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## Testimony

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# SMALL BUSINESS ADMINISTRATION

## Planning for Loan Monitoring System Has Many Positive Features But Still Carries Implementation Challenges

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Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss the Small Business Administration's (SBA) activities to complete planning for its loan monitoring system, as required by the Small Business Reauthorization Act of 1997. As we recently reported, SBA has prepared a project plan for completing the eight actions mandated in the act.<sup>1</sup>

My testimony today discusses our recent report and focuses on SBA's project plan for completing the mandated actions. While SBA has not yet completed any of the mandated actions in the 6 months since the act was passed, it has written a project plan that describes an approach for addressing those actions that has many positive aspects. As SBA moves forward to execute the plan, however, it will face several technical and management challenges and risks.

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## Background

SBA's need to monitor activities of lenders that help deliver its programs has increased significantly in recent years. One reason is that the reported volume of loans processed by lenders almost doubled between 1992 and 1997, from about \$24 billion to about \$46 billion. A second reason is that SBA shifted to lenders the responsibility for key loan origination, servicing, and liquidation functions during this same time period. In 1993, SBA district offices reviewed the creditworthiness of about 84 percent of lenders' requests for loan guarantees, with the remainder being processed under a preferred lender program. At that time, SBA also serviced and liquidated all loans that went into default. By 1997, preferred lenders processed about 52 percent of the loans and, starting in 1998, lenders became responsible for servicing and liquidating all loans they make under the 7(a) program, which constitutes about 80 percent of SBA's loan portfolio.<sup>2</sup>

To improve its ability to monitor lenders' loan servicing and liquidation actions, SBA asked for \$18 million in its fiscal year 1998 budget request. According to SBA, these funds were to be used for (1) recruiting expertise in lender oversight, (2) establishing financial performance goals for private-sector partners, (3) creating a database for lender and portfolio management, and (4) developing an information system for timely and accurate reporting to agency management.

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<sup>1</sup>Small Business Administration: Mandated Planning for Loan Monitoring System Is Not Complete (GAO/AIMD-98-214R, June 30, 1998).

<sup>2</sup>The program authorized under Section 7(a) of the Small Business Act is the agency's primary vehicle for providing small businesses with access to credit.

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After reviewing SBA's basis for this request, we reported in June 1997 that the agency had not undertaken the essential planning needed to develop the proposed loan monitoring system.<sup>3</sup> The Congress subsequently enacted provisions in the Small Business Reauthorization Act of 1997 that required the SBA Administrator to

“perform and complete the planning needed to serve as the basis for funding the development and implementation of the computerized loan monitoring system, including—

- (1) fully defining the system requirement using on-line, automated capabilities to the extent feasible;
- (2) identifying all data inputs and outputs necessary for timely report generation;
- (3) benchmark loan monitoring business processes and systems against comparable industry processes and, if appropriate, simplify or redefine work processes based on these benchmarks;
- (4) determine data quality standards and control systems for ensuring information accuracy;
- (5) identify an acquisition strategy and work increments to completion;
- (6) analyze the benefits and costs of alternatives and use to demonstrate the advantage of the final project;
- (7) ensure that the proposed information system is consistent with the agency's information architecture; and
- (8) estimate the cost to system completion, identifying the essential cost element.”

The act also required SBA, within 6 months of enactment, to submit a report to the Congress and to us on its progress in carrying out these mandated actions. As required, SBA submitted its report on June 2, 1998.

We were required by the act to evaluate and report on SBA's compliance with the act within 28 days of receipt of SBA's report. On June 30, 1998, we reported that SBA had formed a team for the loan monitoring system in December 1997, but it had not yet completed any of the eight mandated actions. We noted that SBA's report included a project plan, laying out its

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<sup>3</sup>Small Business Administration: Better Planning and Controls Needed for Information Systems (GAO/AIMD-97-94, June 27, 1997).

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approach for addressing these actions. Work on the first of the required planning actions was begun in May 1998 and, according to the project plan, SBA will complete work on the last of the eight mandated actions in August 1999.

In conducting our review, we analyzed SBA's systems development and related information resources management policies and procedures, reviewed SBA's activities to prepare for undertaking the required planning actions, and reviewed and analyzed SBA's June 2, 1998, report to the Congress on its progress in carrying out the eight required actions that was issued pursuant to the Small Business Reauthorization Act of 1997. Our work was performed from December 1997 through June 1998, in accordance with generally accepted government auditing standards.

