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SMALL BUSINESS ADMINISTRATION

Actions Needed to Improve COVID-19 Loans' Internal Controls and Reduce Their Susceptibility to Fraud

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A Century of Non-Partisan Fact-Based Work

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GAO@100 Highlights

Highlights of GAO-21-472T, a testimony before the Committee on Small Business and Entrepreneurship, U.S. Senate

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Why GAO Did This Study

SBA has made or guaranteed more than 17 million loans and grants through PPP and the EIDL program, providing about $910 billion to help small businesses adversely affected by COVID-19. PPP provides potentially forgivable loans to small businesses, and EIDL provides low-interest loans of up to $2 million for operating and other expenses as well as advances (grants). However, the speed with which SBA implemented the programs left them susceptible to fraud. Given these concerns, GAO added these emergency loan programs to its High-Risk List in March 2021.

This testimony discusses fraud risks associated with PPP and the EIDL program. It is based largely on GAO's June 2020 - January 2021 reports on the federal response, including by SBA, to the economic downturn caused by COVID-19 (GAO-20-625, GAO-20-701, GAO-21-191, GAO-21-265). For those reports, GAO reviewed SBA documentation and OIG reports; analyzed SBA data; and interviewed officials from SBA and the Department of the Treasury.

What GAO Recommends

In addition to GAO's previous recommendations, GAO anticipates making four recommendations on fraud risks in PPP and EIDL and one on EIDL oversight in its March 2021 report on the federal COVID-19 response. SBA agreed with the recommendations, stating it would implement fraud risk assessments for both programs and an oversight plan for EIDL.

View GAO-21-472T. For more information, contact William B. Shear at (202) 512-8678 or shearw@gao.gov.

What GAO Found

In April 2020, the Small Business Administration (SBA) quickly implemented the Paycheck Protection Program (PPP) and expedited the processing of Economic Injury Disaster Loans (EIDL) and a new EIDL advance program. These important programs have helped businesses survive during the very challenging COVID-19 pandemic. In an effort to move quickly on these initiatives, SBA put limited internal controls in place, leaving both programs susceptible to fraud. GAO found the following:

- **PPP oversight.** Given the immediate need for PPP loans, SBA implemented limited safeguards for approving PPP loans. Because ongoing oversight is crucial, GAO recommended in June 2020 that SBA develop plans to assess PPP risks. SBA has since developed plans to review PPP loans and has recently provided us detailed information about its oversight process.
- **Analysis of EIDL data.** GAO reported in January 2021 that SBA had provided about 5,000 advances totaling about $26 million and approved at least 3,000 loans totaling about $156 million to potentially ineligible businesses. Therefore, GAO recommended that SBA conduct portfolio-level analysis to detect potentially ineligible applications.
- **Assessment of fraud risks.** Although SBA has taken some steps to mitigate fraud risks to PPP and EIDL, such as conducting PPP loan reviews and implementing new EIDL controls, the agency has not yet conducted a formal fraud risk assessment for either program.
- **Suspicious activity reports.** From April through October 2020, financial institutions filed more than 21,000 suspicious activity reports related to PPP. From May through October 2020, financial institutions filed more than 20,000 such reports related to EIDL. These reports identified suspicious activity, such as indicators of identity theft and the rapid movement of funds.
- **Department of Justice charges.** From May 2020 through February 2021, the Department of Justice publicly announced charges in over 100 fraud-related cases associated with PPP loans and 30 fraud-related cases associated with EIDL loans. The charges include bank and wire fraud, making false statements, identity theft, and money laundering.
- **SBA Office of Inspector General.** The SBA Office of Inspector General (OIG) received over 70,000 hotline complaints related to CARES Act programs, including PPP and EIDL, compared to the 700 to 800 it typically receives in a year. In October 2020, the OIG reported that its initial review revealed strong indicators of widespread potential fraud in the EIDL program. The OIG and other law enforcement agencies had seized over $450 million from over 15,000 fraudulent EIDL loans, according to the report.
- **Financial statement audit.** In December 2020, SBA's independent financial statement auditor issued a disclaimer of opinion on SBA's fiscal year 2020 consolidated financial statements because SBA could not provide adequate documentation to support a significant number of transactions and account balances related to PPP and EIDL.

Chairman Cardin, Ranking Member Paul, and Members of the Committee:

I am pleased to be here today to discuss our work on the Small Business Administration's (SBA) Paycheck Protection Program (PPP) and the Economic Injury Disaster Loans (EIDL) program. As of March 7, 2021, SBA had made or guaranteed more than 17 million loans and grants, providing about $910 billion to help small businesses adversely affected by Coronavirus Disease 2019 (COVID-19).

As we reported in June 2020, lenders and SBA moved quickly to make and process PPP loans.[1] Given the immediate need for these loans, SBA worked to streamline PPP so that lenders could begin distributing funds as quickly as possible. SBA's initial interim final rule allowed lenders to rely on borrower certifications to determine the borrower's eligibility and use of loan proceeds, and it required only limited lender review of borrower documents to determine the qualifying loan amount and eligibility for loan forgiveness.[2] We also reported that as of June 2020, SBA had already approved more EIDLs than for all previous disasters combined, according to SBA officials.

