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Hearing: Action Through Innovation: Private Sector Solutions to Recouping Stolen Pandemic Loan Funds
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Summary

The COVID-19 pandemic was the largest and most damaging fraud event in modern history. The two pandemic loan programs administered by the Small Business Administration (SBA)— the Paycheck Protection Program (PPP) and the COVID-19 Economic Injury Disaster Loan program (COVID-EIDL)—were especially targeted by fraud actors. Fraud estimates in these programs vary widely, largely because of differences in definitions and assumptions and a disparity in access to data. While SBA implemented more preventative controls in later rounds of pandemic lending, the backlog of actionable leads of potential fraud in PPP and COVID EIDL to investigate is enormous and the SBA Office of the Inspector General (SBA OIG) is overstretched.

Agencies like the SBA were unprepared for the fraud they encountered largely due to a lack of attention on fraud risks. The Government Accountability Office (GAO) issued its *Framework for Managing Fraud Risks in Federal Programs* in 2015, but regretfully little attention was paid to putting in place the preventative controls to manage fraud risks GAO called for. Congress and the SBA have the opportunity to demonstrate a commitment to preventing fraud in the future, following the devastating fraud losses experienced during the pandemic.

Pandemic Loan Fraud Loss Estimates Vary

In oversight work conducted by the SBA OIG and the GAO, myriad fraud schemes were uncovered in PPP and COVID-EIDL loan programs. For example, fraudsters submitted loan applications using stolen personal and business information and false documentation, such as fabricated payroll records and tax forms. They created fictitious businesses solely for the purpose of obtaining PPP and EIDL loans, with no legitimate operations or employees. In some cases, lenders and borrowers colluded to obtain larger loan amounts or to expedite loan approval, even if the applicant did not meet the eligibility criteria. And due to the urgency of disbursing funds to struggling businesses, there was limited time for thorough verification of applications, which made it easier for fraudulent applications to slip through the cracks.

SBA and the oversight community have different estimates of fraud losses. On the low end, SBA estimates $36 billion of $1.2 trillion (3%) in pandemic relief emergency program funds were obtained fraudulently.[1] On the higher end, SBA OIG estimates that over $200 billion (16.6%) were potentially fraudulent.[2] GAO for its part, identified over 3.7 million unique recipients with fraud indicators out of a total of 13.4 million who applied for SBA pandemic relief programs (27.6%).[3]

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[1] SBA, *Protecting the Integrity of the Pandemic Relief Programs: SBA's Actions to Prevent, Detect, and Tackle Fraud* (Washington, DC: June 27, 2023).

[2] SBA OIG, *COVID-19 Pandemic EIDL and PPP Loan Fraud Landscape*, Report 23-09 (Washington, DC: June 27, 2023).

[3] GAO, *COVID Relief: Fraud Schemes and Indicators in SBA Pandemic Programs*, GAO-23-105331 (Washington, DC: May 18, 2023).

At the root of this wide range of estimates are issues related to 1) definitions and assumptions, and 2) data access.

Definitions and Assumptions

The SBA and the OIG have good-faith disagreements about what qualifies a loan as potentially fraudulent. For example, SBA OIG contends that borrowers who fraudulently obtained PPP loans are unlikely to apply for loan forgiveness because they had already obtained the funds and had no intention of repaying or using loan proceeds appropriately. Thus, the OIG includes in its potential fraud estimates all PPP loans in which applicants had not applied for loan forgiveness or made any required principal repayments as of May 2023, resulting in borrower default of the loan.

In contrast, SBA contends that many defaulted loans are not fraudulent; they represent real businesses that did not make it through the turbulence of the pandemic, have no ability to repay, and no longer exist to apply for loan forgiveness, or are simply not aware this is an option.

Likewise, according to SBA, 88% of COVID-EIDL lending went to businesses that have either fully repaid their loan or begun to do so (74%) or are still in the allowed deferment period (14%). According to SBA, common sense dictates that a bad actor would not fraudulently obtain a loan, only to repay it with interest. OIG, on the other hand, believes that repayment alone is not a factor in whether the underlying application was potentially fraudulent.

The truth most likely lies somewhere in the middle.

These differences in opinion demonstrate the value of using common definitions when measuring and estimating fraud. Consistent definitions would allow experts to compare and aggregate data within and across agencies, assess trends, and show progress in fraud prevention.

Data Access

Another key reason there are differing estimates of fraud is that SBA cannot access datasets that the OIG and GAO can. For example, the GAO analyzed PPP data using comparisons against the National Directory of New Hires (NDNH) wage data at the Department of Health and Human Services (HHS), whereas SBA cannot access these datasets.

Furthermore, SBA was initially barred from using IRS data to check for identity fraud. After Congress granted SBA the authority in 2021 to use IRS data to verify identity for its pandemic programs, it was able to make improvements in its processes for identifying and denying loans to ineligible and fraudulent applicants.

Improving agency access to data is a key accelerator in fraud prevention and detection. For instance, in January 2023, the PRAC urged SBA to work with the Social Security Administration (SSA) to explore information-sharing agreements that will allow for verifications across all SBA-funded grant, loan, and benefit programs that are vulnerable to identity fraud.[4] SBA concurred and has coordinated with SSA on this matter, but as of April 2023, the SBA found that SSA may lack the legal authority to share information with SBA.

