been in this world much longer than I.

So Number one, I think we view it as being very important to look at those factors and make sure that what we have out there does not come under—is not weak in the face of attack.

Number two, once again, we looked at the strong advice on two factors that we got by the research academy that laid the pathway for how this should happen and we took those two pieces of advice and we followed them.

Senator LEVIN. Let me just move on to another question. I will take two more minutes, because I think I understand what you did and I disagree with it. You can have ten different approaches that are defensible legally, one of which is the most bulletproof, the next one is the second most bulletproof, and so forth. If you take the fourth or fifth or sixth most bulletproof one—it is not the most, but it is the best in terms of policy, and you have a darn good chance of defending it legally from a policy perspective, it is worth doing, and that is, at least from my one perspective——

Mr. PRESTON. I understand.

Senator LEVIN [continuing]. The mistake that I think you have made. And I have been in that situation many times, by the way, as a lawyer, where the goal was we have got to achieve a policy and the question was do we do it this way, this way, or this way, and the decision would be it is so important that we achieve the policy, we will take a 5 percent risk on legality to achieve a 50 percent gain on policy. That is where, from my understanding, you have made, I think, a mistake. It may be different from the understanding of others on the Committee, but that is the way I frame it in my mind.

It is much too narrow. It is needlessly so in the quest of gaining the most technically, theoretically bulletproof legal approach, but you have lost so much in terms of the policy gain that you have taken an approach which seems to me to be the wrong one in terms of the policy of the law.

Real quickly on Women's Business Centers——

Mr. PRESTON. Yes.

Senator LEVIN. You have now resolved some of the uncertainty about the future funding of these business centers. You have replaced a sustainability pilot program with a 3-year renewal grant program which is more permanent. I applaud you for that and I just would urge that you implement this program as soon as possible and I am wondering if you can tell us what the time table is for that.

Mr. PRESTON. It would be—the submissions for the Women's Business Centers came in, I believe, last week. That was completed. By the end of the month, they will know whether or not they are getting grants, and shortly after that, they will begin getting their grant money.

The other issue which I should report, which you didn't bring up but it is related, is historically these Women's Business Centers have gone through a very difficult and arduous process to get their grant money, resulting in delays, and you know these centers, they need their money when they need their money. So we have rolled out a new program where they will be getting their money very quickly upon submitting the grant request and we will be doing—it is much more responsive, much more sensitive to their needs and certainly has been received very happily by the community.

Senator LEVIN. Thank you. I do very much support that program and I applaud you for the steps that you have taken in that area.

Mr. PRESTON. Thank you.

Senator LEVIN. Thank you, Mr. Chairman.

Chairman KERRY. Thank you very much, Senator Levin. Thank you for helping to clarify that, as usual, capably, and we appreciate it.

Following up on that just a little bit, Mr. Administrator, and we do have some other questions in a couple of areas, but I am reading from the RAND study. Here is what it says. We found that the measurement of whether women-owned small businesses are underrepresented in Federal contracting is sensitive to whether contract awards are measured in dollars or in number of awards, and to whether the population of ready, willing, and able firms comprises essentially all employer firms or just those firms that have registered as potentially bidders on Federal contracts. So right up front, they acknowledge the sort of universe issues here, which if you wanted to, I mean, you could say, okay, let us look at this in a way that is going to accomplish the public policy goal. But let me go further.

Depending on the measure used, underrepresentation of women-owned small business in government contracting occurs either in no industries or in up to 87 percent of industries. Then most importantly, it said, this variation is especially large in the measures that use contract dollars rather than number of contracts. The most important sentence, this report does not advocate a particular measure.

Mr. PRESTON. No, that report didn't——

Chairman KERRY. Rather, it highlights industries where the disparities occur.

Mr. PRESTON. Right. That is exactly right.

Chairman KERRY. So, you know, again——

Mr. PRESTON. The NAS laid out the recommendations——

Chairman KERRY. No, NAS—but this study was done because NAS made a judgment of the original study, but it wasn't the gospel with respect to how we proceed forward on this. The RAND study was the study that was supposed to say, what does the underrepresentation look like?

Mr. PRESTON. The RAND study made no judgments on methodology. They simply——

Chairman KERRY. Correct.

Mr. PRESTON [continuing]. NAS recommendations.

Chairman KERRY. That is exactly where I started at the beginning of this hearing——

Mr. PRESTON. Right.

Chairman KERRY [continuing]. And that is the main point here——

Mr. PRESTON. What I——

Chairman KERRY. They did make no recommendation. They left to your judgment, to your discretion how you would implement the policy that the U.S. Congress had put into law. Now, that is what is at stake here. Let me read you—this is fairly simple stuff when you really get at it, I think. Other categories—these are other categories—this is under the RAND study. Other categories where women are considered underrepresented had SBA used the broader numbers in the RAND study, which was your discretion.

Let me just give you a sense of it: water, sewage and other systems; residential building construction; utility system construction; foundation, structure, building exterior; building equipment contractors; building finishing contractors; other specialty trade contractors; other textile product mills; cotton sew apparel manufacturing, which I went through earlier; converted paper product manufacturing; printing and related support activities; other chemical products; forging and stamping; architectural and structural metals; oil tanker shipping containers; coding, engraving, and heat treating; other fabricated metal products; commercial and service industry machining; communications equipment manufacturing; navigational measurement; electro-medical; manufacturing and reproducing magnetic media; electrical equipment manufacturing.

I mean, I can go on and on. There are 105 different business areas: business support services; facility support services; administrative services; waste treatment and disposal; technical and trade schools; educational; beer, wine, distilled alcoholic beverages; warehousing and storage; software publishers; data processing. Run the list——

Mr. PRESTON. Right.

Chairman KERRY [continuing]. Where there are, according to the study, available discrepancies of underrepresentation of women in procurement. You could have embraced these.

Mr. PRESTON. Okay. I guess the way I think of it, Senator, is the NAS was sort of the engineer. They laid out the plan. RAND was sort of the assembly line, okay. The NAS, in looking at this, specifically says—I am quoting here—that the two-digit codes appear to be too broad to be used as a basis of disparity ratios to inform an understanding of the role of women-owned small business in Federal contracting and what kind of preferential treatment may be indicated. Specifically, this was the group that basically threw out our old study and said, this is what you need to look at and this is why we have relied heavily on their guidance.

Chairman KERRY. Well, again, I think you are getting a sense here, as I wrote to you in the letter, as I have written—you haven't gotten it yet, but——

Mr. PRESTON. No, and I think Senator Levin's point is very important, which is what is sort of the balance between the policy goals——

Chairman KERRY. Right, but let me build on that because there is a legal standard here and you are trying to assert that you thought it was the most legally justifiable and both of us disagree, or all three of us disagree.

Mr. PRESTON. I think also closest to the heart of the matter, closest to understanding what we are actually——

Chairman KERRY. What you seem to be applying is what in the law is called a strict scrutiny level of view to a gender-based program, and the Supreme Court has held in 1976 that gender-based programs are subject to intermediate scrutiny standards, meaning that to justify the program, the government only needs to prove an important governmental interest and that a program is substantially related to the achievement of that purpose. That is the standard. And under that standard, Mr. Preston, you know, it just is incomprehensible that you would go to the sort of most defensible standard to the lowest common denominator here, as Senator Snowe has called it.

Mr. PRESTON. Well——

Chairman KERRY. So I think we have made our point. I think that if you want to respond, I am happy to have your response——

Mr. PRESTON. My understanding is that the standard that was applied was intermediate scrutiny. I know strict scrutiny is referred to in the RAND study, but I believe they are referencing a racially based program, which is a different standard, and I think—so our understand—my understanding——

Chairman KERRY. It does not require the standard of race-based programs which is laid out in city of Richmond——

Mr. PRESTON. That is right——

Chairman KERRY. Boren, that is a different standard, and the Adarand decisions——

Mr. PRESTON. Exactly——

Chairman KERRY [continuing]. It does not apply here.

Mr. PRESTON. Right. What I am saying is even though RAND mentioned that strict scrutiny, the standard we applied was intermediate scrutiny. I will have to rely upon my legal colleagues to get into this in more depth, if you want to at some point. But my understanding was that the issues that need to be addressed between strict and intermediate are the same issues. It is a matter of degree rather than what needs to be considered. And I think, Senator, that deals more with the issue of discrimination rather than what we are talking about in the RAND study.

Chairman KERRY. Well, under either way, Mr. Administrator, it seems clear to us that you ought to be able to go back to the drawing board here and broaden this. I mean, there are women sitting behind you right here in this audience who are owners of some of these kinds of businesses. There is a woman by the name of Norma Byron here who is owner of the Ashlawn Group. She is one of the only, if not the only woman munitions developer in the country. She could be selling. Magdalah Silva is here today. She owns an IT company, and she testified before this committee previously on the difficulties that she has in the Federal contracting area getting a fair share. We have a supply chain consultant here, Jennifer Sully, who is fighting for these opportunities, and under your rule, they don't get a shot.

Mr. PRESTON. Well, I think they have a shot. We are talking about a preference program. We are not talking about blocking them or not letting them compete on the same basis with other——

Chairman KERRY. Well, when I say shot, I am talking about——

Mr. PRESTON. But you know, the reason that concerns me is when you look at the reports in the media, when you look at the statements that are coming out of some of your colleagues, it is being implied that somehow, we are erecting a barrier that doesn't exist today. I think it is very important for us to understand that because it is a preference program, we have standards that we have to hit. And I understand——

Chairman KERRY. Erecting a barrier that doesn't—well, in a sense you are——

Mr. PRESTON. We are not——

Chairman KERRY [continuing]. And I will tell you how, because you could have chosen a different road. You are erecting your standard of interpretation of the law, which is not necessary here. So in a sense, you are erecting a barrier. But in another sense, what you are also doing is not, giving the opportunity, of taking down a barrier——

Mr. PRESTON. I think——

Chairman KERRY [continuing]. And that is the really big difference here.

Mr. PRESTON [continuing]. That if we all believe that there is broad-based discrimination that is resulting in barriers, then we are in a whole different playing field and that is certainly not something that we addressed in our study, but——

Chairman KERRY. Women-based preference is not based solely on the discrimination. It is based on the valid government purpose articulated in the law of wanting to broaden, because of the numbers of women who own businesses, their participation in fair share. I guess the Senator from Maine said it, a fair, equitable share. That is a government purpose, defensible under almost any standard. And so the whole purpose here is to try to broaden that.

Mr. PRESTON. And what I would tell you, Senator——

Chairman KERRY. This is such a home run missed kind of deal where you guys could just embrace and say, wow, what a productive thing. We are going to be the administration that makes certain that we have opened up more opportunity and we are going to get more procurement——

Mr. PRESTON. Well, I think where it comes to expanded outreach, where it comes to holding Federal agencies accountable, they all have women-owned procurement goals. We have rolled out IT tools to help them find women-owned businesses more easily than they ever have before. When it comes to this agency putting an effort behind reaching out and making connections with people, working with our Federal procuring partners to drive this number forward, we are doing a tremendous amount. I think when it comes into designing a preference program, we are in a different realm, and that is why I think we have some of the challenges we do here.

Chairman KERRY. Well, let me ask you this so we can wrap this part of it up anyway, and I will turn to Senator Snowe and see if she has any more questions on that part of it. But are you prepared to engage in a dialog with us and open this up to hopefully some kind of more sensible, mutually agreed upon rule that might——

Mr. PRESTON. Yes. We are in the middle of a public comment period right now, we will be looking very hard at all the comments we get. To the extent that comments address the NAS methodology as applied by RAND, I think it will be important for us to understand the substance behind why a different methodology is better. To the extent that they address the legality issues or the constitutional issues, which you and the Senator alluded to earlier, it will be important for us to understand the precedents that those arguments are based in, but we will be looking at those very carefully and open-mindedly.

Chairman KERRY. Senator Snowe, did you want to pursue that further?

Senator SNOWE. I think we have obviously explored this issue extensively, and certainly Mr. Administrator, you recognize disappointment with the direction the SBA has taken in this regard. With no question, when we are trying to open up pathways for women-owned small businesses to access Federal contracts and there are other ways, and just looking at the list here, in terms of the one down here, but there are many other ways in which to accomplish that and using contract dollars with industries that show a high percentage of underrepresentation of women ownership.

So I hope we can work together on this. This is something that has to be rectified. It has been part of the Small Business Act and removing these barriers, these discriminatory barriers, and to only achieve a result of 2 percent of all women-owned small businesses simply isn't realistic—it certainly is not fair. There is another way. So I am hoping that we can work together to figure this one out, because this isn't where we should be today.

We should be exploring a pathway that we can make sure that women who are participating as small business owners have the right to access Federal contracts. We have set a goal. It has not been accomplished. The law hasn't been implemented in 7 years, and we have got 50 agencies that have failed to even achieve the 5 percent, with hundreds and hundreds of billions of dollars worth of Federal contracts and women cannot participate. It simply isn't fair and it is not equitable and it could have been done differently.

So I am hoping that we can work together to forge that relationship. It is going to be essential in the days ahead, and certainly I will work with the Chairman in that regard, as well.

Chairman KERRY. Thank you, Senator Snowe.

Mr. Administrator, let me run into a couple of other areas, if we can. As I had mentioned earlier, I think people are excited about the progress on the Women's Business Centers Program. Can you just share with us, though, on the contracted out grants disbursement process to the Department of Health and Human Services, which I know was geared to try to prevent some of the problems that had existed, can you just share with us the thinking behind the outsourcing on that?

Mr. PRESTON. Yes. A lot of other agencies outsource to HHS. They have a very sophisticated, very responsive operation in place. They, Senator, will primarily be doing the processing of the requests for dollars. So we will continue to do the paperwork behind that. The difference is, historically, these Women's Business Centers had to provide us with all their paperwork ahead of time. We would review it, we would go back and forth, and they would have to go through the entire process before they got any money. We——

Chairman KERRY. How are the Women's Business Centers going to get paid under this process?

Mr. PRESTON. They get paid—once they are eligible for a grant, once they know, they will be able to submit the request to HHS. HHS will pay them quickly and then on the back end we will do a reconciliation of the paperwork. So they won't have to get——

Chairman KERRY. Is there an interruption at all in that process——

Mr. PRESTON. No——

Chairman KERRY [continuing]. Before they take it over——

Mr. PRESTON [continuing]. No, that is going to be—no, in fact, right after——

Chairman KERRY. That will be a seamless transition?

Mr. PRESTON. Yes. Right after they find out they are going to get their grants, in the weeks after that, we will be going through training with all the Women's Business Centers to take them through how to apply for those grants on the HHS system, but it will be much more responsive and it is a pretty straightforward process.

Chairman KERRY. Great. And one of the things we learned at the September hearing was that the Women's Business Centers are not being clearly told what their criteria are for evaluation, why they get the score that they do, and I understand the funding level is based on that, so it is important for them to do. Can you share with us what SBA is doing to deal with that or what it has done?

Mr. PRESTON. Well, certainly what we try to do is make the standards clear——

Chairman KERRY. You sort of communicate to them and have a transparency to that process?

Mr. PRESTON. Right. We are pulling that whole process into the Women's Business Centers Group. Historically, the granting process was in a grant administration group that didn't work directly with the Office of Women's Business Ownership. We are pulling that into Entrepreneurial Development. It is going to be done in the same way that we do Small Business Centers right now, which is a very responsive process. So I am hoping that those issues will be resolved, but as a follow-up, I will make sure to see where this issue is coming from—to make sure we don't drop the ball on that.