While millions of small businesses have benefited from these programs, the speed with which they were implemented left SBA with limited safeguards to identify and respond to program risks, including susceptibility to improper payments and fraud. Since June 2020, we have reported on the potential for fraud in both PPP and EIDL. Further, as we have reported multiple times, SBA's failure to provide us with data and documentation on PPP and EIDL in a timely manner has impeded efforts to ensure transparency and accountability for the programs. This includes delays in our obtaining key information from SBA, such as detailed oversight plans and documentation for estimating improper payments. As a result, we included these programs as a new area on our High-Risk List

[1]GAO, *COVID-19: Opportunities to Improve Federal Response and Recovery Efforts*, GAO-20-625 (Washington, D.C.: June 25, 2020).

[2]*See* 85 Fed. Reg. 20,811 (Apr. 15, 2020). The interim final rule stated that lenders would be held harmless for borrowers' failure to comply with program criteria. Congress later codified a PPP lender hold harmless provision, providing that lenders may rely on any certification or documentation submitted by applicants that is submitted, and attests that it is submitted, pursuant to all applicable statutory requirements. Pub. L. No. 116-260, § 305, 134 Stat. 1182, 1996-97 (2020).

in March 2021 because of their potential for fraud, significant program integrity risks, and need for much improved program management and better oversight.[3] We also cited the results of SBA's most recent financial statement audit, in which the auditor issued a disclaimer of opinion on SBA's financial statements because SBA was unable to provide adequate documentation to support a significant number of transactions and account balances related to PPP and EIDL.[4]

In this statement, I will discuss fraud risks associated with PPP and the EIDL program and the lack of adequately documented controls in the programs, as identified in prior work.[5] In preparing this statement, we primarily relied on our body of work issued from June 2020 through January 2021 that reviewed, among other things, SBA's implementation of these programs in response to the economic downturn caused by COVID-19.[6] We also included some preliminary findings from our ongoing work on PPP and EIDL.

For the reports issued from June 2020 through January 2021, we reviewed SBA documentation and analyzed program data, and we interviewed officials from SBA and the Department of the Treasury (Treasury). We also reviewed reports by SBA's Office of Inspector General (SBA OIG). Information on our scope and methodology can be found in our June 2020, September 2020, November 2020, and January 2021 reports. For our ongoing work on PPP and EIDL, we interviewed

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[3]GAO, *High-Risk Series: Dedicated Leadership Needed to Address Limited Progress in Most High-Risk Areas*, GAO-21-119SP (Washington, D.C.: Mar. 2, 2021).

[4]Small Business Administration, Office of Performance Management and the Chief Financial Officer, *Agency Financial Report Fiscal Year 2020* (Washington, D.C.: Dec. 18, 2020), 39–63.

[5]Fraud risk exists when individuals have an opportunity to engage in fraudulent activity, have an incentive or are under pressure to commit fraud, or are able to rationalize committing fraud. When fraud risks can be identified and mitigated, fraud may be less likely to occur.

[6]See GAO-20-625; GAO, *COVID-19: Brief Update on Initial Federal Response to the Pandemic*, GAO-20-708 (Washington, D.C.: Aug. 31, 2020); *COVID-19: Federal Efforts Could Be Strengthened by Timely and Concerted Actions*, GAO-20-701 (Washington, D.C.: Sept. 21, 2020); *COVID-19: Urgent Actions Needed to Better Ensure an Effective Federal Response,* GAO-21-191 (Washington, D.C.: Nov. 30, 2020); and *COVID-19: Critical Vaccine Distribution, Supply Chain, Program Integrity, and Other Challenges Require Focused Federal Attention,* GAO-21-265 (Washington, D.C.: Jan. 28, 2021).

officials from the Federal Bureau of Investigation (FBI), SBA, and the SBA OIG.

We conducted the work on which this statement is based in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

CARES Act and Subsequent Appropriations

In response to the far-reaching public health and economic crises resulting from COVID-19, in March 2020, Congress passed, and the President signed into law, the CARES Act, which provides over $2 trillion in emergency assistance and health care response for individuals, families, and businesses affected by COVID-19.[7]

Among other things, Congress established PPP in the CARES Act to help small businesses affected by COVID-19.[8] To date, Congress has provided commitment authority of about $814 billion for PPP.[9]

Through the CARES Act, Congress also temporarily expanded eligibility for SBA's EIDL program and appropriated $10 billion to create emergency EIDL advances, a new component of the EIDL program under the CARES Act.[10] Prior to the enactment of the CARES Act, SBA had begun awarding EIDLs to small businesses affected by COVID-19 using existing

[7]Pub. L. No. 116-136, 134 Stat. 281 (2020). As of March 2021, six other relief laws were also enacted in response to the COVID-19 pandemic: the Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020, Pub. L. No. 116-123, 134 Stat. 146; the Families First Coronavirus Response Act, Pub. L. No. 116-127, 134 Stat. 178 (2020); the Paycheck Protection Program and Health Care Enhancement Act, Pub. L. No. 116-139, 134 Stat. 620 (2020); the Paycheck Protection Program Flexibility Act of 2020, Pub. L. No. 116-142, 134 Stat. 641; Consolidated Appropriations Act, 2021, Pub. L. No. 116-260, 134 Stat. 1182; and American Rescue Plan Act of 2021, Pub. L. No. 117-2, 135 Stat. 4.