I have long advocated for better data access, sharing and analytics in preventing and detecting fraud. Agencies cannot prevent fraud if they cannot access the data needed to detect it in the first place. And even today, three and a half years after the pandemic started, Treasury's Do Not Pay

[4] PRAC, *FRAUD ALERT: PRAC Identifies $5.4 Billion in Potentially Fraudulent Pandemic Loans Obtained Using Over 69,000 Questionable Social Security Numbers* (Washington, DC: January 30, 2023).

system continues to lack access to SSA's full death data and it may be cost-prohibitive for Treasury to purchase it.

I have previously recommended that Congress establish a well-funded, centralized antifraud office that would have the necessary skills and focus to work on addressing the profound data challenges facing every level of government when it comes to preventing fraud. It is imperative that Congress learn from the lessons the pandemic provided by helping to facilitate better access to and sharing of data.

Preventative Controls Save Taxpayer Money

As in medicine, so in fraud: Prevention is key. Every dollar invested in fraud risk management can result in thousands, if not millions, of dollars saved. Both GAO and OMB have issued guidance noting that preventive controls are more effective than a "pay-and-chase" model.

SBA has seen this firsthand. After it began implementing improved internal controls and data screening practices midway through the pandemic—such as pre-award application screenings, automated screenings for PPP, tax transcript verifications for COVID-EIDL, and data checks using the Treasury Department's Do Not Pay system—the agency observed substantial savings in prevented fraud. Thanks to these improvements, SBA estimates that it achieved dramatically lower fraud rates in the two relief programs designed and launched in 2021, Shuttered Venue Operators Grants (SVOG) and the Restaurant Revitalization Fund (RRF). SBA must further invest in advanced analytics and improve its use of intra-agency data to identify fraud indicators in its loan programs going forward, and Congress should ensure SBA is resourced to do so.

Identity Theft Poses a Significant Threat

Identity theft has emerged as the largest fraud threat facing organizations today. The massive trove of personally identifiable information available for sale through data breaches coupled with advanced technology like deepfakes— accelerated by Generative AI voice spoofing— create a significant risk to government programs. The pandemic created the means for fraud actors to steal at scale using stolen identities.

It is unknown how much of the PPP and EIDL fraud was identity theft-related, but some indicators reveal that it may have been significant. In August 2021, the OIG reported over 1 million complaints of EIDL loan identity theft. In January 2023 the PRAC identified over 221,000 Social Security Numbers (SSNs) used on applications that were either not issued by SSA or that identifying information in SSA's records did not match the name and/or date of birth information provided by the COVID-19 EIDL or PPP applicant, suggesting potential identity fraud in the use of those SSNs. The PRAC also determined that $5.4 billion in COVID-19 EIDL or PPP loans was disbursed to applicants using 69,323 of those SSNs between April 2020 and October 2022.

SBA has implemented some controls that can screen for the presence of stolen identities since the start of the pandemic. It is vital that the fraud risk management efforts the agency undertakes going forward include robust tools to uncover possible identity theft before approving a loan. SBA leadership must demonstrate sustained attention and commitment to fight this new, more sophisticated adversary.

Investigations Backlog is Enormous, and the OIG is Overstretched

The vast majority of the pandemic loan programs are now over, and in the case of PPP, the forgiven loans have largely been extinguished, leaving the work of clawing back fraudulent funds to the OIG and its law enforcement partners.

Investigations yield a substantial return on investment. In 2019, SBA OIG achieved $111.0 million in monetary recoveries and savings—a fivefold return on investment to the taxpayers, and in 2020, OIG achieved $142.5 million in monetary recoveries and savings—a sixfold return on investment to the taxpayer.[5]

Yet, the SBA OIG remains woefully under resourced when compared to the challenge it faces. SBA has referred or likely will refer 744,000 cases of likely fraud from approved awards, grants, and loans to its OIG. The OIG has repeatedly and publicly indicated that the office is overstretched. Deputy IG Shoemaker told Congress in March 2023 that the office had over 80,000 actionable leads, but only 550 open cases across both PPP and COVID-EIDL.[6] SBA describes the analytic process it undertook to get to $36 billion in suspicious loans that it then referred to OIG as comprehensive and believes that its analysis provides a basis for the OIG to focus its investigative resources on those loans.

SBA's COVID-19 programs were three times the size of the 2009 Troubled Asset Relief Program (TARP) and significantly more complex, but SBA OIG's funding has been significantly less than the funding Congress provided for TARP. In the FY 2023 Omnibus passed in December 2022, Congress provided $32 million to SBA OIG. However, more resources for law enforcement are needed. Continued increases in annual appropriations for OIG will enable the office to enhance its data analytics unit and hire more permanent investigative personnel.

Conclusions

Lessons from the pandemic are already being applied at SBA. GAO has made recommendations to the SBA to enhance its proactive fraud risk management posture and in response, the agency has made progress in implementing a more robust framework, including establishing a Fraud Risk Management Board as a designated entity, in accordance with the GAO Fraud Risk Management Framework.

More work remains. Through proactively and regularly assessing vulnerabilities in its programs, implementing data-driven, preventative controls, establishing a culture where staff feel comfortable talking about fraud, and collaboratively engaging with the OIG, SBA can help ensure that it is well-prepared for any future crises that may be exploited by fraud actors. Congress can play a role by helping facilitate access to datasets and providing funding to the OIG to address its investigative backlog and to SBA to implement advanced, data-driven fraud prevention tools.

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[5] SBA OIG, *FY 2022 Congressional Budget Justification* (Washington, DC: May 2021).

[6] SBA, *Protecting the Integrity of the Pandemic Relief Programs.*