Chairman KERRY. That would be helpful. And also, when Mr. Prakash was here and testified, there was discussion—the IG report had recommended putting the training handbook and program online, the changes, and also allowing Women's Business Centers to provide missing or incomplete sections of the application without submitting the whole new application. Do you know if those——

Mr. PRESTON. I know the training for the grant process will be online in March. They are going to find out at the end of February, and then the second week or first week of March, that is going to be online. I don't know about the process of partial submissions, but I will check on that as well.

Chairman KERRY. That would be great. That would be helpful to them. I know they were particularly concerned about that and I think he took that as something——

Mr. PRESTON. Yes, and what I would tell you is we have had very good, very, I think, rich dialogs with the representatives of the Women's Business Centers, so all the changes we are making are really based on direct feedback that we have gotten from them and it has been very helpful, because this is an area where we do want to be responsive to them.

Chairman KERRY. Well, we really have heard and we welcome the fact that the Business Centers are singing the praises of that increased cooperative effort, so we certainly want to make sure people are aware that there are those good things happening.

On the lender oversight reforms, who is the head of the Office of Risk Management charged with lender oversight?

Mr. PRESTON. Well, the head of all Capital Access is a new Associate Administrator that we hired a couple of months ago named Eric Zarnikow, who has got a very deep background in credit. He is a career-long financial person, and when we brought him in, we specifically charged him as his top responsibility to ensure that we continue to make progress in improving expanding the lender oversight process. Underneath him, he has got a deputy named Janet Tasker, and then a gentleman named Bryan Hooper specifically runs that segment of the——

Chairman KERRY. Is that office going to be independent from the Office of Capital Access?

Mr. PRESTON. It is independent of that office today, but they both are part of the broader Capital Access organization. But they are headed by two different individuals——

Chairman KERRY. Is there a conflict there? Will they be making independent decisions?

Mr. PRESTON. I think they make independent decisions today. Now, what I will say is, and I think you are probably referring to an IG recommendation that Lender Oversight be totally pulled out of the Capital Access area. What I would tell you is any financial institution in our country has got oversight practices and outreach practices in the same institution. At some point, they come up into the same individual. But in terms of those separate groups, they are run completely separately at the working level and they don't come together until we get to the top of the Capital Access Office, which is the Deputy and the Associate Administrator.

Chairman KERRY. We also at the last hearing discussed the BLX fraud issue and whether or not it might have raised a red flag, and particularly I asked the question whether or not repurchases of $28 million, or whatever it was, from one officer, and one branch might have raised a red flag or whether it was sort of a normal process. You acknowledged then that you weren't aware of whether or not that was, in fact, so. Have you since considered enhancing diagnostic tools to track loans by lending officer and branch. Can you sort of share with us where we are in that?

Mr. PRESTON. Well, I think one of the important things to understand is most of the BLX fraud was perpetrated in sort of the 2002–2004 time line. I don't have the exact loans and the dates here with me and I would be happy to provide that with you.

Most of the enhancements in lender oversight have been in the 2004 to 2008 timeframe, we have dramatically expanded our onsite reviews. We have dramatically expanded the analytical work we do. We are in the process of significantly improving the loan purchasing process and the reviews we do there. And in the process of managing the BLX issues, we are working with a third-party vendor. One of my teams is working with them to come back and give us any lessons learned from their perspective of a third party, looking at how these loans were made, why they were made, and how we might have been able to see that.

I do want to remind the Committee, and I know this isn't a perfect answer, but we don't expect the taxpayer to lose any money based on this. When something like this happens because of the lender negligence, they keep the risk. Obviously, it reflects badly on everybody.

So I think our lender oversight processes, purchase reviews and the whole gamut have dramatically improved since those frauds were perpetrated and they will continue to improve——

Chairman KERRY. Well, one area of concern where I am not sure that there has been any motion yet is the Sacramento 504 center. We heard three recommendations that were made here during the hearing regarding that center, and as of last Friday, I am not sure they had been implemented. Have they reinstituted lender oversight at the Sacramento office?

Mr. PRESTON. The Sacramento——

Chairman KERRY. That is the Abridged Submission Method audits, what is known as ASM?

Mr. PRESTON. Well, they still have the ASM method, and I think the issue that the 504 industry is concerned about in Sacramento was some of the backlog issues that we had out there in terms of turning around decisions quickly so that they could then close their loans in a timely basis. I am not familiar with specific oversight issues that you are referring to, but I would be happy to follow up on them for the record.

Chairman KERRY. Well, on employee retention, there were pay issues. There was an issue about additional staff for processing loan approvals, et cetera——

Mr. PRESTON. Yes.

Chairman KERRY. There was an issue about the lender oversight, expanding ASM audits to loans of the premier certified lenders.

Mr. PRESTON. Yes. Let me——

Chairman KERRY. If you would like, I mean, I have got a number of questions. We don't have time, obviously, to do them all. I would like to leave the record open——

Mr. PRESTON. Great.

Chairman KERRY [continuing]. And we will probably submit some in writing, if we can, and——

Mr. PRESTON. Let me take 1 minute to comment broadly. One of the things we have found, and you all have obviously digested it in chunks in a number of our different programs, but very broadly speaking, I think many of our processing centers in disaster, in 7(a), in 504, and in our 8(a) programs have suffered from processes that aren't terribly efficient, technologies that aren't very supportive, and backlogs.

And so as you look at what we are trying to do at this agency much more broadly, is to bring in management practices where we go in and say, 'who are we serving at the end of the day, how does this process need to get to them quickly and efficiently, how do we need to provide technology so that we can communicate with them well, make good decisions,' and it is hitting across all of our processing centers and Sacramento is no exception.

Now, the other thing we have, Senator, which frankly we didn't have even a year ago was good data on these centers to really understand where these problems were.

So the reason I give you that broader context is this is a part of a much broader thing. I would be happy to brief the Committee's staff on where we are going with all these matters——

Chairman KERRY. I think that would be really helpful, because one of the questions I wanted to ask, and maybe you just want to comment on it, you mentioned disaster. Are the IG recommendations with respect to that being implemented?

Mr. PRESTON. Oh, yes. There are any number of IG recommendations, but what I would tell you is the work that we are doing in disaster goes far beyond any of the IG recommendations in terms of preparedness. So I think the IG recommendations tended to look at specific processes or problems. They are sort of being encompassed in a much broader program to improve the——

Chairman KERRY. Well, I think it would be great to have staff follow up on that and get that briefing in full so we can——

Mr. PRESTON. Yes, and frankly, we would be happy to take you all down to Fort Worth to look at that processing center and see what we have done down there. We think it is a great example of what can be done.

Chairman KERRY. Thank you very much. That is a good idea. Senator Snowe?

Senator SNOWE. Yes, thank you, Mr. Chairman.

Just to follow up on that, some of the issues that were raised by a former employee of the SBA as well as the Inspector General regarding the Office of Disaster Assistance, and you mentioned that you were going to convene a meeting of the leaders in that office——

Mr. PRESTON. Yes.

Senator SNOWE. Has that happened, and what——

Mr. PRESTON. Let me tell you what we did——

Senator SNOWE [continuing]. To rectify some of those issues?

Mr. PRESTON. Right, and you and I talked about it after the last hearing, as well. Yes. Let me tell you what we did. We wanted to go about this systematically, so we did a couple of things. First of all, we decided to do a broad-based employee survey down there, similar to the employee survey we did for the rest of the agency, and then we worked with the IG to expand that survey to include questions specifically that they wanted to see to understand the environment down there.

Right now, we are in the process of hiring a third party to come in, review that survey, and then spend time down there to make sure that any issues that came out in that survey are being addressed. So we are trying to do it in sort of a methodical way in conjunction with the IG on the survey and then bring a third party in to do the analysis.

What I would tell you is, and I know some of you may have seen a press release on this, when we did our 2007 employee survey compared to 2006, neither of which included the disaster operation, we saw dramatic improvements in employee morale, employees saying that they could do their jobs effectively. When we surveyed the disaster business separately, their scores dramatically exceed the rest of the agency now. So the very part of the agency that was suffering so badly is now in terms of employees saying that they can operate effectively, employees saying that they respect leadership, is now sort of the gold standard in the agency.

And so we are not only trying to understand whether or not we have kind of addressed those issues, we are trying to understand how we can make sure to apply those standards to the rest of the agency because the feedback we are getting is so good.

But we are on a pathway. We are hiring a third party. The input is going to be independent. The IG will be part of it——

Senator SNOWE. That is outstanding. I think that is important and I applaud you for your efforts in that regard. I know that the employee morale prior to your tenure was remarkably low, and so——

Mr. PRESTON. We still have a ways to go.

Senator SNOWE. You have a ways to go, but——

Mr. PRESTON. We still have a ways to go.

Senator SNOWE [continuing]. You are moving—that you are on the ascent is very important in that regard, the right direction. I applaud you and——

Mr. PRESTON. I appreciate that——

Senator SNOWE.—I hope you will continue those efforts, because I think it means a great difference to the employees and their families within that agency, so thank you for doing that.

Mr. PRESTON. You know, the thing, I think, that is—one of the things that is most heartening about the results we have is we are seeing specific improvements in areas like employees saying that they have the skills to do their jobs, they have the training, they have the development capability. So it is not just "I feel good about being here". It is, "I feel like I can do my job effectively and serve effectively", and those are really the outcomes that we are hoping to see.

Senator SNOWE. That is critical. That is very good.

Mr. Administrator, the American Banker reported that at your State of the Agency speech last Tuesday, you indicated that the SBA loan volume has dropped by roughly 3,000 loans compared to the previous September–December quarter——

Mr. PRESTON. Hmm——

Senator SNOWE [continuing]. Because the banks now have automated systems and it is hard to work with the outdated, non-automated system at SBA. Is that true?

Mr. PRESTON. I don't think I cited a number, but I would be happy to give you those numbers. I don't have them at the top of my head. What we are seeing in loan volume is the following. We are seeing a decline in SBA Express. As you know, SBA Express is sort of a very simple process. A lot of them, especially the larger banks, had programs set up that were heavily credit scored, and as they began to experience some of the issues in their broader portfolios, what they began to do was require higher credit scores for SBA Express. So in the smaller high-volume Express loans were seeing a fall-off.

On the PLP loans, which are typically larger loans, they are more integrated, I think, into sort of the broader relationship management side of the bank, we are seeing much more stability in the volume. So as a result, we are seeing a higher decline in numbers of loans than dollars because the little ones are the ones that are falling off.

When I look at that, the concern I have is, and this is something we are dissecting from every angle. The concern I have is the potential that those smaller loans often go to startup businesses, and what we found in the Urban Institute study on all of our programs is that we have a dramatically higher penetration as a percentage of our portfolio in startup businesses than the conventional lending sector. So we want to make sure we are doing everything we can to reach those businesses.

Now, in the last couple of weeks, we have rolled out relationship plans throughout our national network so that our district offices are looking at their top 15 banks, putting in place calling programs, reaching out to them to make sure we understand what we can be doing to expand our relationship with them. My team has come to me with a personal outreach plan for me, for my deputy, and for the head of Capital Access to reach out to senior levels at the major lending institutions around the country. We are having a lender roundtable in a couple of weeks with senior lenders coming in and I have personally had meetings with any number of them, even in the last couple of months. So we are working very hard to make sure that we are coordinated with them and doing everything we can to expand the usage of our products where it makes sense.

Senator SNOWE. Is it a direct result of organizational issues——

Mr. PRESTON. Yes.

Senator SNOWE [continuing]. Or is it a result of the economy?

Mr. PRESTON. You know, I think that the organizational issues are being led by other challenges that some of these banks have in their portfolios. Some of the banks, I think, that have reported the largest credit challenges have been ones that are making the most immediate decisions to pull back.

What I would also tell you is that we are not seeing a tremendous amount of continuity across banks in terms of what decisions they are making. Some of them are actually expanding. Some of them are contracting heavily. The one piece of common information, I think, across the banks is that the Express products are seeing some decline.

Senator SNOWE. And the American Banker also indicated that over the last 2 years, 368 lenders have dropped out of the SBA's lending program——

Mr. PRESTON. Yes, that——

Senator SNOWE [continuing]. Is that true?

Mr. PRESTON. Yes——

Senator SNOWE. And how does that exacerbate matters in terms of delivering these products——

Mr. PRESTON. It does exacerbate matters, it absolutely does, and this is why we are rolling out Rural Lender Express. We have an outreach effort right now with a new loan process to bring community banks back into the program. Because what the community banks have told us is our processes are too difficult, they have to go up a learning curve. So what we are doing right now——

Chairman KERRY. Is that why most of them are dropping out?

Mr. PRESTON. The anecdotal feedback we get from our field is yes, that if I am doing three loans a year, it doesn't make any sense for me to try to learn now to do an SBA loan. So what we are doing is we are rolling out something that is a two- or three-page application. They can do it online. It is relatively simple. We are promising them turnaround time on the loan in a few days. And if they have questions, we have set up a help desk for them so they can get real-time support. We are piloting it right now in eight States and as soon as we find out—as soon as we feel like we have got the product where it needs to be in terms of ease of use and the support in Sacramento to handle it, we are going to begin adding regions.

But, you know, I think, Senator, you have been on this issue a long time, which is are you doing the right kind of outreach to community banks. I think this product will be a big solution for us. It will take us a number of months to get this out across the country, but it is going to be very important for us.

Senator SNOWE. Also, one other area is lender oversight fees and the impact it has on lender participation. I understand that the SBA is now going to increase lender oversight fees in April, is that true, for three quarters——

Mr. PRESTON. Yes, the lender oversight——

Senator SNOWE. What impact is that going to have on lender participation and the overall health of the lending programs?

Mr. PRESTON. Yes. The cost of the lender oversight fee relative to the size of the portfolio, the banks that are getting hit by the fees, in most cases is relatively small. The offset fee is $73 per million, I think, so it is a fraction of a basis point. In addition, the larger lenders, $10 million and above, require an onsite exam every 2 years and we charge them for the cost of that exam. It is generally—I think it is $26,000. The IG recommended that we perform onsite exams for loans with portfolios as small as $4 million. We felt that that was too small. We did portfolios as small as $10 million.

So generally, I think 350 of our 5,000 lenders will have onsite exams. Most of them are not affected by it. It is really the larger ones. I have some concern that when you look at the smaller lenders that have the onsite exams, it may be a bit of a challenge. I think it will be ten or 11 basis points on their portfolio. So one of the things we are looking at right now is whether or not that bottom part of the tier, right when they come in, whether or not we can be doing something there.

But broadly speaking, I don't think it is going to have a significant impact. I think there is a——

Senator SNOWE. Well, it dovetails with the decline in the economy, too, so I wonder if the timing of that, raising those fees in the midst of a declining economy won't have——

Mr. PRESTON. Yes——

Senator SNOWE [continuing]. An adverse impact on the overall participation in the program, or losing more lenders, for that matter. I don't know.

Mr. PRESTON. Yes.

Senator SNOWE. I think this is obviously something you have to gauge——

Mr. PRESTON. It is an issue I have been discussing with my staff, but by the same token, that is allowing us to go from 50 lenders a year to about 250 lenders a year in terms of doing good onsite reviews, so we are significantly expanding our oversight based on those fees.

Senator SNOWE. No, I understand because I think it is important to enhance accountability and also certainly in conducting oversight. That is one of the other issues that emerged in one of the hearings with Inspector General Thorson and with the Preferred Lenders Program, as well, making sure that the SBA exacts accountability.