[8]PPP was authorized under SBA's 7(a) small business lending program.

[9]Pub. L. No. 116-136, §§ 1102(b)(1), 1107(a)(1), 134 Stat. at 293, 301; Pub. L. No. 116-139, § 101(a), 134 Stat. at 620; Pub. L. No. 117-2, § 5001(d) 135 Stat. at 85.

[10]Pub. L. No. 116-136, §§ 1107(a)(6), 1110, 134 Stat. 281, 302, 306.

funds.[11] In total, Congress has appropriated $50 billion in loan credit subsidies for the cost of EIDL loans and $40 billion for advances to assist businesses affected by COVID-19.[12] The $50 billion in loan credit subsidies would enable SBA to provide about $470 billion in EIDL loans.

GAO's Fraud Risk Framework

We have previously reported that strong internal controls help ensure that emergency relief funds are appropriately safeguarded.[13] While some level of risk may be acceptable in an emergency, an effective internal control system improves accountability and transparency, provides feedback on how effectively an entity is operating, and helps reduce risks affecting the achievement of the entity's objectives. A major component of internal control is identifying and responding to fraud risks. Recognizing fraud risks, and thoughtfully and deliberately managing them in an emergency environment, can help federal managers safeguard public resources while providing needed relief.

[11]The Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020, deemed COVID-19 a disaster under the Small Business Act, which made businesses experiencing economic injury caused by COVID-19 eligible for EIDLs. As a result, SBA began using existing $1.1 billion in loan credit subsidy to provide EIDLs to these affected businesses. The $1.1 billion in loan credit subsidy supported between $7 and $8 billion in EIDL loans. Loan credit subsidy covers the government's cost of extending or guaranteeing credit and takes into consideration the estimated cash flows to and from the government. The loan credit subsidy amount is estimated to be about one-seventh of the cost of each disaster loan.

[12]SBA provided advances using the $10 billion Congress appropriated under the CARES Act. On April 16, 2020, SBA announced that the lending authority for EIDL loans and the funding for EIDL advances had been exhausted. Under the Paycheck Protection Program and Health Care Enhancement Act, Congress appropriated another $10 billion for advances and $50 billion in loan credit subsidy for EIDL loans. Additionally, Congress made agricultural enterprises eligible for EIDL loans and advances. SBA began accepting new applications from only agricultural enterprises on May 4, 2020. On June 15, 2020, SBA reopened the application portal to all eligible applicants. Congress appropriated an additional $20 billion for targeted EIDL advances to eligible entities located in low-income communities with 300 or fewer employees that experienced an economic loss of greater than 30 percent in the Consolidated Appropriations Act, 2021. Qualifying entities may receive up to $10,000 in targeted advances. The American Rescue Plan Act of 2021 appropriated an additional $10 billion for the targeted EIDL advances; and $5 billion for a newly created $5,000 targeted EIDL advance program for business entities that qualified for the targeted EIDL advances but also meet smaller (employs less than 10 employees) and more economically harmed (economic loss greater than 50 percent) criteria than the original targeted EIDL advances. Pub. L. No. 117-2, § 5002, 135 Stat. 4, 85. The act also appropriated $70 million for EIDL loans. Pub. L. No. 117-2, § 5006, 135 Stat. at 92.

[13]GAO-20-625.

According to federal internal control standards and GAO's Fraud Risk Framework, managers in executive branch agencies are responsible for managing fraud risks and implementing practices for mitigating those risks.[14] When fraud risks can be identified and mitigated, fraud may be less likely to occur.[15] Federal internal control standards call for agency management officials to assess the internal and external risks their entities face as they seek to achieve their objectives.[16] The standards state that management should consider the potential for fraud when identifying, analyzing, and responding to risks. Risk management is a formal and disciplined practice for addressing risk and reducing it to an acceptable level.

In July 2015, we issued the Fraud Risk Framework, which provides a comprehensive set of key components and leading practices that serve as a guide for agency managers to use when developing efforts to combat fraud in a strategic, risk-based way.[17] The critical control activities for managing fraud risks fall into three general categories—prevention, detection, and response. Among other things, the Fraud Risk Framework recommends that agencies plan regular fraud risk assessments that are tailored to the program, and that these assessments should be conducted when there are changes to the program. As part of these risk assessments, legislation and guidance from the Office of Management and Budget require agencies to consider risk factors that are likely to contribute to significant improper payments, including whether the

[14] GAO, *Standards for Internal Control in the Federal Government*, GAO-14-704G (Washington, D.C.: Sept. 10, 2014); and *A Framework for Managing Fraud Risks in Federal Programs*, GAO-15-593SP (Washington, D.C.: July 18, 2015).