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## SBA's Project Plan for Completing the Mandated Actions

SBA's project plan provides information in many key areas to explain how it intends to complete the mandated actions. The plan delineates the project's goals and objectives, resource requirements, quality standards and control systems, assumptions, methodologies, work breakdown structure with a timetable for completion of tasks, and estimated costs.

SBA established four goals for the loan monitoring system project:

- Have high-quality, timely data necessary to perform roles such as the management of risk, collection of fees from recipients, and reporting to internal and external entities.
- Enforce uniform practices for loan making and reporting that will result in equal access by all eligible small businesses.
- Have business processes that support a streamlined workforce, use appropriate work flows, use best practices of both the government and private sectors, and include the ability to cope with both upward and downward changes in demand and resource availability.
- Have a computer infrastructure that supports efficient and user friendly information exchanges within SBA and among SBA and external entities, and that can enhance SBA's program delivery and its ability to carry out its oversight functions.

According to the project plan, SBA's strategy for achieving these goals is to build on "best industry practices," reengineer inefficient business processes, and implement contemporary technologies. In support of these goals, SBA also established objectives for the loan monitoring system; they include the following functionality:

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- on-line update by lenders of disbursements, payments, unilateral servicing actions, and requests for SBA approvals, as necessary;
  - waiting-to-be-processed queues for action by service center personnel;
  - electronic (digital) signatures to identify and verify who takes and approves actions;
  - electronic notification of actions via external e-mail or lender notification queues;
  - on-line exception reporting to notify SBA of potential problems, such as “neglected” loans, poor credit analysis, and slow lender servicing or reporting;
  - data analysis tools for management information, such as lender and loan trend identification, and end-user query and reporting;
  - a centralized electronic file to replace on-site paper loan folders;
  - integrated interactive voice response allowing borrowers and lenders to receive status data;
  - on-line electronic collateral file with a centralized storage site for paper collateral documentation;
  - centralized, automated generation of uniform commercial code filing documents;
  - expanded use of auto-dial for collections; and
  - sophisticated industry models to analyze and manage credit risk and portfolio performance.

SBA included estimates of the personnel resources that it would need to execute the project plan. It estimated that 18 staff would be needed for the first phase of the project, which addresses the completion of the mandated actions, and that an additional three staff would be needed for the development phase. The project plan also describes the types of skills needed—such as programming, systems architecture, and database administration—to manage and execute the project.

To address the quality standards and controls to be used for the loan monitoring system project, the plan includes work elements to establish systems development standards and procedures and process change control procedures. The plan also describes the quality control process that SBA plans to use to identify compliance with standards, and defines how the compliance findings will be reported.

The plan recognizes that the project includes a number of assumptions that may affect its success. It identifies seven key assumptions that SBA made but will need to validate during the project. For example, SBA

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assumed that the agency's information technology architecture<sup>4</sup> will be completed before it is needed to support this project, and that agreements with benchmarking partners will be timely and structured to meet SBA's needs.

The project plan also cites the methodologies that SBA plans to use or is considering for key areas of the project. These include methodologies for project planning and management, benchmarking, reengineering, systems development, software acquisition, risk management, and development of an information technology architecture. In some areas, such as software acquisition, SBA is comparing its current methodologies with industry best practices to select the methodologies that will be used for the project. In other areas, such as benchmarking, SBA did not have a methodology; it has now either selected a new methodology or is in the process of selecting one for these areas.

Included in the project plan is a work breakdown structure that lists the work elements from the start of the project through completion. These elements include the individual steps necessary to complete the mandated actions and the steps planned for the subsequent system design, development or acquisition, and implementation. The work elements for completing the mandated actions are sequenced, beginning with benchmarking and ending with the identification of an acquisition strategy to support a make-or-buy decision. The project plan recognizes that the project will not have enough information to fully evaluate the make or buy issue until it has completed benchmarking, business process reengineering, requirements gathering and analysis, and benefits and costs analyses.

According to the project plan, SBA estimates that the loan monitoring system will cost about \$20 million to complete. In addition to the automated system, this estimate includes the costs of staffing; developing training; developing lender performance standards; establishing subsidy rate analysis processes; and making infrastructure improvements, such as buying communications hardware and software. The project plan specifies that SBA will refine the cost estimates after the systems requirements have been defined and the alternatives analyzed.

