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February 2015

# SMALL BUSINESS CONTRACTING

## Opportunities Exist to Further Improve HUBZone Oversight

# GAO Highlights

Highlights of [GAO-15-234](#), a report to congressional requesters

## Why GAO Did This Study

Small firms participating in SBA's HUBZone program received about \$4 billion in federal contracts in fiscal year 2013. The program's purpose is to stimulate economic development in economically distressed areas. A certified HUBZone firm is eligible for federal contracting benefits, including limited competition awards such as sole-source and set-aside contracts. GAO previously reported on weaknesses in SBA's internal controls and problems with ensuring that only eligible firms participate in the program. GAO was asked to examine the steps SBA has taken to address these issues. This report (1) describes HUBZone designations and how SBA communicates with interested parties about the program, and (2) examines SBA's certification and recertification processes for firms.

To address these objectives, GAO analyzed statutory provisions, SBA documents, and federal procurement data. GAO also interviewed SBA and representatives from applicant firms (certified, decertified, and denied) and local economic development agencies located in four HUBZones selected for geographic diversity.

## What GAO Recommends

SBA should (1) establish a mechanism to better ensure firms are notified of changes that could affect their participation in the program, and (2) assess the recertification process and implement additional controls, such as criteria and guidance for a risk-based approach to requesting and verifying information during recertification. SBA agreed with both recommendations.

View [GAO-15-234](#). For more information, contact William B. Shear at (202) 512-8678 or [shearw@gao.gov](mailto:shearw@gao.gov).

February 2015

## SMALL BUSINESS CONTRACTING

### Opportunities Exist to Further Improve HUBZone Oversight

## What GAO Found

The Small Business Administration (SBA) designates economically distressed areas as Historically Underutilized Business Zones (HUBZone), based on demographic data such as unemployment and poverty rates, but lacks an effective way to communicate program changes to small businesses. The designations apply to areas such as nonmetropolitan counties and census tracts and are subject to periodic changes as economic conditions change. Small businesses in HUBZones can apply for certification to participate in the program. HUBZones that lose their qualifying status due to changes in economic conditions become "redesignated" and undergo a 3-year transition period. In 2015, 3,417 redesignated areas will lose their HUBZone status. There are 578 firms in those areas (see table below). SBA relies on website updates and broadcast e-mails to inform firms about program changes, and consequently not all affected may be informed about the changes before their resultant decertification. SBA has initiated efforts to improve notification of program changes, but its communications may not reach all affected firms and do not specify when the status of areas might change or what firms are located in those areas. As a result, some firms in the program lack timely awareness of information that could affect their eligibility.

**Number of Firms and Amount of Contracts Received for Firms in HUBZone Areas in Fiscal Year (FY) 2013, by Designation Status**

	Number of certified firms, as of June 2014		Amount of contract obligations to firms in area (FY13)	
	Total	Percent	Total	Percent
Qualified areas	4,318	83%	\$3,295,006,042	81%
Redesignated until 2014	146	3	\$24,467,606	1
Redesignated until 2015	578	11	702,784,535	17
Redesignated until 2016	69	1	28,832,221	1
Redesignated until 2017	78	2	40,477,929	1
<b>Total</b>	<b>5,189</b>	<b>100%</b>	<b>\$4,091,568,333</b>	<b>100%</b>

Source: GAO analysis of SBA data. | GAO-15-234

SBA has addressed weaknesses in its certification process that GAO previously identified, but lacks key controls for its recertification process. For instance, to receive certification SBA now requires all firms to provide documentation to show they meet the eligibility requirements. SBA also conducts site visits at selected firms based on, for example, the amount of federal contracts they received. However, SBA does not require firms seeking recertification to submit any information to verify their continued eligibility or provide guidance on when staff should request or verify documentation for recertification. Instead, it relies on firms attesting that they continue to meet the program's eligibility requirements. By not routinely requiring and reviewing key supporting documentation from recertification applicants, SBA is missing an additional opportunity to reduce the risk that ineligible firms obtain HUBZone contracts.

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### Abbreviations

ACS	American Community Survey
BLS	Bureau of Labor Statistics
DCI	data collection instrument
DSBS	Dynamic Small Business Search
FPDS-NG	Federal Procurement Data System-Next Generation
FTE	full-time equivalent
HCTS	HUBZone Certification Tracking System
HUBZone	Historically Underutilized Business Zone
HUD	Department of Housing and Urban Development
LIHTC	Low-Income Housing Tax Credit
MSA	Metropolitan Statistical Area
OIG	Office of Inspector General
PMSA	Primary Metropolitan Statistical Area
SBA	Small Business Administration
SOP	Standard Operating Procedures

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February 12, 2015

The Honorable Benjamin L. Cardin  
Ranking Member  
Committee on Small Business and Entrepreneurship  
United States Senate

The Honorable Maria Cantwell  
United States Senate

The Small Business Administration (SBA) administers the Historically Underutilized Business Zone (HUBZone) program, which was created in 1997.<sup>1</sup> The program's purpose is to stimulate economic development in economically distressed communities by providing federal contracting preferences to small businesses located in HUBZone areas that employ residents of the areas. As of June, 2014, there were more than 18,500 HUBZones and about 5,200 firms in the program.