[15] "Fraud" and "fraud risk" are distinct concepts. Fraud involves obtaining something of value through willful misrepresentation. Fraud risk exists when individuals have an opportunity to engage in fraudulent activity, have an incentive or are under pressure to commit fraud, or are able to rationalize committing fraud. A fraud risk can exist even if fraud has not yet been identified or occurred. When fraud risks can be identified and mitigated, fraud may be less likely to occur. Determining if an act is fraud is beyond management's professional responsibility for assessing risk (such determinations are made through judicial or adjudicative systems). See GAO, *Medicare and Medicaid: CMS Needs to Fully Align Its Antifraud Efforts with the Fraud Risk Framework,* GAO-18-88 (Washington, D.C.: Dec. 5, 2017).

[16] GAO-14-704G.

[17] GAO-15-593SP.

program or activity reviewed is new to the agency.[18] The legislation and guidance also require agencies to consider recent major changes in program funding, authorities, practices, or procedures as part of risk assessments. In July 2016, the Office of Management and Budget issued updated guidelines that, among other things, affirmed that managers should adhere to the leading practices identified in GAO's Fraud Risk Framework.[19]

Leading practices identified in the Fraud Risk Framework call for a strategic approach for assessing and managing fraud risks. The Fraud Risk Framework notes that such an approach includes designating an entity that should, among other activities, manage the fraud risk assessment process and coordinate antifraud initiatives across the program. The fraud risk assessment should (1) identify inherent fraud risks facing the program, (2) assess the likelihood and impact of inherent fraud risks facing the program, (3) determine fraud risk tolerance, (4) examine the suitability of existing fraud controls and prioritize residual fraud risks, and (5) document the program's fraud risk profile. Such an assessment helps program managers determine whether they have the right controls in place to combat the most likely and impactful risks facing the program. The fraud risk assessment is particularly informative when the volume and nature of fraud risk indicators signify an evolving fraud risk landscape. Further, the risk profile serves as the basis for the antifraud strategy, which defines key elements, such as responsibilities, activities, and timelines for addressing residual risks and continuously identifying emerging fraud risks to the program.

[18]For example, the Payment Integrity Improvement Act of 2019, Pub. L. No. 116-117 (2020), and related guidance by the Office of Management and Budget, including Memorandum No. M-18-20, app. C to Circular No. A-123, *Requirements for Payment Integrity Improvement* (June 26, 2018).

[19]Office of Management and Budget, *Management's Responsibility for Enterprise Risk Management and Internal Control*, Circular No. A-123 (Washington, D.C.: July 15, 2016).

Ongoing SBA Oversight Is Necessary to Minimize Fraud in the Paycheck Protection Program

Program overview. PPP loans, which are made by lenders but guaranteed 100 percent by SBA, are low interest (1 percent) and fully forgivable if certain conditions are met. Subsequent legislation has modified the program, including the Paycheck Protection Program Flexibility Act of 2020, the Consolidated Appropriations Act, 2021, and the American Rescue Plan Act of 2021.[20] As modified, at least 60 percent of the loan forgiveness amount must be for payroll or other eligible expenses to qualify for full loan forgiveness, and there is a simplified loan forgiveness application process for loans of $150,000 or less.[21] PPP initially ended on August 8, 2020, but the Consolidated Appropriations Act, 2021, authorized additional loans under the program, including second PPP loans of up to $2 million for PPP borrowers provided they meet certain criteria.[22] SBA relaunched the program (Round 2) on January 11, 2021, and small businesses can apply for a PPP loan through March 31, 2021.[23]

Program usage. According to SBA, as of March 7, 2021, lenders had made about 7.6 million PPP loans totaling about $687 billion. The majority of these loans (5.3 million loans totaling more than $521 billion, according

[20]For example, the Consolidated Appropriations Act, 2021, expanded the list of allowable uses of proceeds and loan forgiveness to include certain operations, property damage, supplier, and worker protection expenditures. Pub. L No. 116-260, div. N, tit. III, § 304, 134 Stat. at 1993-94 (2020).

[21]Under the Consolidated Appropriations Act, 2021, the loan forgiveness certification should not be more than one page in length and should only require borrowers to provide a description of the number of employees they were able to retain because of the loan, the estimated amount of the loan amount spent on payroll costs, and the total loan value. Borrowers must also attest that they complied with all PPP loan requirements. Borrowers must retain relevant employment records for 4 years following submission of the form and other relevant records for 3 years. SBA retains the right to review and audit these loans for fraud.

[22]PPP borrowers are eligible to receive a second PPP loan of up to $2 million provided that they meet certain criteria, such as having not more than 300 employees, having used or intending to use the full amount of their initial PPP loan, and documenting quarterly revenue losses of at least 25 percent in a quarter of 2020 when compared to the same quarter in 2019. Pub. L No. 116-260, div. N, tit. III, § 311, 134 Stat. 1182, 2001 (2020); *see also* 86 Fed. Reg. 3712 (Jan. 14, 2021).