Mr. PRESTON. Yes. Now, we have seen a decline in our delinquencies until very recently, and I think when you look at when we began instituting heavier lender oversight, we actually began to see the portfolio quality improve over time. I have to say, though, given what is happening in the economy today, these banks are reporting higher delinquencies and we are starting to see some pressure there——

Senator SNOWE. I would hope that you would submit to the Committee the delinquency rate and what is happening there. That is something that obviously we should be privy to——

Mr. PRESTON. We will come over and brief your staff——

Senator SNOWE. Definitely——

Mr. PRESTON [continuing]. We will show them the graphs and tell them what is happening and why we think it is happening. We have looked at regions and industries and to really get a handle on this data.

Senator SNOWE. Definitely. And finally, on the SBA energy clearinghouse, is that operational yet?

Mr. PRESTON. Right now, we are working to make sure that we are complying with the 2007 law as well as the one enacted in 2005. I think in some places it modified it, and I know I spoke with my Chief of Staff this morning. She feels good about the progress we are making. She is meeting with the Energy Star people tomorrow. But if you would like us to come back with any detailed outline of what we are doing for the record, we would be happy to do that.

Senator SNOWE. We would definitely like that. It is obviously an area—

Mr. PRESTON. Yes.

Senator SNOWE [continuing]. Where small businesses are looking——

Mr. PRESTON. Especially considering energy costs today, sure.

Senator SNOWE. Exactly, and only 43 percent are participating in that regard, so clearly we have to do more, so if we can get it up and operational and working to satisfy the interests of those who are wanting to engage in energy programs and adopt energy efficient programs in their industry, they ought to have the ability to have that information.

Mr. PRESTON. Okay.

Senator SNOWE. Okay. Thank you, Mr. Administrator.

Mr. PRESTON. Thank you.

Chairman KERRY. Just a final couple of questions, if I can. Thank you, Senator Snowe.

I want to follow up on Senator Snowe's question on the lender oversight fees. I think, Mr. Administrator, I mean, I hope you can hear this. I think it is a huge mistake to move down that road, especially in light of what you have just said about what the sort of pull-back of many people in this economy already troubled from the lending. SBA got out of the business of direct lending because it decided it didn't want to carry that expense of doing it. We would let the private sector do it. And the one thing the SBA would do is oversight, be responsible for guaranteeing the safety and security of the process.

In addition to the other fees which we have been trying to lower which have been raised, to now charge those folks for their own oversight is sort of to send a message to them, in my judgment, you know, we just don't care that much about this and you guys carry the cost. If you want to participate, terrific.

I think you have got to make it—you know, it is a relationship and I think you are at risk in those fees of driving more people away and of actually having a counter-impact on the marketplace from what you want to have right now, particularly at this moment.

Mr. PRESTON. Right. We are doing a number of things, actually, to bring down the cost for banks through all sorts of automation initiatives, initiatives to simplify our interactions with them, initiatives to reduce their paperwork. All that resonates very strongly with the banks because they are going in that direction. If they go in that direction with us, it brings down their costs.

Chairman KERRY [continuing]. Oversight—shouldn't that be in the SBA's budget?

Mr. PRESTON. It is no—well, I don't see it any different than——

Chairman KERRY. It is government protection and function, the oversight. We are asking to make a government-backed loan.

Mr. PRESTON. Well——

Chairman KERRY. We need to be the ones——

Mr. PRESTON [continuing]. First of all——

Chairman KERRY [continuing]. To know what is going on. It is our responsibility. And that is the part of the relationship that sort of encourages them to do it, I think.

Mr. PRESTON. Well, I am not sure that I would look at it——

Chairman KERRY. All the lenders are against it, aren't they?

Mr. PRESTON. Uh——

Chairman KERRY. The lenders clearly——

Mr. PRESTON. I think any time—sir, any time you ask them if they want to pay a fee or not, they are going to, you know——

Chairman KERRY. But——

Mr. PRESTON. The larger lenders have come back——

Chairman KERRY [continuing]. If you were in that seat and somebody said, okay, here is an extra fee on you, would it not conceivably be the tipping point where they would say, okay, to hell with this. We don't need to do this.

Mr. PRESTON. It could be for certain lenders, but I would counter with——

Chairman KERRY. Why take the risk?

Mr. PRESTON.—I think we are making and taking any number of actions which go far beyond the challenge with this fee to make it easier for them to do business with us, do better outreach, simplify our process, and be an easier institution to do business with.

Chairman KERRY. Well, I would love to see the quantifiable net sheet on that.

Mr. PRESTON. Great. The other thing I would say is——

Chairman KERRY. I am asking you to provide that to the Committee.

Mr. PRESTON. Okay.

Chairman KERRY. I would like to see the quantifiable net-net of how this leaves them plus in terms of their expenditures.

Mr. PRESTON. Well, I don't think this fee leaves them plus, but I don't think——

Chairman KERRY. Well, then——

Mr. PRESTON [continuing]. An FDIC fee——

Chairman KERRY [continuing]. Why press the tipping point here? Why send them the message that you have got to pay for your own oversight and——

Mr. PRESTON. We are paying to do oversight for the benefit of the—I mean, this whole issue we are talking about with all these things, this enables us to do sufficient oversight because it gives us the funding to do that. And so, you know, we are dramatically expanding the number of institutions we can get to because of that. And so the other thing I would mention is it pales in comparison to the fees that most of these banks are paying to other regulators. It is a small fraction of what they are going to pay to somebody else. This specifically doesn't——

Chairman KERRY. This is the first time I have heard the government make an argument that the private sector ought to pay more because they are already paying more to the government.

Mr. PRESTON. But the government pays about $150 million that isn't covered by these fees to run our Capital Access Programs. I mean, we run——

Chairman KERRY. We get something for this. We get them to do the lending, to make loans they might not otherwise make.

Mr. PRESTON. I agree with you on the value of our programs. What I am telling you is I do think that we have a very rich investment that we don't charge them for——

Chairman KERRY. That sounds like we are getting into a private sector competitive analysis, which is not what this is about.

Mr. PRESTON. You know, I think if you look at the cost, this is a relatively small number, and I do concede that there is a group of banks on whom it may have an impact. But in the broad scheme of things, I don't think that these fees are significant compared with the profitability they are getting in these programs, the fee they would expect to pay to a regulator, or our overall cost of doing this business——

Chairman KERRY. Well, as I said, I would really like to see that comparative sheet——

Mr. PRESTON. Okay.

Chairman KERRY. I would like to ask for it as part of the record here.

I have only one other question and that is on the Military Reservist Economic Injury Disaster Loans.

Mr. PRESTON. Okay.

Chairman KERRY. How are we doing on that?

Mr. PRESTON. Umm——

Chairman KERRY. Have we issued more loans since the last hearing when we were at about 260-some or whatever it is?

Mr. PRESTON. I would have to get back to you on that.

Chairman KERRY. Would you find out for me?

Mr. PRESTON. I don't know——

Chairman KERRY. Do you know what the demand has been like——

Mr. PRESTON. This is a program that is—you know, we continue to do outreach on it. Frankly, Senator, I think it is one of the best programs we have and probably the most underutilized, so we would love to work with you to get the word out there, but certainly every time I am in front of a veterans' group, every time I am talking to my counterparts in other agencies, I am talking about this program, trying to encourage usage and get the information out. It is a great program, but whatever number we give you, it is not enough because I don't think we are as effective as we need to be in getting the word out.

Chairman KERRY. Well, we would like to know. If you can find out and submit that also as part of the record, I would like to see where we are in that now. I would like to get a sense of the demand on it, too, and what the outreach—what the affirmative outreach effort is——

Mr. PRESTON. Sure.

Chairman KERRY [continuing]. Of the agency itself beyond your own speeches to the veterans' community because I think it is going to be particularly important in this economy.

Well, I think we really appreciate your taking the time to be here with us today. I know it is time you would probably love to spend somewhere else, I am sure. But on the other hand, I think it is an important part of the process and we appreciate it.

Let me say for myself, and I think Senator Snowe shares this, that it is very clear how immersed you are in a lot of the details and it is clear also you are providing leadership. Sometimes we may disagree with the direction and what you are doing, but I think you are engaged and providing some badly needed leadership at the agency and we appreciate that very, very much. I think you have spoken today with a command of detail and certainly expressing your point of view about things that has been absent from some of these hearings in the past and I want to pay my respect to that. I think you have been very articulate, even though obviously, I think on occasion you have been wrong, but——

[Laughter.]

Chairman KERRY. But that said, we certainly appreciate your time.

Mr. PRESTON. Thank you.

Chairman KERRY. Senator Snowe, do you want to add anything?

Senator SNOWE. No.

Chairman KERRY. So thank you for this. We will see you very shortly. The budget will be coming up. We will have the budget hearing, will be the next time we see you, and I hope obviously your budget is one that reflects the administration's commitment to these reforms and efforts and we look forward to that discussion.

We stand adjourned. Thank you.

[Whereupon, at 11:55 a.m., the committee was adjourned.]

APPENDIX MATERIAL SUBMITTED

Statement for the Record for
Senator Mary Landrieu
for Small Business Committee Hearing on
"Holding the Small Business Administration Accountable: Women's Contracting and Lender Oversight"

Thank you Chairman Kerry for calling this oversight hearing on holding U.S. Small Business Administration (SBA) accountable regarding Women's Contracting and Lender Oversight. I also thank Administrator Preston for his willingness to testify before the Committee on the SBA's work on these issues. This hearing continues the important bipartisan work with Ranking Member Snowe and other members of Congress to monitor the SBA's performance in implementing key legislation that would release assets for women-owned small businesses.

As you know, in 2000 Congress enacted section 811 of the Small Business Reauthorization Act. This law stated that 5 percent of Federal contracts should go to women-owned businesses. It has yet to be implemented, for in 2006, women-run businesses only won just over 3 percent of Federal contracting dollars. This percentage is astounding with almost a third of all business in the U.S. owned by women. Women-owned businesses contribute a great deal to our struggling economy and deserve a fair shot at doing business with the Federal government.

According to the Census Bureau, in Louisiana in 2002 there were 86,900 women-owned businesses, which are 26 percent of the state's 328,800 businesses. Furthermore, these businesses generated $12.3 billion in revenues. So in my state, women-owned businesses are an important part of our economy just as they are in the rest of the country. Following Hurricanes Katrina and Rita, I have been fighting to ensure that our local small businesses have an important role in rebuilding their communities. I believe that just as our local businesses deserve their fair share of Federal recovery contracts, so too do women-owned businesses deserve a level playing field when competing for Federal contracts.

Despite the fact that there has been a call to action from the courts and Congress on the issue of women's procurement, the SBA published rule #3245-AF40 in December 2007. This rule considered 4 of 2,300 women business categories underrepresented. In my perspective, the SBA had many different options on the table in terms of how to implement a rule on this issue. The rule which was published might be one which can hold up to scrutiny in the courts but it seems to defy conventional wisdom. It might be legal but, for me it defies logic. For example, this rule contradicts a study commissioned by the SBA itself which noted that women were underrepresented in Federal contracting in 87 percent of all industries. So it appears that this new rule does not follow Congressional intent nor the law enacted in 2000. For this reason, I, along with other women Senators, sent a letter to SBA on February 2, 2008 voicing our strong opposition to rule #3245-AF40.

In closing, it is my sincere hope that the SBA will come up with a new rule that would be comparable to the growing number of women-owned business. It is important that women-owned businesses are given a fair chance to compete and it is my hope that this hearing will accomplish that. I look forward to working closely with the SBA and my colleagues on the Committee to work towards a reasonable solution on this issue.

I thank the Chair and ask that a full copy of my statement, as well as a copy of the February 2, 2008 letter appear in the record.

United States Senate

WASHINGTON, DC 20510

February 1, 2008

The Honorable Steven C. Preston
Administrator
Small Business Administration
409 Third Street, SW, Suite 7900
Washington, DC 20416-2230

Dear Administrator Preston,

As women in the Senate we strongly oppose rule #3245-AF40 regarding Women-Owned Small Business Federal Contract Assistance. This rule undermines 8 years of Congress' efforts to help women-owned small businesses compete on a level playing field for federal contracts.

Almost a third of all businesses in the US are owned by women. They are mothers, wives, and sisters but also hardworking entrepreneurs contributing to the economy. They deserve a fair shot at doing business with their government but in 2006, women run businesses only won 3.4% of federal contracting dollars.

In 2000, Congress passed a law that said 5% of federal contracts should go to women-owned businesses. Considering the growing number of women business owners, a 5% goal seems more than realistic. To meet this goal, SBA was supposed to instruct agencies to limit certain competitions to women-owned businesses. However, the agency dragged their feet and according to the court that looked at the case "sabotaged...the implementation of the program."

In December, despite clear congressional intent and a strong call to action from the courts, the SBA published a rule that would only help women in 4 of 2,300 business categories. This is outrageous, especially considering a study commissioned by the SBA itself found women were underrepresented in federal contracting in 87% of all industries. SBA's new rule would do almost nothing to help level the playing field – which is what Congress has been trying to do for over 8 years.

Congress has demanded that women in business be given a fair chance and we're relying on your agency to come through for them. Your first step should be to come up with a new rule that takes a realistic look at women's growing small business presence but continued lack of federal contracting opportunities. The pending rule ignores congressional intent, SBA's own research, and the reality many women confront when trying to work with the federal government. It needs to be withdrawn.

Sincerely,

Barbara A. Mikulski
United States Senate

Dianne Feinstein
United States Senate

Barbara Boxer
United States Senate

Patty Murray
United States Senate

Mary L. Landrieu
United States Senate

Debbie Stabenow
United States Senate

Maria Cantwell
United States Senate

Hillary Rodham Clinton
United States Senate

Senator John F. Kerry
Questions for the Record for Administrator Preston
"Holding the Small Business Administration Accountable: Women's Contracting and Lender Oversight"

Disaster Questions

1. **After Hurricane Katrina, the SBA faced many challenges, and the Committee heard reports of some questionable loan practices that emerged to deal with the backlog of applications. Documenting some of these challenges, the SBA IG has come out with the final version of a report entitled "Cancellation of Approved Disaster Loans to Individuals and Businesses Impacted by the Gulf Coast Hurricanes." What specific steps have you taken and are taking to implement the IG's recommendations and ensure that the mistakes of the past will not be repeated?**

   Response: SBA has established procedures for processing disaster loan applications and closing disaster loans. SBA sends loan closing documents to each approved Applicant, and includes a letter instructing the Applicant how and when to complete and return the loan closing documents if he or she wants to pursue obtaining a loan from SBA. Applicants are notified at the time of a loan approval that they have 60 days to return their loan closing documents. Under normal procedures, SBA will send the Applicant a notice that the loan will be cancelled in fourteen days if the loan closing documents are not completed and returned to SBA. These and other procedures were developed by SBA to help manage the credit risk in the disaster program and to protect government funds that might otherwise be lost to fraud, waste or abuse.

   Additionally, SBA had reconsidered the Agency's policy on reinstatement deadlines for victims of the Gulf Coast Hurricanes and had extended the deadline for Applicants to notify SBA that they would like to reinstate their loans until January 31, 2008. Applicants that could not be contacted by phone were mailed letters to their last known address explaining the deadline had been extended.

   The IG report did not outline specific recommendations to change policy or procedure. The report recommended that the SBA contact Applicants that had not received the benefit of multiple phone calls and extend their reinstatement period and review four canceled loans that should have been declined and referred to FEMA as appropriate. SBA complied with both recommendations.