The contracting preferences that a certified HUBZone firm (one that meets program requirements) can receive include limited competition awards such as sole-source and set-aside contracts. A certified firm also can receive a price evaluation preference of 10 percent in full and open competition if the apparent successful offering firm is not a small business. In addition, HUBZone firms can receive awards without set-asides (through open competition), through a small business set-aside, or a set-aside through other programs. For example, a HUBZone firm that also qualifies as a service-disabled veteran-owned small business could receive an award under the Service-Disabled Veteran-Owned Small Business program. In fiscal year 2013, federal agencies awarded prime contracts valued at about \$4 billion to HUBZone firms that were certified as of June 2014.<sup>2</sup> Federal agencies are responsible for trying to meet an

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<sup>1</sup>HUBZone Act of 1997, Pub. L. No. 105-135, Title VI, 111 Stat. 2592, 2627-38 (1997).

<sup>2</sup>A prime contract is awarded directly by a procuring agency to the bidder or offeror (prime contractor). See appendix I for additional information on the calculations presented in the report.

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annual statutory goal for awarding contracts to HUBZone firms (3 percent of all prime contracts and subcontracts).<sup>3</sup>

We and SBA's Office of Inspector General (OIG) previously have reported on the need for SBA to strengthen its internal controls and fraud prevention to ensure only eligible firms participate in the program.<sup>4</sup> We identified a number of internal control-related deficiencies in the HUBZone program. For example, we identified problems with the mechanisms that SBA used to certify and monitor firms and that SBA was not following its policy of recertifying firms every 3 years (a certified firm can participate in the program as long as it remains eligible and is recertified).<sup>5</sup>

You requested that we review the HUBZone program to examine steps SBA has taken to address the issues we previously identified and some potential changes in the program. This report (1) describes how HUBZone designations change and how SBA communicates these changes to interested parties, and (2) examines SBA's certification and recertification processes for firms, including the extent to which SBA has

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<sup>3</sup>In the HUBZone Act of 1997, Congress increased the overall federal contracting goal for small businesses from 20 percent to 23 percent to address concerns that the HUBZone contracting requirement would reduce federal contracts for non-HUBZone small businesses.

<sup>4</sup>GAO, *Small Business Administration: Undercover Tests Show HUBZone Program Remains Vulnerable to Fraud and Abuse*, [GAO-10-920T](#) (Washington, D.C.: July 28, 2010); *Small Business Administration: Undercover Tests Show HUBZone Program Remains Vulnerable to Fraud and Abuse*, [GAO-10-759](#) (Washington, D.C.: June 25, 2010); *HUBZone Program: Fraud and Abuse Identified in Four Metropolitan Areas*, [GAO-09-440](#) (Washington, D.C.: Mar. 25, 2009); *HUBZone Program: Fraud and Abuse Identified in Four Metropolitan Areas*, [GAO-09-519T](#) (Washington, D.C.: Mar. 25, 2009); *Small Business Administration: Status of Efforts to Address Previous Recommendations on the HUBZone Program*, [GAO-09-532T](#) (Washington, D.C.: Mar. 25, 2009); *HUBZone Program: SBA's Control Weaknesses Exposed the Government to Fraud and Abuse*, [GAO-08-964T](#) (Washington, D.C.: July 17, 2008); *Small Business Administration: Additional Actions Are Needed to Certify and Monitor HUBZone Businesses and Assess Program Results*, [GAO-08-975T](#) (Washington, D.C.: July 17, 2008); and *Small Business Administration: Additional Actions Are Needed to Certify and Monitor HUBZone Businesses and Assess Program Results*, [GAO-08-643](#) (Washington, D.C.: June 17, 2008). Also see Small Business Administration, Office of Inspector General, *Opportunities Exist to Further Improve Quality and Timeliness of HUBZone Certifications*, 14-03 (Washington, D.C.: Nov. 19, 2013); and *HUBZone Program Examination and Recertification Processes*, 6-23 (Washington, D.C.: May 23, 2006).

<sup>5</sup>For example, see [GAO-08-643](#).

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implemented procedures to address recommendations previously made to improve these processes. In addition, in the appendixes to this report we present information about selected characteristics of HUBZones and certified firms, how potential changes to designation criteria would affect the number of HUBZones, and summary data related to HUBZone application processing.