[23]Round 1 of PPP was initially scheduled to end on June 30, 2020, but Congress extended the deadline for borrowers to apply until August 8, 2020.

to SBA) were made during Round 1 of PPP, which ended August 8, 2020.[24]

Status of oversight plans. Given the immediate need for emergency funding, SBA implemented PPP quickly with limited safeguards for approving PPP loans.

In June 2020, we reported that SBA's initial interim final rule for PPP allows lenders to rely on borrowers' certifying their eligibility and the use of loan proceeds.[25] It also requires a limited review by the lender of documents provided by the borrower to determine the qualifying loan amount and eligibility for loan forgiveness.[26] We noted that reliance on borrower self-certifications can leave a program vulnerable to exploitation by those who wish to circumvent eligibility requirements or pursue criminal activities.

We also reported that because SBA had limited time to implement safeguards for the PPP loan approval process and assess program risks, ongoing oversight would be crucial. At that time, SBA had announced that it would review loans of more than $2 million to confirm borrower eligibility after the borrower applied for loan forgiveness and that it may review any PPP loan it deemed appropriate. However, SBA provided few details on these reviews at that time. Therefore, we recommended that SBA develop and implement plans to identify and respond to risks in PPP to ensure program integrity, achieve program effectiveness, and address potential fraud, including in loans of $2 million or less. SBA neither agreed nor disagreed with our recommendation at that time.

In December 2020, SBA officials said the agency had completed oversight plans and provided a Loan Review Plan for the loan review process. The plan references detailed policies and procedures for loan reviews and loan forgiveness reviews. In February 2021, SBA provided seven of the eight documents referenced in the plan and stated that the last document covering reviews of loans of $2 million or greater was still

[24]Totals exclude canceled loans. According to SBA, canceled loans may include, but are not limited to, duplicative loans, loans not closed for any reason, and loans that were fully paid off. In our September 2020 report, we provided information on the types of borrowers that received PPP loans and the size of PPP loans.

[25]GAO-20-625.

[26]As previously noted, Congress later included a hold harmless provision in the Consolidated Appropriations Act, 2021. Pub. L. No. 116-260, § 305, 134 Stat. 1182, 1996-97 (2020).

being finalized. The documents SBA provided include additional details on how SBA and its contractors will conduct the various reviews, at least for those loans approved in 2020. We continue to review these documents to determine the extent to which they address our recommendation.

In addition, SBA has added up-front controls to PPP as part of its implementation of Round 2 of the program. In the initial round of PPP, SBA did not conduct reviews of loan or borrower information prior to issuing a loan number. However, in Round 2, SBA is implementing front-end compliance checks of loan and borrower information prior to the loans being approved and closed by the lender. These reviews compare loan applications against Treasury's Do Not Pay service and public records, according to SBA officials and documentation.[27] Among other things, these validation efforts include determining whether the loan applicant business was in operation as of February 15, 2020.

Estimating improper payments. The limited safeguards for approving PPP and EIDL loans may have increased SBA's susceptibility to improper payments and fraud.

As we reported in November 2020, it is especially important for agencies with large appropriated amounts, like SBA, to quickly estimate their improper payments, identify root causes, and develop corrective actions when there are concerns about the possibility that improper payments, including those resulting from fraudulent activity, could be widespread.[28] Because SBA had not taken these measures for PPP, we recommended that SBA expeditiously estimate improper payments and report estimates and error rates for PPP because of concerns about the possibility that improper payments, including those resulting from fraudulent activity, could be widespread. SBA neither agreed nor disagreed with our recommendation at that time.

In response to our recommendation, SBA stated that it was planning to conduct improper payment testing for PPP and that it took improper payments seriously. In February 2021, SBA officials stated that SBA had submitted the sampling plan for this testing to the Office of Management

[27]Treasury's Do Not Pay service is an analytics tool that helps federal agencies detect and prevent improper payments made to vendors, grantees, loan recipients, and beneficiaries. Agencies can check multiple data sources to make payment eligibility decisions.

[28]GAO-21-191.

and Budget and would use this sampling plan to estimate both improper payments and error rates for PPP. We will continue to monitor the agency's actions to address this recommendation.

Suspicious activity and potential fraud. In January 2021, we reported on potentially suspicious activity in PPP.[29] From April through October 2020, financial institutions filed more than 21,000 suspicious activity reports (SAR) related to PPP with the Financial Crimes Enforcement Network (FinCEN). These reports identified multiple types of potentially suspicious activity related to PPP, such as indicators of identity theft, the rapid movement of funds, and forgeries. Although the filing of a SAR does not necessarily mean that fraud has occurred, law enforcement agencies use these reports to help support investigations, such as those related to PPP fraud.[30] Over 1,400 institutions had filed SARs related to PPP from April through October 2020, and the number of SARs filed generally increased during this period.[31]

DOJ and law enforcement agencies have reported ongoing efforts related to potential fraud in PPP. From May 2020 through February 2021, DOJ publicly announced charges in over 100 fraud-related cases associated with PPP loans, charging at least 170 defendants. The charges—filed in federal courts across the U.S. and investigated by a range of law enforcement agencies—include allegations of making false statements and engaging in identity theft, wire and bank fraud, and money

[29]GAO-21-265. We analyzed aggregate SAR data across U.S. financial institutions from April through October 2020. These data did not include identifying information on financial institutions that filed SARs, such as PPP lender status.