2. **We have a disaster bill currently in conference with a provision that deals with ensuring adequate staffing levels, both full-time and reserve staff, to deal with a future large scale disaster. I have heard concerns that, over time, if we do not have another large scale disaster, it will be difficult to maintain a large, well trained staff. Can you explain your plan to ensure you maintain enough trained staff to respond to a future large scale disaster?**

Response: ODA's Disaster Reserve is composed of two groups: Active Reserve and Ready Reserve. There are approximately 1,480 Active Reservists currently on SBA's rolls. When former SBA employees join SBA's Active Reserve, they commit in advance to report for duty within a 48 hour timeframe. For planning purposes, SBA anticipates that 70 percent of Active Reservists will honor that commitment (70% of 1,480 = 1,036). By having a large Active Reserve list, the Agency has better positioned itself to handle a catastrophic disaster situation, and augment its ability to quickly ramp up.

In addition, approximately 2,300 Ready Reserve employees are currently on SBA's list as potential sources of human capital. For planning purposes, SBA anticipates that 55% of Ready Reservists will report to duty if asked (55% of 2,300 = 1,265). These individuals provide SBA a base of potential employees that can easily be re-integrated into SBA's operations, leveraging existing familiarity with SBA systems and processes to save resources and expedite the surge process.

In addition SBA has identified and trained employees in the Office of Capital Access and District Offices that will be immediately available in the event of a catastrophic disaster.

Energy Program

1. **In 2005, I helped pass an energy bill that instructed the SBA, along with the EPA, to develop a government-wide program building on the Energy Star for Small Business Program to assist small businesses in becoming more energy efficient, understanding energy efficiency cost savings, and accessing federal procurement opportunities with Energy Star technologies. In response to this mandate and after questioning in past hearings, the SBA has put up a single webpage. I have looked at this webpage (http://sba.gov/energystar/index.html) and all I see are series of links, most leading to the Energy Star program, some leading nowhere. This is not what we envisioned as a government-wide program when we passed the original legislation.**

   The 2007 CLEAN Energy Act instructs you to follow the 2005 law within 90 days, expands on this program, and takes further actions to improve energy efficiency. The 2007 bill includes programs that promote telecommuting, grant loans for energy efficiency projects, and facilitate on bill financing for energy improvements. Who will be in charge of implementing these programs? Will they have a budget to get the job done and how many staff will be devoted to these projects? Will resources and grants be given to the Small Business Development Centers to promote energy efficiency? How are you preparing to respond to the provisions in the 2007 CLEAN Energy Act?

   Response: SBA has developed a government-wide portal that builds upon information provided by the Energy Star for Small Business program which will provide America's small businesses with a wide variety of energy efficiency information available not only through Federal sources, but through state and local resources also. The portal that SBA has established contains a wealth of information for small businesses that brings to bear the resources of several federal agencies, including the Environmental Protection Agency and the Department of Energy.

The portal contains links to the Energy Star for Small Business Program, small business financing options and other Energy Star resources. The portal does not try to duplicate all of the information contained on the Energy Star website, but builds upon the Energy Star website's exhaustive resources to provide relevant and easy to find information for small businesses.

The Office of Policy and Strategic Planning will be responsible for implementing the programs in the 2007 CLEAN Energy Act. There will be a total of five (5) staff members devoted to these projects.

The SBA is currently drafting the appropriate Policy Notices and regulations in order to respond to the provisions on the 2007 CLEAN Energy Act. In addition, SBA is establishing a small grant program of $1 million, to be split between the Energy and Vets programs, to provide energy efficiency assistance through the Small Business Development Centers.

SBA is working with EPA's Energy Star for Small Business office to obtain printed materials for distribution to each of the 1,200 SBA district offices and each office of the Agency's Resource Partners. These materials will inform small businesses on how to become more energy efficient, increase cost savings from improved energy efficiency, and provide financing options for energy efficiency upgrades.

Additionally, SBA will distribute a CD-ROM version of these materials to aid in disseminating them to end-users, as well as a publicity poster for district offices and resource partners.

Women's Business Center Program Questions

1. **At the women's small business hearing in September, the SBA IG Office reported an egregious number of late payments to Women's Business Centers. These late payments—sometimes over 300 days late—forced centers to reduce services or curtail staff. SBA has done a lot to address these concerns. However, at this time:**
    - **How many payments are currently still pending at SBA?**
    - **How many of those are 30 days or older?**
    - **What is SBA doing to get those payments taken care of and how long will it take?**

Response: As of February 20, 2008, a total of 91 invoices are in-house. The breakdown is as follows:

30 days or less: 53 (FY 2008 invoices/advances not yet reviewed)

31 days or more: 38 (5 with match or compliance issues awaiting legal opinion, 33 awaiting additional information from respective WBC or now in final *review process)*

2. **At the women's small business hearing in September, Associate Administrator Anoop Prakash testified that the renewal grant program would be implemented within 120 days.**

- **Please describe, in detail, the plan you expect to follow in continuing to implement the new renewal grant program. Specifically, I would like a timeline of when we can see the selection of centers, awarding of grants and disbursal of funds completed.**

Response: The current timeline is attached, and we are pleased to have met the 120 day mark set in September.

- **In addition, please tell me when graduated centers can expect to begin receiving SBA grant funding.**

Response: Notices of Award were sent to returning centers during the first week of March 2008.

Lending Oversight

1. **At the hearing, you indicated that the new lender oversight fees charged by the SBA were "not significant" when compared with (i) the profits made by banks on the SBA-backed loans, (ii) the fees that banks would expect to pay a government regulator, and (iii) the SBA's overall cost of running the program. Please provide the formula, metrics, analysis, etc. that supports your assertion.**

Response: Each lender is unique, so there is no "one size fits all" approach to determining the comparative profit and cost calculation for the entire 7(a) lender community. For example, a lender's profitability depends upon such factors as the size of the loan, the loan's interest rate relative to the lender's cost of funds, whether the lender retains the servicing interest in the loan or sells loan servicing, and the lender's administrative and servicing cost structure. It is also important to note that, while in some respects the SBA program may be more costly to lenders than conventional lending, the SBA guaranty does provide significant financial benefits to lenders. For example, the guaranty reduces a lender's potential loss on a defaulting loan by between fifty and eighty-five percent. In addition, the U.S. government guaranty reduces the reserves a lender needs to carry on its balance sheet relative to a conventional, non-guaranteed loan.

SBA believes that its lender oversight fees are a relatively insignificant cost to lenders. Although the FY2008 off-site review fee has not yet been determined, the off-site review fee billed in 2007 was at a rate of $73 for every $1 million in SBA guarantee dollars outstanding, or less than 1 basis point. Since the fee is based solely on the SBA-guaranteed portion of the loans, the affect of the off-site fee is further minimized. For example, if a lender's portfolio consists entirely of SBA*Express* loans, the lender's off-site fee would apply to only 50% of the total loan amount.

The on-site review is a fixed rate, contract cost. The average cost per review is approximately $25,000. However, on-site reviews are performed on only those lenders with an outstanding SBA portfolio of more than $10 million, and the agency is evaluating whether it can reduce the on-site review cost for small lenders just above the $10 million threshold. Since federal regulators include the cost of their safety and soundness examinations in their insurance assessments, it is difficult to make a direct comparison between SBA's on-site review cost and regulatory safety and soundness examinations. In addition, federal financial regulators generally assess their fees based upon the bank's total assets. Based upon our review of the regulator's fee structures, the SBA's on-site review fee is a fraction of the fees charged by federal financial regulators.

2. **The IG, in reviewing the SBA's oversight of BLX and the Agency's lack of disciplinary action, concluded that SBA may not have taken disciplinary action against BLX because it was one of the SBA's largest lenders and taking action against them would have reduced loan volume. The IG came to that conclusion because the lender oversight programs answer to the Office of Credit Access, which is responsible for loan volume. Do you plan to give the Office of Credit Risk Management independence from the Office of Capital Access? Please explain why or why not.**

   Response: We believe that the retention of the Office of Credit Risk Management (OCRM) within the Office of Capital Access (OCA) allows both offices to operate most effectively. The current structure allows OCRM to operate independently, while facilitating an appropriate level of communication between the offices responsible for the oversight of lenders and for the program policy and lender relations functions. Allowing both offices to report to OCA ensures that there will be an open line of communication that may not exist if OCRM was an independent organization.

   However, SBA has taken additional steps where needed to maintain the independence of the lender oversight function. In October 2004, SBA created the Lender Oversight Committee, which plays a critical role in the oversight and enforcement process and which is comprised of a majority of members outside of OCA. The Lender Oversight Committee, composed of senior SBA managers including the Deputy Administrator, Associate Administrator for Capital Access, Chief Financial Officer and General Counsel, has the authority to review the activities of OCRM and approve lender oversight actions. In addition, OCRM has the authority to refer any actions directly to the Lender Oversight Committee, rather than OCA, and has direct access to senior SBA executives if necessary.

3. **You maintain that the SBA's loan monitoring system is not designed to detect fraud but to identify "irregularities." In the November 2007 lender oversight hearing, I**

asked whether there were aspects of the BLX fraud that should have raised a red flag. For instance, the $28.4 million in purchases of SBA loans from one lending officer in one bank branch; that seemed to be an "irregularity." You responded that you didn't know and the response at the January 30, 2008, hearing was unclear.

a. **Have you determined whether that was an "irregularity" when compared to branches with similar volume?**

   Response: Our review of loans purchased from BLX indicates that the office in question had a higher purchase rate than other branch offices. However, it is important to note that a significant number of these loans were originated and purchased during the years when SBA was still developing its lender oversight capabilities. As we have outlined in the November hearing and in subsequent briefings with Committee staff, SBA has made significant strides in lender oversight and continues to build on these improvements.

b. **Are you considering enhancing the SBA's diagnostic tools to track bad loans (those repurchased) by lending officers?**

   Response: At the present time, SBA does not have the data to track loans by loan officer. We will evaluate whether it is feasible and cost-effective to add loan officer tracking data to the information we collect and analyze; however, adding such a capability would take a substantial amount of time, and would likely only be added for new loans rather than loans already approved by SBA.

c. **Are you considering enhancing the SBA's diagnostic tools to track bad loans (those repurchased) by branch?**

   Response: The SBA is looking for ways to find unusual patterns of activity in addition to existing tools. We will consider adding branch level portfolio review if our analysis indicates that it is feasible to perform branch level analysis, and that such an analysis would prove effective.

4. **In response to your offer to follow-up on my questions regarding lender oversight of the 504 loans in the Sacramento Center: In the November 2007 hearing, the 504 loan program representative, Mr. Jim Baird, made three recommendations that could have easily been implemented before the hearing on January 30, 2008. However, as of the Friday before the hearing, on January 25th, none had been implemented.**

   a. **Has the Sacramento office re-institute the Abridged Submission Method (ASM) audits, which is a lender oversight function to maintain credit quality?**

      Response: ASM audits are actually designed as compliance audits, not underwriting reviews completed for the purpose of determining loan credit quality. ASM audits are conducted periodically throughout the year, on a sampling basis. Due to issues related to turnover in the Sacramento Loan Processing Center, SBA has found it necessary to focus its processing efforts on maintaining responsive loan processing and servicing action turnaround times, which are higher priorities to SBA and the Certified Development Companies (CDCs). As we fill vacant positions, the processing center will focus more of its efforts on its ASM audit process.

b. **Have you expanded the Abridged Submission Method (ASM) audits to cover loans submitted by Premier Certified Lenders (PCLs), those who have delegated authority and go largely unsupervised?**

Response: We have heard CDC concerns about Premier Certified Lenders, and we are looking into whether it is possible to expand the ASM audit process in this way.

c. **Have you added staff to process loan approvals? Our witness testified that there is insufficient staff to do a thorough, timely process of loan approvals that SBA is scrimping on appraisal checks and environmental checks on the properties.**

Response: As a result of a staffing review, SBA has decided to allocate additional staffing resources in the Sacramento processing center. These positions are in the process of being filled.

d. **Has a review taken place of the compensation of staff in Sacramento to address the assessment that there is high turnover because the pay is not high enough?**

Response: A review of the compensation of staff in the Sacramento processing center has been performed. Based upon the results of the review, SBA has approved additional analyst positions for the center at a salary level we believe will reduce employee turnover.

5. **During an exchange about lender oversight fees, several questions were posed that the Committee would like to see answered in greater detail. The Committee continues to receive feedback from 7(a) lenders regarding the lender oversight fees imposed last year, asserting that their cost and the value of what the lenders are paying for is contributing to the decline in 7(a) lending. As I stated in the hearing, the fees are the tipping point for many, compounding existing fees that are about to rise and market conditions that have diminished secondary market premiums and in other ways made the program less attractive to lenders.**

    a. **Have you reviewed the survey results by the National Association of Government Guaranteed Lenders (NAGGL), released the day before the**

hearing on January 29th, regarding the impact of the new lender oversight fees? If yes, what is your assessment? If no, why not?

Response: SBA has requested, but not received, the results of NAGGL's survey, so we are unable to comment on the overall results. However, NAGGL did provide SBA with a few survey highlights. While our observations are consistent with the finding that lending institutions have tightened their underwriting standards (at least based on the conclusion we were provided), we note that a smaller percentage of respondents had tightened underwriting of their SBA loans than of their conventional loans.

We also note that NAGGL indicated that nearly three-quarters of the lenders believed that the on-site review conducted by SBA duplicate the oversight of federal bank regulators. Unfortunately, SBA is unable to rely upon oversight provided by federal banking regulators for two reasons: first and foremost, the regulators have declined to provide SBA with copies of their lender examination results; second, it is our understanding that the regulators perform a very limited review of any government guaranteed loan portfolio, including lenders' portfolio of SBA guaranteed loans.

Finally, the results we were provided indicated that most of those surveyed did not see any value to SBA's off-site monitoring program. SBA has taken great strides to ensure that our lenders are given access to nearly all of the information used by SBA to monitor those lenders. However, as a regulator, it is critical that SBA maintain a loan and lender monitoring system in order to provide effective oversight of the nearly 5,000 lenders participating in our credit programs. SBA's monitoring system is a valuable tool in our risk management process.

b. **The SBA decided years ago to, for the most part, get out of the direct lending business and instead have the private-sector make the government-backed loans. The SBA was able to save substantial money by becoming a lender-oversight agency. If lender oversight is the SBA's role, why should the lenders pay for their examinations given that they have taken over the SBA's government function?**

Response: We disagree that SBA is exclusively a "lender-oversight agency;" SBA continues to process, service and liquidate loans, and reach out to lenders and small businesses in support of the role both parties play in driving the nation's economy. However, SBA recognizes that lenders have been delegated additional authority in the lending process. SBA believes that it is prudent to increase the level of oversight of lenders to ensure they are using that additional authority properly, and the on-site review process is a critical part of the oversight process. Charging 7(a) lenders for the cost of the reviews allows the agency a predictable level of resources to perform on-site reviews of enough lenders to ensure that the vast majority of loans guaranteed by SBA are originated, serviced, and liquidated properly.

c. Why shouldn't the SBA ask for the funding in its budget to cover those costs after realizing all these savings?

Response: In 2004, Congress provided SBA with the statutory authority to charge lenders for its lender oversight activities. SBA assumes that Congress provided this authority with the presumption that SBA would implement increased oversight activities - such as more extensive on-site reviews, off-site portfolio performance monitoring, and predictive modeling - and offset the cost through the oversight fee authority. SBA also recognizes that the budget process may be unpredictable, and the oversight fee provides the agency with the level of resources necessary to maintain this higher level of lender oversight.

6. In regard to the negative impact lender oversight fees are having on lender participation and loan volume, you argued that the agency was "doing a number of things...to bring down the cost for banks through all sorts of automation initiatives, initiatives to simplify interactions with them, initiatives to reduce their (banks) paperwork," things that "go far beyond the challenge with th[e lender oversight] fee." You were asked to provide the Committee with a quantifiable spreadsheet explaining how those changes leave the lenders ahead in their expenditures. Please provide the Committee with that chart.