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<sup>4</sup>SBA is conducting a separate project to develop an information technology architecture and expects to complete it in time to support the loan monitoring system project.

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## Challenges and Risks in Executing SBA's Project Plan

While developing the project plan is a good start, SBA must still successfully execute it to complete the eight mandated actions. In executing the plan, SBA will face formidable technical and management challenges and risks, including

- establishing software project management capability while undertaking its largest information technology project ever;
- using methodologies and practices for the first time while conducting a large, complex project; and
- implementing the loan monitoring system project without having an information technology architecture in place.

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## Establishing Software Project Management Capability

SBA recognizes the need to establish defined processes for software project management and use them on this project. Research by the Software Engineering Institute has shown that defined and repeatable processes for managing software acquisition or development are critical to an organization's ability to consistently deliver high-quality information systems on time and within budget. These critical management processes include project planning, requirements management, software project tracking and oversight, software quality assurance, software configuration management, and change control management.<sup>5</sup>

If SBA cannot implement disciplined software development and acquisition processes for this project, it risks building or buying a system that does not effectively meet its requirements, is delivered late or over budget, or does not perform as specified.

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## Using Methodologies and Practices for the First Time

The loan monitoring system project team will be using, for the first time, methodologies it has selected for benchmarking, business process reengineering, information technology architecture development, project management, and systems development. Each of these methodologies is complex and will require staff with the necessary skills and abilities for rigorous implementation. The staff currently on the project management team will need to develop the skills and abilities to use the new methodologies as they execute this large undertaking. SBA may also need to hire staff with the necessary skills and abilities to use the new methodologies, and hire contractors with the necessary expertise to support the project team.

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<sup>5</sup>Definitions of these processes were obtained from the Software Engineering Institute's Capability Maturity Model for Software, Version 1.1.



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Successfully learning and employing several new methodologies simultaneously will present a considerable technical and management challenge. If the team is not up to the task, the project may not achieve its intended results.

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## Implementing the Project Without an Information Technology Architecture

SBA plans to work concurrently on an information technology architecture and the loan monitoring system as separate projects.<sup>6</sup> The act requires SBA to ensure that the loan monitoring system is consistent with the architecture. An information technology architecture provides a comprehensive “construction plan” or “blueprint” that systematically details the breadth and depth of an organization’s mission-based mode of operation. An architecture provides details first in *logical* terms, such as defining business functions, providing high-level descriptions of information systems and their interrelationships, and specifying information flows; and second in *technical* terms, such as specifying hardware, software, data, communications, security, and performance characteristics. By enforcing an information technology architecture to guide and constrain a modernization program, an agency can preclude inconsistent systems design and development decisions, and the resulting suboptimal performance and added cost.

SBA has started developing an information technology architecture by documenting its current computing environment. It plans to continue developing the architecture while the loan monitoring system project is underway. As stated earlier, SBA assumes that the information technology architecture will be completed before it is needed to support this project. If both logical and technical components of the architecture are not completed as scheduled, the loan monitoring system project will likely be delayed and plans may need to be revised because, as required by the act, the plans must be consistent with the information technology architecture.

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In conclusion, the extent to which SBA meets these challenges and manages these risks will determine how well business processes and systems requirements are defined, and the quality of support for decision-making on the purchase or development of the needed system. Because this system is a critical part of SBA’s modernization, its senior officials must closely monitor progress in implementing the project plan

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<sup>6</sup>The Clinger-Cohen Act of 1996 gives the Chief Information Officer of an executive agency the responsibility of developing, maintaining, and facilitating the implementation of a sound and integrated information technology architecture. An information technology architecture is sometimes referred to as a systems architecture.

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and ensure that appropriate steps are taken to mitigate the significant risks involved. SBA should complete all of the eight actions mandated by the Small Business Reauthorization Act of 1997 before buying hardware or systems. In particular, SBA should ensure that (1) the project has the active participation and support of senior program managers and staff, (2) a disciplined software development and acquisition processes is implemented for this project, (3) project staff are adequately trained and supported by contractors with expertise in the methodologies used for this project, and (4) the information architecture is adequately developed and used to guide the requirements for the loan monitoring system.

Mr. Chairman, this concludes my statement. I would be happy to respond to any questions that you or other members of the Subcommittee may have at this time.

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