[30]SARs are reports certain financial institutions are required to file if a transaction involves or aggregates at least a certain dollar amount in funds or other assets (generally $5,000), and the institution knows, suspects, or has reason to suspect that the transaction is designed to evade any Bank Secrecy Act requirements or involves money laundering, tax evasion, or other criminal activities. *See, e.g*. 31 C.F.R. § 1020.320. Under the Bank Secrecy Act's implementing regulations, banks are also required to file a SAR when a transaction meets certain other criteria, such as for known or suspected criminal violations involving insider abuse of any amount. 12 C.F.R. §§ 21.11(c), 163.180(d)(3); 12 C.F.R. § 208.62(c); 12 C.F.R. § 353.3(a). Law enforcement agencies query FinCEN systems as part of their investigations of potential financial and other crimes.

[31]Banks and other financial institutions must file a SAR no later than 30 calendar days after the date of initial detection of facts that may constitute a basis for filing a SAR. If no suspect is identified on the date of detection of the incident requiring the filing, the financial institution may delay filing a SAR for an additional 30 calendar days to identify a suspect, but the report must be filed no more than 60 calendar days after the date of initial detection of a reportable transaction.

laundering. As of February 2021, over 30 defendants had pleaded guilty to federal charges of defrauding PPP.

In addition to ongoing prosecutions, law enforcement officials we spoke with noted a large number of ongoing investigations and hotline complaints related to CARES Act loans, including PPP and the EIDL program. A senior official with SBA OIG told us that, as of January 2021, the OIG had opened over 260 investigations related to CARES Act loans, at least three times the number of investigations the office would typically open in a year. Similarly, SBA OIG reported receiving over 70,000 hotline complaints related to CARES Act programs, compared to the 700 to 800 it would receive in a typical year.

Law enforcement officials also reported systemic patterns of fraud across PPP and EIDL investigations. Officials at SBA OIG and the FBI told us that they have identified systemic patterns of potential fraud, including identity theft, false attestations on loan documents, fictitious and inflated employee counts, falsified tax documentation, and misuse of proceeds. Additionally, the FBI reported in June 2020 that early investigations of PPP-related fraud involved bank insiders, previously convicted felons, the use of dormant or cash businesses, and identity theft.

SBA has taken some steps to mitigate fraud risks to PPP. According to SBA officials, they conducted an informal fraud risk assessment for PPP that resulted in reviews and the addition of some upfront controls, as discussed above. For example, SBA brought together subject matter experts from SBA and Treasury, as well as contractors, to identify fraud risks and mitigating controls for the program. To identify fraud risks, SBA used information on vulnerabilities observed through existing loan reviews as well as information from external sources, such as SBA OIG reports. In February 2021, SBA officials told us the agency would complete a formal fraud risk assessment but did not provide a firm date for when they would complete such an assessment.

We anticipate recommending in our March 2021 report on the federal COVID-19 response that SBA (1) conduct and document a fraud risk assessment for PPP and (2) develop a strategy that outlines specific actions to monitor and manage fraud risks in PPP on a continuous basis. SBA agreed with the recommendations, stating that it would work to ensure that a fraud risk assessment for PPP is completed and that fraud risks are monitored on a continuous basis.

Inability to support PPP transactions and related controls. In December 2020, SBA's independent financial statement auditor issued a disclaimer of opinion on SBA's fiscal year 2020 consolidated financial statements, meaning the auditor was unable to express an opinion due to insufficient evidence.[32] As the basis for the disclaimer, the auditor reported that SBA was unable to provide adequate documentation to support a significant number of transactions and account balances related to PPP due to inadequate processes and controls.

The auditor identified several material weaknesses in controls related to SBA's CARES Act programs, including PPP. In its discussion of material weaknesses related to PPP, the auditor noted there were over 2 million approved PPP loans (with an approximate total value of $189 billion) flagged by management that were potentially not in conformance with the CARES Act and related legislation. SBA management flagged the loans for one or more of 35 reasons (such as borrowers with criminal record or inactive businesses). In addition, the auditor found that SBA reported approximately $6 billion of PPP loans approved but not disbursed because of unsubmitted or unprocessed reports from lenders. In addition, the auditor noted there were over 896,000 errors from lender reporting that were identified but not reviewed or processed. The auditor recommended that SBA review loans with incomplete or inaccurate reporting and update records as appropriate, among other things.