Response: SBA has worked to provide lenders with the ability to make online processing and servicing actions, saving lenders both time and expense. Lenders now submit online applications over 75% of the time; three years ago, online submissions accounted for less than 50% of applications. SBA does not have detailed information about the actual savings to lenders that online transactions have produced, though lenders have provided the agency with positive feedback and individual accounts of cost and time savings. Providing a quantifiable estimate for these benefits requires a number of assumptions about processes and costs that vary from bank to bank. From feedback SBA has received, we estimate that at a per-unit level, submitting an application or cancellation or servicing action or through e-tran can save about 80% of the time and expense of a paper transaction.

Military Reservist Economic Injury Disaster Loan Program

1. At the hearing, we talked about the demand for the Military Reservist Economic Injury Disaster Loan (MREIDL) program. My staff has received the loan numbers for 2007. Please submit for the record the number of MREIDL loans that have been awarded in each year since 2000.

Fiscal Year	#	$
2000	N/A	
2001	N/A	

2002	47	$3,544,000
2003	77	$6,589,000
2004	73	$7,001,200
2005	43	$4,779,600
2006	27	$2,361,100
2007	20	$1,598,500
2008	4	$ 440,100

WBC PROGRAM RE-ENGINEERING PHASE II - FY2008

Scorecard Report: April 1, 2008		Returning Renewable Grants	Graduating Renewable Grants	Existing Initial & Sustainability Grantees
Project Kick-off	Wk of 9/20/07			
Establish Work teams	Wk of 9/24/07			
Conducted Rural WBC Focus Group	Wk of 10/22/07			
Conducted DOTR Focus Group	Wks of Nov 5,12,19, 2007			
Conducted WBC Director Focus Group	11/14/ 2007			
Pub. 3 Prog. Announc.		Wk of 12/17/07	Wk of 12/17/07	Wk of 12/17/07
Prog. Announc. Closed		January 24, 2008	January 24, 2008	January 24, 2008
HHS MOU cleared by SBA	Wk of 01/28/08 (Act. Wk of 02/04)			
Transition of grant/invoice process responsibility to OWBO	02/04/08			
Proposal Review Panels		Wk of 02/04/08	Wk of 02/04/08	
Prop. Budget Reviews		Wk of 02/11/08	Wk of 02/11/08	
Notice of Award to Grantees (4/1/08-9/29/08) Rvsd. 2/14[1]		Wk of 03/03/08 3/10/08	Wk of 03/03/08 3/10/08	
Grantee registration in HHS Payment Mgmt System		Wk of Feb 25, 2008	Wk of Feb 25, 2008	
Grantee Training for HHS System (Ready Talk & HHS)[2]Rvsd 3/4/08		(Wks of Mar 3 & Mar 10, 2008) Wks of Mar 10 and Mar 17	(Wks of Mar 3 & Mar 10, 2008) Wks of Mar 10 and Mar 17	
Request for Updated Work plans & Budgets (Existing) Rvsd. 3/4/08[3]				(Wk of Feb 25, 2008); Wk of March 17, 2008
Grantee Training for HHS System (Ready Talk & HHS)[4]				(Wks of Mar 17, 24, 31, 2008) Wks of Mar 10 and Mar 17
Work plan & Budget Approvals (Existing)				Wk of Mar 31, 2008
Work Plan & Budget review				Wks of Mar 31, June 2, 2008
DOTR Training				Wks of 04/1,7,14, 2008
WBC Secure Site on SBA website	April 1, 2008			
Conversion of all Grantees to HHS System	April 1, 2008			
Notice of Award (9/20/08 -9/29/09)				Wk of May 5, 2008
National Program Training Conference: WBC & DOTR Training	Wk of June 23, 2008			

[1] NOAs were delayed due to an unforeseen accounting system problem.
[2] These dates were revised to accommodate Trainers from HHS.
[3] This deadline was changed to March, as the priority was to get the returning centers and graduated centers under new NOA's and get centers registered and trained on the new HHS system. Prep for the HHS training took longer than expected, but will be delivered on time. There is no adverse effect by moving this date back.
[4] All centers in the program will be trained the weeks of March 10 and 17th; so this deadline has been accelerated.

4-01-08

Post-Hearing Questions for the Record
Submitted to Administrator Steven C. Preston
From Senator Joseph I. Lieberman

"Holding the Small Business Accountable: Women's Contracting and Lender Oversight"

January 30, 2008

1. **I am disappointed in the proposed rule that the SBA issued in December to implement the Women's Procurement Program (72 Fed. Reg. 73285, Dec. 27, 2007). The narrow methodology selected by the SBA, used to identify industries in which women-owned small businesses (WOSBs) are underrepresented in federal contracting, undermines the intent of the program, which is to expand opportunities in federal contracting to WOSBs. Will you commit to revisiting the rule?**

   Response: By definition, a "Proposed Rule" provides an opportunity for the public to submit comments on the rule. SBA provided an initial 60-day comment period and extended it an additional 35 days, allowing a total of 95 days for public comment. The SBA intends to review every comment and will consider changes in the Final Rule based on the comments.

2. **I am particularly concerned about the proposed rule's requirement – not required by the authorizing statute – that before an agency may award a contract under the program, it must conduct an analysis of the agency's past procurement activities and make a finding of past discrimination by that agency in the particular industry.**

   The proposed rule acknowledges that this program, as a gender-based program, is subject to the "intermediate scrutiny" that the Supreme Court articulated under <u>Craig v. Boren</u> , 429 U.S. 190 (1976), and later affirmed in <u>United States v. Virginia</u>, 518 U.S. 515 (1996). Under this test, the program must further an important government interest by means that are substantially related to serving that interest.

   Here, under what is an "intermediate scrutiny" test, the proposed agency-specific past discrimination test appears to impose requirements that go beyond what the Supreme Court has required under the more stringent "strict scrutiny" test for affirmative action programs based on race (requiring a program to be justified by a compelling government interest and narrowly tailored to achieve that interest). Even under the Supreme Court's test for "strict scrutiny," as most recently laid out in <u>Adarand Constructors, Inc. v. Pena</u>, 515 U.S. 200 (1995), federal affirmative action programs will be upheld if the programs respond to the practice and effects of discrimination in the relevant industry; the Court did not require a finding of discrimination by the agency itself.

   - **Can you point to anything in the Supreme Court's case law on "intermediate" scrutiny that would require an agency to make a finding of past discrimination by that agency? If this type of analysis is not**

required even under "strict scrutiny," why would you require it under a program that you acknowledge falls under "intermediate scrutiny"?

Response: The Department of Justice has advised SBA and testified before Congress that, under the intermediate scrutiny standard, courts are likely to strike down gender-based preference programs if the Government cannot show genuine and non-hypothetical evidence of discrimination in the specific economic sphere in which the program will operate. Based on this guidance, the proposed rule was drafted by SBA and reviewed by DOJ to withstand this judicial scrutiny.

- **As a practical matter, doesn't this part of your proposed rule gut the women's procurement program? Do you really expect that any agency will be willing to find itself guilty of past discrimination? Would not such a determination open an agency to all sorts of legal challenges?**

  Response: As in any proposed regulation affecting small business, the SBA's principal concern is drafting a regulation that will benefit small businesses and will withstand judicial scrutiny. Based on guidance received from the Dept. of Justice, this proposed rule was drafted to achieve those objectives.

- **How would this part of the rule be applied at DHS, which or course is a new agency where many programs are still being stood up? Is it your interpretation of the SBA's proposed rule that if an agency has no past practice to examine, the agency may not award a contract under the program?**

  Response: As you know, DHS is compromised of many smaller agencies that existed independently, or which were part of different departments, prior to DHS's creation. Therefore, by virtue of that history of the smaller agencies, DHS has past practice to examine.

3. **For several years, I have been a strong supporter of the Women's Business Center located in Stamford, Connecticut. We are fortunate to have a dynamic program in Stamford, providing a number of classes in entrepreneurial development and professional skills. After celebrating its 10th anniversary, the Stamford Women's Business Center has produced hundreds of success stories in Connecticut. Over 123,000 women own businesses in Connecticut, which amounts to well over one-third of all privately held firms in the state.**

   Given these statistics and the long history of a successful Women's Business Center in my home state, you can understand I want to make sure the processes to fund Women's Business Centers are working at optimal levels. I know that the Inspector General's November 2007 review of grant disbursements to Women's Business Centers had some constructive criticism of the program. There were ten recommendations in the IG report to ensure that grant funds are distributed in a

timely fashion. Administrator Preston, can you tell me if you have been able to put the wheels in motion to implement these recommendations? Are there any recommendations you feel you are unable to execute? If so, can you tell us why?

Response: Each of the ten recommendations from the IG has been reviewed and either favorable results have been achieved or favorable results are in process. None of the ten recommendations will go unaddressed.

4. **In addition to the November 2007 IG report, GAO also performed its own independent evaluation of the Women's Business Center program. GAO concluded that the SBA has not provided enough staff for adequate oversight of the Women's Business Center program. GAO described the staff resources for the WBCs as "limited." Have you addressed the issue of SBA staffing for the Women's Business Center program? If you still rely upon district staff to oversee the WBCs, have you provided them with adequate management training? Do you need additional staff in your district offices to keep up with oversight of Women's Business Centers?**

Response: The Office of Women's Business Ownership (OWBO) has completed an evaluation of the roles and responsibilities of the District Office Technical Representatives (DOTRs) in providing oversight and compliance activities for the WBC program. This evaluation comprised several activities:

- A total of four (4) hours of facilitated focus groups with all DOTRs to ascertain the aspects of their roles that were appropriate and able to be completed, and those areas that needed more definition, investment or additional training.

- A well-respected leader from the DOTR field group was brought into SBA's Central Office for 45 days to work in the WBC program office as a subject matter expert in the area of DOTR roles and responsibilities. She convened an advisory panel of DOTRs from across the country to make recommendations to the program leadership on areas for improvement, training and communication.

A newly constructed grant making and invoicing process for the WBC program is being implemented. The principal role of the DOTR will remain the same with primary focus on the mid-year and year-end site evaluations of the centers. However, the roles and responsibilities have been streamlined and clearly defined oversight procedures are being put in place to focus on critical, high risk areas.

The Office of Entrepreneurial Development will soon begin work with the Office of Field Operations, to whom the District Office DOTR employees report, to coordinate the formal revision to their roles and responsibilities and arrange for the appropriate training in these new areas.

Senator Mark Pryor
Small Business and Entrepreneurship Committee
Hearing on Women's Contracting and Lender Oversight
January 30, 2008
Questions for the Record

1. **Please describe the qualifications and training given to the Office of Credit Risk Management auditing teams? Do these teams ever include outsourced contractors as part of the field audits?**

   Response: On-site reviews are performed by a team of contract staff, with a senior examiner from SBA assigned to manage each review from SBA's offices. SBA senior examiners manage each on-site review via telephone; the examiners participate in the review entrance and exit conferences, and are also available as a resource throughout the entire review process should either the contractor staff or the lender/CDC staff have concerns or request guidance on particular issues. Senior examiners also manage SBA's lender oversight processes between on-site reviews, monitoring lender portfolio performance and ensuring that corrective actions are being taken by the lender to address performance problems.

   Review staff essential skills include: 1) knowledge of generally accepted and prudent commercial lending and credit processes - including credit underwriting, credit administration, liquidations and workouts, loan risk classification systems, and financial analysis, 2) knowledge of basic due diligence techniques, and 3) knowledge of government audit and lender or servicer review experience. Review staff are formally trained by SBA OCRM staff, in classroom style, at least annually. This is augmented by direct training from contractor management, and periodic conference calls to maintain proficiency and provide alerts to new or problematic subjects, as applicable. The contract project manager and OCRM's Contracting Officer Technical Representative (COTR) engage in a weekly conference call to ensure training needs are identified and addressed.

2. **Most lenders are using electronic imaging to store their documents. This is both a fast and reliable method of data storage. What instructions does the SBA give the auditors with respect to reviewing electronic files versus requiring that "paper files" be presented?**

   Response: SBA does not specify a storage media that lenders are required to use. SBA's on-site lender review teams have the capacity to review files in either electronic or paper format. However, to reduce the time, effort and cost of the review, SBA does recommend that the lender should have their files stored in a well-organized system with easy accessibility to the documents, regardless of whether the files are stored in paper format or electronically. An electronic system, if used should have some form of search or "find" resource, so that required documents can be easily and quickly identified. Lenders are also instructed to make available terminal or computer access for every reviewer on the review team to facilitate efficient review activities.

3. **The SBA audits are intended to monitor lending risk. Are the auditors required to review individual lender's internal lending policies and internal controls, some of which may be confidential?**

Response: One of the required elements of SBA's risk-based, on-site reviews of SBA lenders is a review and analysis of the lender's operational policies, procedures and internal controls. The review team evaluates these policies, procedures and internal controls to determine the adequacy of those controls, and will issue a finding if the policies and procedures are determined to be inadequate. Any findings, including findings regarding the policies, procedures and internal controls, are included in a final review report provided to the lender with the expectation that the lender will take action to correct the finding.

SBA is sensitive to the need to retain the confidential nature of lenders' proprietary or sensitive information. Therefore, SBA's review report is also considered confidential. To retain the confidentiality of the review report and the information contained therein, each report is flagged with the following cover page alert:

THIS REPORT IS STRICTLY CONFIDENTIAL

This copy of the Report is the property of the U.S. Small Business Administration, Office of Credit Risk Management, and is furnished for the confidential use of the examined entity. Under no circumstances shall any recipient of this report or its parent company, or any of their directors, officers, employees, attorneys or auditors disclose or make public this report or any portion thereof. Unauthorized disclosure of any of the contents of this report is subject to the penalties in 18 USC 641. The Office of Credit Risk Management must be notified immediately if the examined entity receives a subpoena or other legal process calling for the production of this report.

4. **The SBA stresses the objective of increased lending to underserved markets. Such loans will exhibit a higher degree of risk, default and loss rate. How does SBA's practice of incorporating credit scores in its risk analysis, and rating lenders on their risk score, affect SBA's stated intent to increase lending to underserved markets?**

Response: The loan credit score and lender risk rating systems assist SBA in focusing its oversight efforts on those among our nearly 5000 7(a) and 504 lenders most in need of monitoring. Through the risk rating system, SBA is able to compare each lender's portfolio performance against its peers using a uniform rating scale similar to those used by other federal financial regulators. However, SBA does not use its credit scoring or risk ratings as the sole basis to determine whether a particular lender's portfolio is creating undue risk to the agency. Instead, SBA uses the risk ratings as a first step towards understanding whether a lender's portfolio performance issues are a result of poor underwriting or credit decisions by the lender, or are a reflection of the market within which the lender's activity is focused. If SBA determines that the lender is actively engaged in lending to underserved markets in support of SBA's goals and mission, and that the lender's performance is comparatively worse than its peers due to its lending efforts in underserved markets, the agency would take such a factor into careful consideration in its oversight of that lender.

Senator Olympia J. Snowe
Follow-Up Questions for the Record
"Holding the Small Business Administration Accountable: Women's Contracting and Lender Oversight."

Women's Contracting:

1. **Please explain how the Small Business Administration's (SBA's) proposed rule for the women-owned small business contracting program will help to achieve the government-wide contracting goal of 5 percent for women-owned small businesses? Wouldn't it be advantageous to include more industry categories to achieve this goaling requirement rather than less? Why or why not?**

   Response: The statutory 5 percent goal is expressed in dollars. Thus, the rule is consistent with the statute. Moreover, although the Government has made substantial progress in achieving the statutory 5 percent goal, we believe that the set-aside program in the proposed regulations constitutes an additional tool in ensuring greater participation of women-owned small businesses in the Federal arena. However, we recognize that we must abide by the standards of intermediate scrutiny established by the judiciary for gender-based affirmative action programs. The standards set forth for intermediate scrutiny require that the remedy be substantially related to achieve important Governmental objectives. Based on advice from the Department of Justice, the proposed rule was drafted to satisfy this standard.