To address our objectives, we reviewed prior GAO and SBA OIG reports, applicable statutes and regulations, and SBA documents, including its Standard Operating Procedures (SOP), and interviewed SBA staff and representatives from the HUBZone Contractors National Council—a HUBZone trade association. We used SBA's Dynamic Small Business Search (DSBS) database and federal procurement data from the Federal Procurement Data System-Next Generation (FPDS-NG) to analyze the number of firms in different types of HUBZones and the number and amount of federal contracts awarded to the firms in fiscal year 2013.<sup>6</sup> We analyzed data from the Census Bureau's American Community Survey (ACS) and unemployment data from the Bureau of Labor Statistics (BLS). After reviewing related documentation or interviewing knowledgeable agency officials, we deemed the DSBS, FPDS-NG, Census, BLS, and SBA data sufficiently reliable for the purposes of describing the characteristics of HUBZones, participating firms, and their contracting. To examine SBA's certification and recertification processes and the extent to which SBA addressed previous recommendations, we reviewed SBA's policies and procedures for certification, recertification, and monitoring of firms. We reviewed a purposive sample of 39 HUBZone applications submitted in fiscal year 2013 to test the extent to which SBA followed its processes.<sup>7</sup> We reviewed and summarized available SBA analyses for certification and recertification activities from January 2013 through September 2014. For our sample of 39 applications, we also reviewed data (related to SBA's documentation and processing of applications)

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<sup>6</sup>DSBS offers an electronic search engine for contracting officers and serves as a marketing tool for small businesses that register with the system. It contains the profiles of thousands of small firms.

<sup>7</sup>Our universe of 1,425 firms (based on applications submitted in fiscal year 2013) consisted of 528 firms that were approved, 418 that were denied, 470 that were withdrawn, and 9 that were decertified. The 39 files we reviewed included 19 applications that were initially approved, 10 that were denied, and 10 that were withdrawn. Included in the 19 approved applications were all 9 firms that had been decertified (in the pool of 1,425 firms).



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extracted from the HUBZone Certification Tracking System (HCTS). To discuss SBA's certification and recertification processes and outreach efforts, we also selected a purposive sample of 16 HUBZone firms, four local economic development agencies, and one Native American Tribe located in four HUBZones we selected for geographic diversity and range of experiences. Of those entities, we interviewed representatives from eight firms and two local economic development agencies (11 entities did not respond to our requests for interviews or declined to speak with us). We reviewed documentation about SBA's efforts to keep certified firms informed about the program. We also used data from HCTS to analyze industry, application status, and processing times of applications received from fiscal years 2008 through 2013. We assessed the reliability of the HCTS data we used by reviewing related documentation, interviewing knowledgeable officials, and electronic testing of the data, and found them to be sufficiently reliable for the analysis we report, but there were some internal inconsistencies that limited our reporting. Appendix I contains additional information on our scope and methodology.

We conducted this performance audit from April 2014 to February 2015 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.

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## Background

There are four types of HUBZones. Initially, the HUBZone Act of 1997 (which established the HUBZone program) identified qualifying areas as

- qualified census tracts, which are determined by the area's poverty rate or household income;<sup>8</sup>
- qualified nonmetropolitan counties, which are determined by the area's unemployment rate or median household income; and

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<sup>8</sup>Qualified census tracts are those tracts designated by the Secretary of the Department of Housing and Urban Development for the Low-Income Housing Tax Credit program.

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- lands within the external boundaries of an Indian reservation, based on the areas meeting certain criteria.<sup>9</sup>

In subsequent years, Congress expanded the criteria for HUBZones to add bases closed under various base closure acts and include counties in difficult development areas outside of the continental United States as part of the qualified nonmetropolitan counties.<sup>10</sup>

To be certified to participate in the HUBZone program, a firm must meet the following criteria:<sup>11</sup>

- when combined with its affiliates, be small by SBA size standards;<sup>12</sup>
- be at least 51 percent owned and controlled by U.S. citizens;<sup>13</sup>
- have its principal office—the location where the greatest number of employees perform their work—located in a HUBZone;<sup>14</sup> and

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<sup>9</sup> HUBZone Act of 1997 (Title VI of the Small Business Reauthorization Act of 1997, Pub. L. No. 105-135).

<sup>10</sup>Difficult development areas have high construction, land, and utility costs relative to area median income. The areas are designated annually using a process that compares these costs. Consolidated Appropriations Act, 2005 Pub. L. 108-447, Div. K, § 152, 118 Stat. 3456-58 (2004), and Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users, Pub. L. 109-59, § 10203, 119 Stat. 1933-34 (2005).