Oversight of Economic Injury Disaster Loans Necessary to Detect Fraud and Determine Eligibility

Program overview. The EIDL program provides low-interest loans of up to $2 million for expenses—such as operating expenses—that cannot be met because of a disaster. The CARES Act expanded EIDL program eligibility to include additional small business entities and relaxed some approval requirements, such as demonstrating that the business could not obtain credit elsewhere.[33] Congress also appropriated $10 billion through the CARES Act to provide small businesses up to $10,000 in advances toward payroll, sick leave, and other business obligations, which borrowers do not have to repay, even if they are subsequently

[32]A disclaimer of opinion indicates that sufficient information was not available for the auditors to determine whether the reported financial statements were fairly presented in accordance with Generally Accepted Accounting Principles. Small Business Administration, Office of Performance Management and the Chief Financial Officer, *Agency Financial Report Fiscal Year 2020*.

[33]Prior to CARES Act changes, eligible businesses included small businesses, most private nonprofits of any size, small aquaculture enterprises, and small agricultural cooperatives.

denied the EIDL. Through the Paycheck Protection Program and Health Care Enhancement Act, Congress appropriated $50 billion in loan credit subsidies for the cost of EIDL loans and an additional $10 billion for advances.[34]

On December 27, 2020, under the Consolidated Appropriations Act, 2021, Congress appropriated an additional $20 billion for targeted EIDL advances. These targeted advances are restricted to certain eligible entities located in low-income communities that experienced an economic loss of greater than 30 percent and have no more than 300 employees. Qualifying entities may receive up to $10,000 in targeted advances. Previously, SBA calculated the advances provided under the CARES Act based on the applicant's number of employees, up to $10,000. On March 11, 2021, under the American Rescue Plan Act of 2021, Congress appropriated additional funding for entities that qualified for targeted EIDL advances under the Consolidated Appropriations Act, 2021.[35] Congress appropriated an additional $10 billion for eligible entities that have not received the full amount of $10,000 in targeted EIDL advances. Congress also appropriated $5 billion to provide an additional $5,000 for eligible entities in low-income communities that suffered economic loss of greater than 50 percent and employ not more than 10 employees. The $5,000 is available in addition to advances obtained under the CARES Act or targeted advances under the Consolidated Appropriations Act, 2021.

Program usage. As of March 2, 2021, SBA had accepted about 18 million applications for EIDL loans related to COVID-19 and approved about 3.8 million of these applications totaling about $204 billion (or an average of about $53,600 per loan). On July 11, 2020, SBA announced that it had fully allocated the $20 billion in funding for EIDL advances and would stop making advances to new applicants. Prior to then, SBA received about 10 million applications for EIDL advances related to COVID-19, and it approved about 5.8 million of these applications totaling $20 billion (or an average of about $3,500 per advance). SBA began implementing the targeted EIDL advances program on February 1, 2021. SBA has not yet announced its implementation of the additional targeted EIDL advances.

[34]The American Rescue Plan Act of 2021 appropriated an additional $70 million for EIDL loans.

[35]Pub. L. No. 117-2, §§ 5002, 5006, 135 Stat. 4, 85, 92.

Detecting potentially ineligible and fraudulent applicants. The CARES Act relaxed some approval requirements for EIDL, such as requiring the applicant to demonstrate that it could not obtain credit elsewhere and restricting SBA from obtaining tax transcripts. In January 2021, we reported that as of July 14, 2020, SBA had provided about 5,000 advances totaling about $26 million to potentially ineligible businesses in three types of industries—adult entertainment, casino gambling, and marijuana retail. Additionally, we reported that as of September 30, 2020, SBA approved at least 3,000 loans totaling about $156 million to potentially ineligible businesses that SBA policies state were ineligible for the EIDL program, such as real estate developers and multilevel marketers.[36]

Therefore, we recommended in January 2021 that to improve SBA's oversight of its EIDL approval process, SBA should develop and implement portfolio-level data analytics across EIDL loans and advances made in response to COVID-19 as a means to detect potentially ineligible and fraudulent applications.

SBA neither agreed nor disagreed with our recommendation. SBA took issue with our finding that potentially ineligible businesses received EIDL advances and loans. SBA stated that CARES Act provisions permitted businesses to self-certify their eligibility and that applicants could not proceed until they certified that they were not engaged in any of the prohibited activities. The agency also stated that a business being in one of the categories we deemed ineligible did not automatically mean the business was ineligible. However, we did not state that the businesses were automatically ineligible.

SBA also referred to actions the agency takes to ensure ineligible businesses do not receive EIDL loans, such as manual review of applications from businesses in prohibited categories. But SBA did not state it had any plans to conduct data analytics to identify potential ineligible businesses. We maintain that portfolio-level data analytics could help SBA improve its management of fraud risk.

As part of the Consolidated Appropriations Act, 2021, Congress requires SBA to perform eligibility verification for advances, and it permitted SBA

[36]Multilevel marketing is a business structure or practice in which an individual seller earns income both from direct sales and from the sales of the seller's recruits, or those recruited by the seller's recruits.

to require additional information from applicants, such as tax returns, for loans and advances as part of its verification.

Suspicious activity and potential fraud. Similar to PPP, we reported on potentially suspicious activity in EIDL in January 2021. Between May and October 2020, over 900 U.S. financial institutions filed more than 20,000 suspicious activity reports related to the EIDL program. These reports identified multiple types of potentially suspicious activity related to EIDL, such as indicators of identity theft, the rapid movement of funds, and forgeries.