2. **What is the likelihood that any agency, like the Department of Defense (DoD), Department of Energy (DoE), or even the SBA, would publicly admit to a history of discriminating against women-owned small businesses, as SBA's rule requires? Since the Department of Justice (DoJ) has approved this unrealistic requirement, isn't it possible that there is a less burdensome alternative? Did the SBA consider any alternatives before publishing this proposed rule? Why or why not?**

   Response: In an earlier Proposed Rule published on June 15, 2006, the SBA did not propose an agency determination of discrimination. However, after further discussion with the Dept. of Justice, it was believed that the inclusion of this provision was appropriate to withstand possible future legal challenges to the proposed set-aside mechanism. Accordingly, the provision was added to the Proposed Rule that was published on December 27, 2007.

3. **In Fiscal Year 2006, roughly 50 procuring federal agencies failed to meet the women's small business statutory goal of 5 percent, including the DoD, which awarded less than 2.93 percent of over $234 billion eligible small business procurement dollars. What is the SBA doing to help agencies like DoD, which has not met their procurement goals for other vital programs like the service-disabled veteran-owned small business procurement program, to meet their 5 percent goal for women-owned small businesses?**

Response: Through its network of Procurement Center Representatives (PCRs), the SBA advocates various set-asides for small business, service-disabled veteran-owned small business, and other socio-economic groups for which set-asides are authorized. When the set-aside mechanism for WOSBs is implemented, SBA's PCRs will encourage contracting officers to use it, when appropriate, along with the other set-aside mechanisms. The PCRs also conduct Surveillance Reviews of Federal buying activities, including DOD buying activities, to ensure that they are providing maximum practicable opportunity to small business, including WOSBs. In FY 2007, SBA developed and implemented a Quick Market Search that enables contracting officers to quickly identify WOSBs and other targeted socio-economic groups when they conduct market research. Lastly, SBA's PCRs and other employees conduct training for other Federal agencies throughout the year, as needed, and participate in numerous outreach events, many of which are targeted to WOSBs.

SBA Lender Oversight:

1. **Regarding lender oversight, one of the biggest complaints lenders have is that the SBA dismisses their concerns and does not sufficiently involve them in the planning and decision-making process. What can be done to open the lines of communication between the SBA and the lending communities? Is there a way to air grievances, and discuss concerns on both sides so that the SBA lenders and the SBA can work together to solve problems, and plan for the future of the program?**

   Response: SBA is committed to maintaining open communication with its lending community on lender oversight issues. SBA staff regularly attend conferences held by the trade associations, both to meet with and talk to individual lenders and to make presentations to the lending community on topics we believe lenders consider important. For example, SBA staff have made (and continue to make) several presentations on a comprehensive overview of the lender on-site review process. We made several presentations to the leadership of the trade associations to educate them on the development of the Loan and Lender Monitoring System prior to its formal implementation in 2006-07, and we also discussed the system and our risk rating process to the membership of those trade associations throughout 2006 and 2007.

   We also notified NAGGL's membership of the proposed lender review fee at the association's national conference in 2006, and urged the members to provide us with comments regarding that rule. And when we received comments on the proposed fee, we carefully reviewed the concerns that were expressed. One of the more frequent comments we received concerned the potential impact of the off-site fee on small lenders, and whether that fee might result in smaller lenders leaving the 7(a) program. After considering the costs and benefits of charging off-site fees to smaller lenders, and the merits of the concerns raised by the lending community, we established a minimum threshold for the fee, and as a result more than 80% of all 7(a) lenders are not subject to an off-site review fee.

   However, while we recognize that trade association conferences allow us to reach the widest possible audience, we are also focused on communicating in other ways. For example, SBA senior management meets one-on-one with individual lenders as well as the leadership of the trade associations. Recently, agency representatives met with NAGGL leaders on the oversight issue, and actively participated in sessions with the Board and other members of NADCO regarding the status of SBA's 504 portfolio along with other oversight-related issues. SBA also holds lender roundtable discussions throughout the country, soliciting lender comments on any issues of concern regarding SBA's loan programs – including lender oversight.

Finally, SBA uses its front line district offices to communicate with our lenders. Not only do the district offices help raise lenders' awareness of our oversight activities, but they also play a vital role in planning teleconferences where SBA oversight staff can make presentations to, and obtain feedback from, smaller groups of lenders.

SBA uses all of these channels of communication to publicize its oversight activities and to solicit feedback from the lending community on their concerns with SBA's oversight proposals. And we continue to look for other ways to reach out to our lending community, both to educate them on the need for lender oversight and to listen to their ideas for a balanced level of oversight.

2. **The American Banker recently reported that at the SBA State of the Agency speech on January 22, 2008, Administrator Preston explained that the SBA's loan volume has dropped by roughly 3,000 loans in comparison to the previous September through December quarter. In the SBA's explanation of this decline, Administrator Preston acknowledged that banks, which have automated their systems, find the SBA's non-automated lending programs outdated. What is the SBA doing to automate its loan underwriting processes so that small businesses are not turned down for loans because lenders find it difficult to work with the SBA's "outdated" loan systems?**

   Response: Many SBA Express and PLP lenders use the E-tran lender interface to obtain loan approvals via an internet system that operates twenty-four hours per day, seven days per week. This system uses a series of drop down menus and fillable blanks to guide a lender through the process to obtain a loan number. There is also a servicing module in E-tran. This permits lenders to complete certain servicing actions rapidly on a 24-7-365 basis.

3. **According to the American Banker, over the last two years 368 lenders have left the SBA's lending programs. What are the factors that are driving these banks out of SBA lending and what is the SBA doing to address these factors?**

   Response: SBA has not performed an analysis of the factors resulting in the net decrease in active 7(a) lenders from FY2005 to FY2007. We believe that a major factor in the decline in active lenders is likely the continued consolidation in the banking industry, which is reflected in data on bank charters maintained by the FDIC. The FDIC has reported that there were 244 fewer commercial banks and 56 fewer savings institutions in FY2007 than in FY2005. Over that three year period, more than 850 commercial banks and 115 savings institutions merged; it is quite likely that many of those institutions were SBA lenders.

However, SBA has adopted a proactive response to address the decline in lender participation. We have stepped up our efforts to reach out to new or inactive lenders, to develop relationships with those lenders, explain the benefits of SBA's lending programs, and provide training to educate those lenders so they can be prepared to develop their SBA lending business and assist small business owners unable to meet their credit needs elsewhere. For example, for Fiscal Years 2007 and 2006, SBA approved a number of credit unions as new participating lenders. SBA also rolled out its pilot Small Rural Lender Advantage program to address the needs of small, rural lenders lacking the sophisticated SBA lending operations of our larger lenders. Small Rural Lender Advantage allows those small lenders to become active SBA lenders without the need to invest in the development of back office operations, by offering timely loan processing by SBA's service centers. We believe Small Rural Lender Advantage will attract small, community-based financial institutions to SBA's products and increase the number of SBA lending partners.

4. **What has the SBA done since the November 2007 Small Business Committee hearing on lender oversight to increase the accountability of preferred lenders? Would it make sense for the SBA to have more flexibility with the preferred lender status so that if a national lender has one branch that is making bad loans the SBA could revoke that branch's PLP without revoking the lender's entire national preferred lender status?**

   Response: The most important step that SBA has taken to hold all lenders more accountable has been to publish its proposed lender oversight regulations, which were published just prior to the hearing in November. These regulations propose a comprehensive lender oversight strategy that provides a consistent level of regulatory oversight for any type of lender (e.g., federally regulated financial institution, non-federally regulated lender, or Small Business Lending Company regulated exclusively by SBA). The regulations also propose a balanced approach to the agency's enforcement activity that will hold any type of lender accountable for problems with their portfolio or the management of their SBA operations. In keeping with our dedication to open dialogue with our lending community, SBA continues to educate lenders on this proposal and solicit their comments on the regulations. SBA believes that the final implementation of these regulations will be yet another significant improvement to the agency's lender oversight process.

   SBA does not believe that the revocation of preferred lender status for a particular branch would be an effective way to increase lender accountability, because we are concerned that such a policy would be difficult to enforce. For example, if SBA revoked the preferred lender status for a particular branch office, the lender could simply submit the loans through another branch office, or through a central office. The lender could also close the branch office and open another branch in a nearby location that would not be subject to the revocation of preferred lender status. Finally, the lender could transfer its originators from the branch with revoked preferred status to other offices. In any of these cases, SBA would simply be turning a problem affecting one office into a lender-wide problem requiring enforcement action to eliminate the problem.

5. **Currently, many lenders argue that SBA lender oversight fees are increasing at the same time the credit crunch is decreasing lenders' profitability and small businesses owners demand for loans. What will be the effect of the lender oversight fees that are to be charged later this year on total lender participation in the 7(a) program?**

   Response: SBA believes that the overall effect of the lender oversight fee will not be enough to affect lenders' decision to participate in the 7(a) program. Although the FY2008 off-site review fee has not yet been determined, the off-site review fee billed in 2007 was at a rate of $73 for every $1 million in SBA guarantee dollars outstanding, or less than 1 basis point. Since the fee is based solely on the SBA-guaranteed portion of the loans, the affect of the off-site fee is further minimized. For example, if a lender's portfolio consists entirely of SBA*Express* loans, the lender's off-site fee would apply to only 50% of the total loan amount. In addition, thousands of small lenders will pay no fee whatsoever; the fee will be paid by those lenders that derive the greatest benefit from the 7(a) program through the increased liquidity and government guarantee provided by SBA. In conversations with the lending community, it has been apparent that other factors, including premiums received for loans sold to secondary market investors and the effect of interest rates on loan demand, are far more critical determinants of lenders' decisions regarding their SBA lending efforts.

   SBA recognizes that the fee associated with on-site reviews may have a disproportionately greater impact upon small lenders subject to on-site reviews. We are looking at ways to minimize the impact of that fee for smaller lenders.

6. **Does the SBA anticipate that a large number of lenders will stop making SBA loans because of these fees? Why or why not?**

   Response: SBA does not believe that lenders will discontinue their participation in the 7(a) program due to the oversight fees. As noted above, lenders have expressed their opinion that other factors such as the effect of interest rates on loan demand and the amount of premiums received for loans sold to secondary market investors will have the greatest impact in their decisions regarding SBA lending.

7. **What will the SBA do if a combination of negative economic factors and increasing lender oversight fees drive a large percentage of lenders out of the program?**
   Response: SBA has already taken steps to develop a nationwide marketing plan to increase lender participation in the 7(a) program. The agency's marketing plan will use both headquarters and district office staff to reach out to our current lending customers, as well as potential new customers. The marketing strategy will include educating lenders on the benefits of the 7(a) program, providing training tailored to the customer's needs, and managing customer relationships through a coordinated communication process across the agency.

   We believe that SBA's guarantee programs are most critical – and most important - during times of uncertainty in the nation's credit markets. SBA provides lenders increased liquidity and reduced risk through our government guaranty. Our strategy will take that message to lenders, and show them how to use our credit programs to continue providing needed access to capital for small businesses, even during the current challenges in our credit markets.

8. **How will the SBA fulfill its mission of providing loans to small businesses that can't obtain "credit elsewhere" if lenders are discouraged from making SBA guaranteed loans because SBA systems are both "outdated" and costly?**

   Response: SBA is working to update its lender interface systems. Many SBA Express and PLP lenders use the E-tran lender interface to obtain loan approvals via an internet system that operates twenty-four hours per day, seven days per week. This system uses a series of drop down menus and fillable blanks to guide a lender through the process to obtain a loan number. There is also a servicing module in E-tran. This permits lenders to complete certain servicing actions rapidly on a 24-7-365 basis.

9. **It has been reported that the staff at the Herndon Processing Center recently went through an employee training process that included redesigning how processes work at the center. What specifically did the SBA do at Herndon and how will these actions help small business borrowers?**

   Response: The Herndon National Guaranty Purchase Center undertook a Lean Six Sigma process reengineering of the entire 7(a) loan guaranty purchase process. The purchase process was made more effective and efficient for SBA's operations, and more accountable and transparent to maintain proper control and oversight. These improvements will increase purchase review quality while reducing purchase review variation, processing time, and expense for SBA's lending partners, thereby reducing their administrative costs of participating in the program. The improvements will also help "level the playing field" for lenders, thereby fostering competition. SBA believes that the reduced cost and increased competition will significantly benefit the small business borrower through lower lender fees and rates, and increase lender incentives to attract the small business borrower in a competitive market.

10. **The SBA states that it has developed a lender monitoring and risk management system that provides the SBA with the capability to conduct the type of monitoring and analyses typical among major lenders and recommended by financial regulators. Please provide information about the major lenders that are using a similar system and which financial regulators recommended similar systems?**

   Response: SBA believes that it's Loan and Lender Monitoring System (L/LMS) is a sound loan monitoring and risk management system similar to those used by both major lenders and other government agencies, and independent examiners agree. L/LMS has been recognized by both SBA's Inspector General (OIG) and the General Accountability Office (GAO) as a loan monitoring and analysis system typical of industry best practices. GAO has stated that "the loan monitoring service SBA obtained under contract from Dun & Bradstreet includes an infrastructure that appears to be on par with best practices, including a strong management information system, quality data, and human capital." SBA's OIG noted that "the Dun & Bradstreet service provides SBA with the capability to conduct the type of monitoring and analyses typical among major lenders and recommended by financial regulators. The L/LMS rating system is also both on par with industry best practices and based on sound financial models."

Due to the competitive nature of the credit modeling industry, and confidentiality agreements with its clients, Dun & Bradstreet is unable to share with SBA a list of its lender clients. However, approximately half of the 60 largest lenders in the 7(a) program use some form of a Dun & Bradstreet/Fair, Isaac credit modeling system either as part of their loan originations or for credit scoring. Most of those lenders use systems similar to SBA for similar purposes.

In discussions with federal financial regulators, those regulators have indicated that their risk management systems have been predominantly developed in-house, using expertise developed over many years. SBA does not have the expertise or the experience to internally develop its own risk rating systems, so it has used commercially available off-the-shelf models that have been created, refined, and tested by professionals with substantial risk management modeling experience.

Additional Issues:

1. **The FY 2008 Omnibus bill provided $13 million worth of funding to Women's Business Centers (WBCs). Will the SBA be able to open any new centers under this funding level? Why or why not? Does the SBA plan to increase their funding request for WBCs in FY 2009 in order to open more new centers?**

   Response: No new centers are being funded for FY 2008 or FY 2009 due to the fact that the 2007 legislation allows graduated centers to return to the program and gives priority funding to these centers. In addition, the returning centers had to be funded for 18 months of operations with FY 2008 monies, meaning they will be funded for half of FY 2008 and all of FY 2009 from the FY08 appropriation.

   The Agency has asked for funding consistent with last year's appropriation. The SBA wishes to maintain a level of predictability for those already in the program.