In October 2020, SBA OIG reported that its preliminary review revealed strong indicators of widespread potential fraud in the EIDL program. According to the report, OIG and other law enforcement agencies had seized over $450 million from over 15,000 fraudulent EIDL loans.

DOJ and law enforcement agencies report ongoing efforts related to potential fraud in the EIDL program. From May 2020 through February 2021, DOJ publicly announced charges in over 30 fraud-related cases associated with EIDL loans and charged over 50 defendants. The charges—filed in federal courts across the United States and investigated by a range of law enforcement agencies—include allegations of making false statements and engaging in identity theft, wire and bank fraud, and money laundering. As of February 2021, at least five defendants had pleaded guilty to federal charges of defrauding the EIDL program.

Law enforcement officials we spoke with also noted many ongoing investigations and hotline complaints related to CARES Act loans, including the EIDL program and PPP. Similar to PPP, they have also reported systemic patterns of fraud across EIDL investigations.

SBA has taken some steps to mitigate fraud risks in the EIDL program. SBA conducted an informal fraud risk assessment for EIDL that resulted in new and enhanced internal controls, according to SBA officials. For example, SBA began conducting eligibility checks through the Department of the Treasury's Do Not Pay service and plans to obtain 2019 tax transcripts from IRS for the targeted advances. The agency also considered fraud risks facing EIDL, the sources and likelihood of those risks, and residual risks.[37] Additionally, SBA officials told us SBA

[37]According to federal internal control standards, inherent risk is the risk to an entity prior to considering management's response to the risk. Residual risk is the risk that remains after management's response to inherent risk.

increased staffing for its OIG liaison team that reviews suspicious loans flagged by loan officers and forwards referrals to SBA OIG. According to SBA OIG, as of January 2021, it had received nearly 750,000 of these referrals related to identity theft and over 585,000 referrals related to other potentially fraudulent activities associated with the EIDL program.

We anticipate recommending in our March 2021 report on the federal COVID-19 response that SBA (1) conduct and document a fraud risk assessment for the EIDL program and (2) develop a strategy that outlines specific actions to address assessed fraud risks in the EIDL program on a continuous basis. SBA agreed with the recommendations, stating that it would work to ensure that a fraud risk assessment for EIDL is completed and that fraud risks are monitored on a continuous basis.

Inadequate approvals and oversight related to the EIDL program. SBA's independent financial statement auditor also found material weaknesses related to SBA's processing of EIDL loans and advances and contractor oversight, and these weaknesses contributed to the auditor's disclaimer of opinion on SBA's financial statements. To process EIDL loans and advances, SBA used a contractor system to first automatically validate applicants and then issue alerts, including fraud alerts, which SBA loan officers were to review and mitigate. The auditor determined that SBA did not adequately design and implement controls to ensure that loan officers accurately recorded and approved EIDL loan and advances for eligible borrowers. Further, SBA did not design and implement controls to ensure loan officers addressed fraud alerts before they approved applications. The auditor also determined that SBA did not adequately design and implement internal controls for evaluating and monitoring the contractor's controls for the validation system.

Identifying and managing risk in the EIDL program. As discussed above, we and others have identified gaps in controls that may have led to fraud and the provision of EIDL funding to ineligible entities. However, SBA's Office of Disaster Assistance, which administers the EIDL program, has not proactively assessed risks to the program. SBA officials told us that SBA does not have documented risk assessments and that SBA has primarily identified problems through loan officer review of loan applications.

The lack of a comprehensive plan to proactively assess controls and mitigate risks in the EIDL program may hinder SBA from achieving the defined objectives of the program and identifying opportunities for improving preventive controls in a timely manner. For example, SBA officials told us that 4 months after SBA started using the service organization's automated validation system to approve loan applications in batches, they realized that these applications contained alerts that should have been reviewed by loan officers.

We anticipate recommending in our March 2021 report on the federal COVID-19 response that SBA implement a comprehensive oversight plan to identify and respond to risks in the EIDL program to help ensure program integrity, achieve program effectiveness, and address potential fraud. SBA agreed with the recommendation, stating that it would implement a comprehensive oversight plan for EIDL.

Our work on PPP and EIDL is ongoing. For PPP, we continue to examine the characteristics of borrowers that received PPP loans, the safeguards SBA implemented to help ensure that lenders and borrowers complied with program requirements, and the loan forgiveness process. For EIDL, we have ongoing work to examine SBA actions to address internal control weaknesses and the integrity of the EIDL program. In addition, we remain concerned about fraud risks in the EIDL program and have ongoing work related to fraud risk management. For both programs, we also continue to monitor SBA's progress toward developing and implementing corrective actions to address the material weaknesses identified by its financial statement auditor.

Chairman Cardin, Ranking Member Paul, and members of the Committee, this concludes my statement. I would be pleased to respond to any questions you may have.

GAO Contact and Staff Acknowledgments

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