2. **Does the SBA believe targeted, timely, and fiscally responsible proposals to implement tax credits to spur small business investment, resolve the crisis in small business health insurance, improve access to capital, promote small business contracting, and bolstering SBA's economic development programs are the appropriate areas in which Congress should be targeting its efforts to help the economy recover from its current slowdown? What specific proposals would you advocate in these areas?**

   Response: We believe that the current stimulus provided by the Federal Reserve of reducing the discount rate, coupled with the passage of the Economic Stimulus Package of 2008 will stimulate the economy sufficiently. We just need to wait for the reduction in the discount rate and the economic stimulus package to take effect fully. We are already seeing some signs of improving economic activity. For example, in the week ending

April 19, the advance figure for seasonally adjusted initial unemployment claims was 342,000, a decrease of 33,000 from the previous week's revised figure of 375,000. Moreover, The Dow Jones Industrial Average shot past 13,000 for the first time this year, powered by better-than-expected corporate earnings that boosted investors' confidence in the U.S. economy. The application of any more stimulus to the economy at this time could result in higher inflation to the detriment of economic growth.

We believe that reigning in health care costs and reducing of trade barriers are the initiatives for improving our economic outlook for small businesses. Health care consumed about 16 percent of our gross domestic product in 2007, and is projected to grow to 20 percent by 2016. This compares to less than 11 percent for such countries as Switzerland, Germany, Canada and France. The relatively high cost not only affects the availability of health care but also the ability of American small businesses to compete domestically and internationally. Either small businesses are not able to provide health care insurance to their employees because of the high costs or when they do, they may put their business at a competitive disadvantage. We believe by making price and quality information more readily available to consumers along with perhaps re-structuring how health care is paid, significant progress can be made in reigning in spiraling health care costs and thus making health care more affordable and available.

Trade has been a significant contributor to our economic growth. Over 40 percent of our growth in GDP was the result of trade and 29 percent of the trade value was generated by small businesses (businesses with less than 500 employees). We would advocate that Congress take the necessary actions to help the economy by passing the U.S.-Colombia Free Trade Agreement. Small business will benefit once Congress passes this crucial legislation since more than 9,000 U.S. companies export to Colombia, of which nearly 8,000 are small and medium-sized firms. The U.S. International Trade Commission has estimated that U.S. exports to Colombia will be $1.1 billion higher once the U.S.-Colombia Free Trade Agreement is fully implemented. This would mean an anticipated increase in exports of $385 million for small businesses if Congress approves the U.S.-Colombia Free Trade Agreement.

It is important to note the recent actions SBA has taken actions to help improve access to capital and contracting opportunities. First, SBA has introduced a new program called SBA Emerging 200. The goal of the SBA Emerging 200 initiative is to identify 200 initiative will enable the participating small businesses to engage in an intensive curriculum focused on developing a winning, expansion strategy for their business, including options for capital access and contracting. Along with SBA's Rural Lender Advantage Initiative, we reaffirm our commitment to reaching out to the underserved markets.

3. **In looking back at the SBA's response to the Gulf Coast Disasters, the local Small Business Development Centers (SBDCs) in the impacted region received no monies from the SBA to hire the counseling staff they needed immediately following the disaster. What is the SBA's view on the role of SBDCs in the immediate aftermath of a disaster? Also, will the SBA ensure that SBDCs are fully utilized immediately following any future disasters?**

Response: The statute doesn't directly provide any direction as to what SBDCs should do or not do in the case of a disaster. Therefore, SBDCs have, as a practice, responded to disasters in their states with existing resources, providing counseling services. These services include counseling to victims applying for SBA disaster loans and general business technical assistance and advice on continuation or sustainability during and after the crisis.

Also, in SBA's disaster recovery plan, which was submitted to Congress, during Level I – Level IV responses, SBA leverages SBDCs, SCORE, and Women-Owned Business Centers (WBCs), as needed. In the case of a Level III or Level IV response the SBA plans to engage resource partners in an official capacity if and only if the surge resources available through the Office of Disaster Assistance are insufficient. These groups primarily help with local outreach:

- Making potential applicants aware of SBA's services and handing out disaster loan applications;
- Screening and interviewing – helping applicants complete documents, reconstruct their financial picture and collect requisite background information.
- Providing additional recovery, crisis management and business development counseling as identified by the individual clients

4. **The Committee last June unanimously passed the Small Business Venture Capital Act of 2007 (S. 1662), which would reauthorize the Small Business Investment Company (SBIC) program through 2010. Since its inception in 1958, the SBIC program has done a remarkable job in helping small businesses meet their requirements for growth and operating capital not available through banks or other private capital sources. Indeed, over the last 50 years, SBICs provided approximately $48 billion of long-term debt and equity capital to more than 100,000 small enterprises, with $2.9 billion invested in 2,121 small firms in FY 2006 alone. Does the Administration believe the SBIC Debentures program is effective and worth reauthorizing? Why or why not? Please provide the Committee with any recommendations the SBA may have to improve the program.**

Response: The Administration supports the debenture program and has proposed an authorization of $3 billion in the FY 2009 budget. A recent study conducted by the Urban Institute indicated that the debenture program is not duplicative and helps address gaps in certain areas not well served by the private venture capital industry. The debenture program is more diverse geographically, has a broader industrial base, reaches smaller businesses and provides a significant portion of its funding to low or moderate income areas. In addition, as evidenced by the FY 2009 budget cost re-estimates, the debenture program provides these benefits while continuing to operate well within zero subsidy cost.

We believe the program is well-designed although the Agency continues to explore changes that make it more attractive to private investors and seasoned fund managers.

United States Senate
COMMITTEE ON SMALL BUSINESS & ENTREPRENEURSHIP
WASHINGTON, DC 20510-6350

December 5, 2007

VIA FACSIMILE & FIRST-CLASS MAIL

The Honorable Steven C. Preston
Administrator
U.S. Small Business Administration
409 Third Street, SW, Room 7000
Washington, DC 20416

Dear Administrator Preston:

On September 20th, 2007, the Senate Committee on Small Business and Entrepreneurship held a hearing on key women's small business programs where we questioned your Associate Administrator for Entrepreneurial Development, Anoop Prakash, extensively on the implementation of legislation making permanent funding available to established Women's Business Centers. During this hearing, Mr. Prakash indicated that the Small Business Administration would implement the Women's Business Centers legislation by not later than January 18, 2008. Following Mr. Prakash's response, we indicated that we would be calling a hearing in order to review the status of this and other programs in 120 days.

As discussed at the November 13th Small Business and Entrepreneurship Committee hearing on lender oversight, which you personally attended, we emphasized how crucial it would be to have you return before the Committee to report on the various oversight issues that were discussed during that hearing. Therefore, the Committee will be holding a hearing, most likely the week of January 21st or January 28th, 2008, to learn of the SBA's progress in implementing the Women's Business Centers legislation, as well as other issues that the Committee has raised in prior oversight hearings this year. The hearing issues may include, but are not limited to:

- Contracting matters, including the final implementation of the Women's Contracting Set-Aside program;
- Completion of small business requirements as mandated by the Energy Policy Act of 2005, including the establishment of a government-wide energy "clearinghouse;"
- The SBA working with the U.S. Department of Health and Human Services (HHS) to promote the State Children's Health Insurance (SCHIP) program;
- Funding of non-credit programs;
- Improving SBA staffing shortages and budgetary issues;

- Improving the Small Disadvantaged Business, 8(a) and HUBZone programs by updating regulatory changes and contracting issues;
- Improving the Agency's disaster lending oversight capabilities;
- Meeting small business contracting procurement target goals;
- Servicing contracts for the 7(a) and 504 loan programs; and
- Improvements to and resources for SBA lender oversight and fraud prevention.

Thank you in advance for your responses on the above issues. We would like to confirm a date for the hearing as soon as possible. Please have a member of your staff work with our staff on this matter. We look forward to establishing a firm date and hearing your testimony on these vital issues.

Sincerely,

John F. Kerry
Chairman

Olympia J. Snowe
Ranking Member

Naomi and Wally,

Below are the responses for the questions raised in the letter of December 5, 2007. I apologize for the delay. You should also get the QFRs from Anoop Prakash by Wednesday.

Regarding some of the issues below, I would like to point out that I believe a number of these questions have been answered previously either formally or informally. That often adds to our confusion here when, having answered a question in one context, we receive it again. That initiates a scramble on our part to understand what wasn't answered before.

At any rate, I believe between the QFRs from the BLX hearing, the July Procurement hearing, the September Women's Business Center hearing and the information below and in the attachments we should have covered everything.

CONTRACTING MATTERS INCLUDING THE WOMEN'S BUSINESS SET-ASIDE

- **Women's Procurement Program**
  SBA is moving forward with implementation of the Women's Procurement Program. On December 27, 2007 SBA published a proposed rule for implementation of a Women-Owned Small Business contracting program. It is currently under the sixty day public comment period until Feb. 25, 2008.

- **CCR improvements and updates**
  We will be sending a copy of a March 2, 2007 letter to the committee which explained the improvements that are on going to the CCR, Mentor-Protégé and bundling practices.

- **GAO recommendations**
  Since 2000 SBA government contracting has been the subject of 5 GAO reports. Those reports produced 15 recommendations. One report and its recommendations are closed. Of the remaining four (4) open reports:

  i. **GAO 06-399: Increased Use of Alaska Native Corporations' Special 8(a) Provisions Calls for Tailored Oversight—10 recommendations.**
     SBA has sent a status letter regarding our actions on the recommendations (attached). GAO has not yet closed any of the recommendations.

ii. **GAO 04-454: Impact of Strategy to Mitigate Effects of Contract Bundling on Small Business is Uncertain: 1 recommendation**

Recommendation: "The Administrator should expedite the dissemination of best practices to maximize small business contract opportunities for incorporation into agencies' training courses, as required by the OFPP strategy."

Status: The Best Practices guide was published in February 2007, and SBA posted a link to the Best Practices guide on our website.

iii. **GAO 02-166: Small Business Subcontracting Report Validation Can Be Improved—1 recommendation**

This recommendation is contingent on both SBA and DOD. DOD will not implement its portion until April 1, 2008. This recommendation will remain open until DOD completes its portion.

iv. **GAO 01-346: Trends and Challenges in Contracting With Women-Owned Small Businesses— 1 recommendation**

This recommendation was completed and closed.

v. **RCED-00-19: SBA Could Better Focus its 8(a) Program to Help Firms Obtain Contracts—2 recommendations**

SBA's previous (2001) response was not sufficient to close out the recommendations. An update will be provided

Recommendation: SBA should periodically perform a nationwide sample survey of 8(a) firms to obtain measurable program data. At a minimum, the survey should assess whether SBA assistance is meeting the firms' expectations and needs.

Status: SBA officials continue to agree that the best way to assess whether the 8(a) program is meeting the needs of participants is through a nationwide survey. SBA has developed a survey but it has not been launched.

COMPLETION OF THE SMALL BUSINESS REQUIREMENTS AS MANDATED BY THE ENERGY POLICY ACT OF 2005

While SBA has undertaken compliance with the required sections of the Energy Policy Act of 2005 through the establishment of a website linked to SBA's main webpage, the recent enactment of the Energy Efficiency Act of 2007 has required a complete and thorough re-evaluation of that action and the implementation of the new requirements. We look forward to fulfilling the implementation of the new mandate within the statutorily dictated 90 days. The website can be found at http://www.sba.gov/energystar/index.html, or at the bottom right hand corner of sba.gov, by clicking on the Energy Star tab.

SBA WORKING WITH THE US DEPARTMENT OF HEALTH AND HUMAN SERVICES TO PROMOTE SCHIP

In accordance with Senator Kerry's request the SBA established a link on its website to the HHS SCHIP homepage.

IMPROVING SBA STAFFING SHORTAGES AND BUDGETARY ISSUES

The FY 2008 Budget Request supported 2,123 employees. The agency plans to add 62 employees during the year and reach that level. That includes 9 new Procurement Center Representatives, new 7(a) and 504 loan processing staff, and staff for understaffed district offices. SBA has already been working to fill these positions and the process will continue throughout the year now that the FY 2008 Omnibus has gone into effect.

In Herndon SBA has increased staffing to approximately 82 employees and plans to bring on an additional 20 short term employees to assist in eliminating the processing backlog. Afterwards, staffing will return to approximately 82 employees depending on demand.

In Sacramento SBA has resumed processing according to planned goals and is also adding an additional 3- 4 employees. SBA has also identified seasonal workload pressures and is working to adapt the E-Tran electronic application processing system for use in the 504 program. This will help streamline application processing.

NON-CREDIT PROGRAMS

Non-Credit FY 2007

(Dollars in thousands)

Non-Credit Program	FY2007
Nat'l Women's Bus. Council	$740,421
Veterans Outreach	740,421
7(j) Technical Assistance	1,480,842
SBDCs	87,863,292
Drug-Free Workplace	987,228
SCORE Program	4,936,140
Native American Outreach	987,228
Women's Business Centers	12,340,350
Microloan Technical Assistance	12,833,964
PRIME Technical Assistance	1,974,456
Total	**$124,884,342**

41% of the WBC funding was applied to sustainability.

The National Veterans Business Development Corporation is no longer funded through the SBA; it is a separate appropriations account.

IMROVING THE SMALL DISADVANTAGED BUSINESS, 8(a) AND HUBZONE PROGRAMS BY UPDATING REGULATORY CHANGES AND CONTRACTING ISSUES

SBA is exploring a number of changes in order to clarify the regulation governing the 8(a) Business Development and Small Disadvantaged Business (SDB) programs. Some of the suggested changes involve technical issues such as changing the term "SIC code" to NAIC code" to reflect the national conversion to the North American Industry Classification System. In addition, SBA is planning on making two changes to the size regulation in order to clarify concerns regarding mentors and protégés.

SBA is drafting proposed regulatory changes to the 8(a) Program to improve oversight and address any actual or perceived opportunities for misuse. In order to amend the 8(A) ANC SBA conducted two tribal consultations in Denver and Alaska. These meetings allowed SBA to consult with Native American and Alaskan Native tribes in accordance with Executive Order 13175.

MEETING SMALL BUSINESS PROCUREMENT TARGET GOALS

SBA publishes an annual small business goaling report that reflects agencies performance against small business contracting goals. The FY06 performance was published in July 2007 and we anticipate publishing the 2007 report in mid 2008.

The small business procurement scorecard was initiated this past year. It evaluates quantitative and qualitative performance of small business progress of the 24 federal agencies covered by the Chief Financial Officers Act. The first semi-annual report was published in July 2007. The second semi-annual report will be published shortly updating agencies' current FY progress in small business procurement.

- SBA has implemented a new web tool called the Quick Market Search, to allow procurement officials to easily find eligible small businesses during their market research.
- SBA has reoriented field staff to focus on outreach, training and counseling businesses so that they are prepared to enter the Federal Marketplace. We have provided additional training to the field to increase their ability to provide assistance to small businesses.
- The field staff has significantly increased the number of anticipated outreach events, including matchmaking sessions. Anticipated events total more than 300.
- SBA has re-oriented Procurement Center Representatives (PCRs) to work primarily with the procuring offices to help agencies meet their procurement goals.
- SBA is hiring more Procurement Center Representatives (PCRs). SBA has 53 PCRs on board and will be hiring eight more PCRs in the next 90 days. SBA will continue hiring PCRs this year with the goal of increasing PCRs to 66 in FY08.

CONTRACTS FOR 7(a) AND 504 SERVICING.

The 504 solicitation was issued on April 2, 2007. The contract was awarded on July 25, 2007. Colson Services was the awardee. The contract term is for 5 years.

The 7(a) solicitation was issued on May 14, 2007. The contract was awarded to Retirement Services Group on Nov 30, 2007. The contract term was 5 years.

SBA has just received a protest from the incumbent, Colson, who lost the 7(a) contract. SBA is therefore forced to extend the 7(a) contract until the protest is resolved by the GAO Board of Contract Appeals. (Estimate 90 days)

IMPROVEMENTS TO AND RESOURCES FOR SBA LENDER OVERSIGHT AND FRAUD PREVENTION

Staffing Issues
As mentioned above staffing at the Herndon and Sacramento processing centers has increased significantly.

IG reports and recommendations
Attached please find a chart describing the recommendations and actions taken in response to them. We would be happy to provide a briefing to discuss them in depth.

PLP Lender Status
With respect to the 6 to 7% of PLP lenders that had their PLP status revoked by SBA, we should clarify that the percentage figure cited in our testimony included non-renewals of both PLP and SBA*Express* status, both of which are delegated lending authorities subject to approval/renewal by SBA. Lenders often apply for both PLP and SBA*Express* delegated lending authority, and SBA will simultaneously review the Lender to determine whether they should be approved for the PLP and SBA*Express* programs.

In FY2007, SBA denied a total of 86 PLP and/or Express applications, or 6.2 percent out of a total of 1,398 applications. Of those 86:
44 were denied primarily due to unsatisfactory performance or performance-related issues,
26 were denied primarily due to enforcement actions imposed by the lender's regulator, i.e. an FDIC action and,
16 were denied primarily due to a lack of loan volume. None of the lenders included on this list <u>voluntarily</u> withdrew their request for PLP and/or Express authority.

Prior to FY2007, SBA did not systematically track and retain the information requested.

Audit Title	Audit Report #	Rec #	Recommendation	Management Response	Issued Date
Survey of The Quality Assurance Review Process	6-26	1	Recommend the AA/OFA determine the level of staffing needed to fully implement all aspects of the QA plan to ensure the QAR process effectively identifies improper purchases and areas of the purchase process needing improvement,	OFA is in the midst of a comprehensive re-engineering review of the National Guarnaty Purchase Center that will address the level of overall staffing as well as staffing needed for an effective QAR function.	7/12/2006
Survey of The Quality Assurance Review Process	6-26	2	Recommend the AA/OFA consult a statistician to develop procedures for selecting samples of all loans purchased at the Center and specific loan categories to be tested in the QA plan.	SBA is working with its internal auditor, Kearney & Co., to development of sound analytical sampling procedures for QAR reviews.	7/12/2006
Survey of The Quality Assurance Review Process	6-26	3	Recommend the AA/OFA update the QAR checklist to include all items required to be evaluated during the original purchase review.	The QAR checklist is being updated as part of re-engineering review.	7/12/2006

Survey of The Quality Assurance Review Process	6-26	4	Recommend the AA/OFA develop procedures to be followed when a deficiency is identified during a quality assurance review to 1) notify purchase reviewers of the deficiencies, 2) provide training, 3) implement revisions to the guaranty review process.	These procedures are being developed as part of the re-engineering review.	7/12/2006
Survey of The Quality Assurance Review Process	6-26	5	Recommend the AA/OFA revise the QA plan, as necessary, and fully implement the QAR process.	These QAR process is being refined and documented as part of the re-engineering review.	7/12/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	1A	Promulgate Regulations to govern the SBAExpress Program in order to ensure that the agency has sufficient legal authority to manage the Program and that the public is put on adequent public notice of this Program	SBA plans to develop proposed regulations for the SBAExpress Program during FY2008.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	1B	Revise the SBA Express Program to clarify the credit analysis for lenders in the Program so that these provisions do not conflict with the "credit elsewhere" provision in the Small Business Act...	Updates to SBA's loan processing SOP will appropriately address this issue.	9/29/2006

Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	1C	Revise the Guide to establish the criteria as to when lenders are permitted to use credit scores, when they can use credit scores as the sole means of determining the creditworthiness of borrowers, and …	SBA's lender oversight reviews assess how lenders using credit scoring for decisionmaking document and validate their credit scoring process. Guidance to that effect will also be included in updates to SBA's loan processing SOP.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	1D	Revise the Guide to identify acceptable credit analysis methods so that lenders have a clear understanding of what is expected of them and SBA employees have a basis for reviewing lender underwriting.	Updates to SBA's loan processing SOP will appropriately address this issue.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	1E	Promulgate Regulations to exempt the SBAExpress Program from existing regulations that conflict with the SBA Express Program Guide or revise the Guide to be consistent with Agency regulations.	SBA plans to develop proposed regulations for the SBAExpress Program during FY2008.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	2A	Amend the Guide to require lenders to provide SBA with a copy of their loan administration procedures as the time they apply for admission to the Program and, if any changes have been made, or…	SBA believe that it has adequate requirements established with regard to program participation and has so advised OIG. These requirements wll be included in the updated SOP. OIG has not responded to SBA's submission.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	2B	Amend the Guide to provide that lenders must provide information about past compliance problems with their regulator or in complying with SBA requirements, within a specific period of time, and …	SBA believes that it already checks a lender's regulatory compliance as part of the lender oversight review of a lender and has so advised OIG. OIG has not responded to SBA's submission.	9/29/2006

Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	2C	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, ensuring that such standards provide data...	SBA believe that it has adequate requirements established with regard to program participation and has so advised OIG. These requirements wll be included in the updated SOP. OIG has not responded to SBA's submission.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	2D	Amend the Guide to identify what training in SBA's policies and procedures is appropriate for new lenders, and to require lender certification that all of the lenders' loan officers that make SBAExpress loans have been taken the training.	SBA believe that it has adequate requirements established with regard to program participation and has so advised OIG. These requirements wll be included in the updated SOP. OIG has not responded to SBA's submission.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	2E	Consider where it would be appropriate to assess the rates of default and losses and compliance with SBA requirements on SBAExpress loans made by new lenders versus loans made by experienced 7(a) lenders...	SBA believe that it has adequate requirements established with regard to program participation and has so advised OIG. These requirements wll be included in the updated SOP. OIG has not responded to SBA's submission.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	3A	Identify in the Guide the specific SOP and regulatory provisions that provide the applicable procedures and requirements.	Updates to SBA's loan processing SOP will appropriately address this issue.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	3B	Consider whether it would be appropriate to revise the web page containing the Guide on Agency's Electronic Lending web page that it contains links that a lender could click to the directed to the relevant provision of the SOP.	SBA is assessing options to make SOPs available on the web with embeded links and an indexed search capability.	9/29/2006

Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	4A	Revise the Guide to eliminate the reference to Notice 5000-753 and implement effective procedures for verififcation of IRS tax returns by SBAExpress lenders.	Updates to SBA's loan processing SOP will appropriately address this issue.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	5A	Take the CommunityExpress Program Guide off the Agency's Electronic Lending website.	Completed.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	5B	Revise the CommunityExpress Program Guide to address the recommendations set forth in concerns 1-4, as applicable.	SBA is considering programmatic changes to Community Express. Once all approvals and notifications have been completed, procedural guidance will be issued.	9/29/2006
Policies and Procedures For the SBAExpress and CommunityExpress Loan Programs	6-34	5C	Obtain Agency clearance of and issue an official CommunityExpress Program Guide.	SBA is considering programmatic changes to Community Express. Once all approvals and notifications have been completed, procedural guidance will be issued.	9/29/2006
Deficiencies in OFA's Purchase Review Process For Backlogged Loans	6-35	1	Perform a risk analysis of the backlog loan porfolio to identify loans with a high risk of improper payment and perform thorough purchase reviews of these loans to identify improper purchases and seek recovery from lenders as necessary.	OFA is embarking on a major initiative to review all loans awaiting post purchase reviews. The recommendations will be included in this review.	9/29/2006

Deficiencies in OFA's Purchase Review Process For Backlogged Loans	6-35	2	Develop a Purchase Review Form 327 for CAPLines loans to ensure these types of loans are adequently reviewed in the future.	CAPLine purchase reviews will be handled by a special unit with expertise in these types of loans. A separate 327 will be prepared to assist in the reviews.	9/29/2006
Audit of an SBA Guarantied Loan	7-02	1		Completed.	10/23/2006
Audit of an SBA Guarantied Loan to Palmarejo Service Station	7-05	1		Completed.	12/20/2006
SBA Guaranteed Loan to Just A Cut Lawn Care, Inc.	7-06	1	Recommend the Acting AA/OFA seek recovery of $28,660 from the lender on the guarantee.	OFA is seeking a negotiated settlement with the lender based upon a percentage of the disbursements that could not be substantiated as having been disbursed for business purposes. OFA will advise OIG of the tinal resolution on this loan.	12/28/2006
Audit of an SBA Guaranteeed Loan One One Nine Consulting Corp DBA Adobe St.	7-07	1		Completed.	12/29/2006

Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	1	Recommend the AA/OFA determine if the loan proceeds, on the 45 loans sampled during our audit were used in accordance with the terms of the loan authorizations...	The use of proceeds for the 45 loans sampled during the OIG audit will be reviewed and determinations made as to appropriate action.	12/29/2006
Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	2	Recommend the AA/OFA determine if lender actions warrant a denial of liability on $14,232 in guarantees associated with the two loans that were either missing a Form 1919...	SBA will review and make determinations regarding the propriety of recovering the guaranty purchase disbursements with respect to these two loans and take appropriate action.	12/29/2006
Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	3	Recommend the AA/OFA recover $7,414 from the lender that awarded an SBA loan to an ineligible company.	Recovery of $7,414 from the ender involved will be requested if there is sufficient legal basis for such recovery.	12/29/2006
Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	4	Recommend the AA/OFA revise the purchase demand kit and review checklists to require that lenders provide SBA staff with use of proceeds documentation...	The revision of the purchae demand kit and associate checklist are part of the NGPC re-engineeing effort.	12/29/2006
Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	5	Recommend the AA/OFA review the 2,729 loans for compliance with SBA rules and regulations and improper payments.	SBA plans to sample the loans to determine if additional work is necessary.	12/29/2006

Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	6	Recommend the AA/OFA recover $27,134 for the two purchaed SBAExpress loans reviewed for which the lender failed to disclose material facts.	Recovery of $27,134 from the lender involved will be requested if there is sufficient legal basis for such recovery.	12/29/2006
Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	7	Recommend the AA/OFA require the Fresno and Little Rock Commercial Loan Servicing Centers ensure lenders have provided technical assistance before purchasing guarantees above 50 percent.	Additional guidance on technical assistance requirements has been issued.	12/29/2006
Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	8	Recommend the AA/OFA obtain evidence from lenders that technical assistance was provided to borrowers on the 43 Community Express loans reviewed...	Additional guidance on technical assistance requirements has been issued.	12/29/2006
Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	9	Recommend the AA/OFA direct the Fresno Commercial Loan Service Center to rescind its September 11, 2003 guidance and inform lenders that proof of technical assistance is program requirement.	Completed.	12/29/2006
Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	10	Recommend the AA/OFA review the $25.1 million of loans in liquidation and refer to the U.S. Department of Treasury those loans that are more than 180 days delinquent and are not in bona fide workout arrangments.	Transfer of legally collectible loans to Treasury for servicing takes place after the lender has completed recovery actions, and SBA has reviewed such actions and charged off the loans.	12/29/2006

Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	11	Recommend the AA/OFA ensure that adequate emphasis is placed on liquidation follow-up and that controls are in place to refer eligible non-tax debts to the Department of Treasury within 180 days of delinquency as required by the Debt Collection Improvement Act.	Supplementing or redirecting resources at the centers is being explored to adequately staff this function. Transfer of legally collectible loans to Treasury for servicing takes place after the lender has completed recovery actions, and SBA has reviewed such actions and charged off the loans.	12/29/2006
Audit of SBA Express and Coimmunity Express Loan Purchase and Liquidation Process	7-08	12	Recommend the AA/OFA require the Fresno and Little Rock Commercial Loan Servicing Centers to obtain updated status reports from lenders on loans currently in liquidation status and charge loans off, as appropriate.	The servicing centers are exploring ways to redirect or supplement existing staff resources to review purchased loans in liquidation status and obtain lender information as necessary for liquidation oversight and charge-off when appropriate.	12/29/2006
Audit of an SBA guaranteed Loan, San Francisco, CA	7-09	1		Completed.	1/9/2007
Audit of an SBA Guaranteed Loan, Grand Rapids, Michigan	7-10	1		Completed.	1/16/2007
Review of An SBA Guaranteed Loan to Daniel Ereaux dba Homesteaders Pizza	7-15	1	Recommend the Acting AA/OFA seek recovery of $82,411, less any subsequent recoveries from the lender on the guarantee paid.	Completed.	2/12/2007

Autid of an SBA Guaranteed Loan to Iron CNC Machining, Inc. and Iron Imaging, Inc.	7-17	1		Completed.	3/12/2007
SBA's Use of the Loan and Lender Monitoring System	7-21	1	Recommend the Director of OLO establish a method, based on a specific standard or other metrics, for assigning risk ratings that more accurately reflect the risk profiles of lenders.	OCRM has research methods of distribution and implemented a new method on 12/01/2007	5/2/2007
SBA's Use of the Loan and Lender Monitoring System	7-21	2	Recommend the Director of OLO develop an on-site review plan or agreed upon procedures for all high-risk 7(a) lenders with guaranteed loan portfolios in excess of $4 million.	OCRM provided LOC on 11/29/2007 a draft copy of the metrics and procedures to implement. With the implementation of the Reorganization the Small Lender Team will provide monitoring to this group of lenders	5/2/2007
SBA's Use of the Loan and Lender Monitoring System	7-21	3		This recommendation was closed prior to the OIG providing final report	5/2/2007
SBA's Use of the Loan and Lender Monitoring System	7-21	4	Recommend the Director of OLO share lender risk ratings with SBA offices that make guarnetee purchase decisions.	After the Risk Rating System was proposed 05/2006 OCRM began providing SBA offices with the quarterly lender performance data	5/2/2007

SBA's Use of the Loan and Lender Monitoring System	7-21	5	Recommend the Director of OLO develop and implement comprehensive loan monitoring policies and procedures that define acceptable lender performance and risk tolerance levels... (Refer to the audit report for the entire recommendation.)	OCRM has developed internal procedures that incorporate internal metrics to be used as a basis for imposition of enforcement actions. The draft copy was presented to the LOC on 11/29/2007	5/2/2007
Guarantee Purchase Process for Selection 7(a) Loans at the National Guaranty Purchase Center	7-23	1	Recommend the Acting Director of OFA seek recovery of $36, 407 on the guarantees paid on the 6 loans listed in Appendix IV of the audit.	NGPC is completing its reviews of the 6 loans and will make a determination whether recovery is appropriate in each case.	5/8/2007
SBA's Oversight of BLC	7-28	1	Setting specific performance goals and target dates for BLX to demonstrate improvement.	SBA does not agreed with the recommendation and is working with OIG to develop an alternative approach.	7/11/2007
SBA's Oversight of BLC	7-28	2	Reducing the guaranty percentages for all new loans originated by BLX.	SBA does not agree with the recommendation and has been advised by OGC that it is not legally permissible.	7/11/2007
SBA's Oversight of BLC	7-28	3	Suspending BLX's delegated lending authorities until the goals in Recommendation 1 are met.	SBA does not agree with the recommendation and believes it has taken appropriate action to address BLX's situation.	7/11/2007

SBA's Oversight of BLC	7/28	4	Developing standard operating procedures to complement revised 13 CFR that describe circumstances under which it will suspend or revoke PLP authority or how it will do so.	SBA does not agreed with the recommendation and is working with OIG to develop an alternative approach.	7/11/2007
SBA's Oversight of BLC	7/28	5	Identifying actions needed to address the potential conflict resulting from OLO's and OFA's placement in OFA.	SBA does not agreed with the recommendation and is working with the Lender Oversight Committee to strengthen the controls in has in place.	7/11/2007