<sup>11</sup>Different rules apply for Indian Tribal governments, Alaska Native Corporations, Community Development Corporations, and small agricultural cooperatives. For example, potentially eligible firms can be wholly owned by one or more Indian Tribal governments; wholly owned by a corporation that is wholly owned by one or more Indian Tribal governments; partly owned by one or more Indian Tribal governments and all other owners are owned or controlled by U.S. citizens or small business concerns; or partly owned by a corporation that is wholly owned by one or more Indian Tribal Governments, and all other owners are U.S. citizens or small business concerns. See Title 13 of the Code of Federal Regulations, Part 126.

<sup>12</sup>The firm, with its affiliates, must meet the size standard corresponding to its primary industry classification as defined in 13 CFR Part 121. SBA's size standards vary by industry and are almost always stated as the average number of employees or average annual receipts of a business.

<sup>13</sup>Qualified HUBZone firms also can be owned and controlled by Alaska Native Corporations, Indian Tribal governments, community development corporations, and agricultural cooperatives.

<sup>14</sup>While a certified HUBZone business must have its principal office in a HUBZone area, it can bid on and receive federal contracts for work to be performed anywhere; that is, HUBZone contracts are not limited to performance in HUBZone areas.

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- have at least 35 percent of its employees reside in a HUBZone.<sup>15</sup>

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## HUBZone Designations Can Change Relatively Frequently but SBA Communications May Not Reach All Affected Firms

HUBZone designations can change with some frequency. However, SBA's communications to firms about programmatic changes, including changes to the HUBZone map (area designations), generally have not been targeted or specific to individual firms that would be affected by the changes.

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## Designations for HUBZone Areas Regularly Change

SBA updates the HUBZone designations regularly based on whether they meet statutory criteria (such as having certain income levels or poverty or unemployment rates). SBA generally uses data from other federal agencies to determine if areas still qualify for the HUBZone program. SBA reassesses the status of nonmetropolitan counties more frequently than it reassesses the status of census tracts. For example, SBA updates the nonmetropolitan county designations each January to incorporate median household income data generated from ACS and each May to incorporate updated unemployment rates from BLS.<sup>16</sup> In contrast, SBA historically has reassessed the status of qualified census tracts at multiyear intervals, such as every 5 years, using the census tract designations that the Department of Housing and Urban Development (HUD) uses for another

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<sup>15</sup>SBA defines an employee as an individual employed on a full-time, part-time, or other basis, so long as that individual works a minimum of 40 hours per month. This includes employees obtained from a temporary employee agency, leasing concern, or through a union agreement or co-employed pursuant to a professional employer organization agreement.

<sup>16</sup>The Census Bureau collects income data as part of its annual ACS. The data are collected over a 5-year period and published on a rolling basis each year. The most recent update, reflecting the 2008-2012 ACS median household income data, was released in December 2013.

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program.<sup>17</sup> See appendix II for more information about the specific criteria for each type of HUBZone area.

In 2001, Congress extended the eligibility of census tracts and nonmetropolitan counties that lost HUBZone eligibility because of changes in income levels or poverty or unemployment rates.<sup>18</sup> These areas—labeled redesignated areas—remain eligible for 3 years after “the date on which the census tract or nonmetropolitan county ceased to be so qualified.” During the 3-year period, firms in those areas can continue to apply to and participate in the program and receive contracting preferences. In 2004, Congress revised the definition of redesignated areas to allow areas to retain eligibility for 3 years or until the public release of data from the 2010 decennial census, whichever was later.<sup>19</sup> Consequently, all of the areas that were redesignated between 2001 and October 2008 received an extension of their 3-year redesignation period.<sup>20</sup> With the release of 2010 Census data in October 2011, a large number of previously redesignated HUBZone areas that had received the extensions lost their designation, including 333 nonmetropolitan counties. In total, 2,396 of the more than 8,000 HUBZone certified firms at the beginning of fiscal year 2012 were decertified when these changes took effect because their principal office was no longer located in a HUBZone. (We discuss decertification in more detail later in this report.) The redesignations for 3,417 HUBZones will expire in 2015, largely because of the end of the approximately 3,400 census tracts that were redesignated in 2012. Finally, redesignated areas also may requalify for the program during their extended eligibility period. For example, after

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<sup>17</sup>The definition of qualified census tracts for HUBZone is the same as that for the Low-Income Housing Tax Credit (LIHTC) program and HUD designates qualified census tracts for purposes of the LIHTC program. Historically, HUD updated the designations every 5 years, but in October 2014 HUD announced that it was establishing a new method for determining qualified census tracts. The revised methodology incorporates 3 years of ACS estimates, but HUD has not announced how frequently it will determine qualified census tracts in future years.

<sup>18</sup>Congress initially created redesignated areas in the Consolidated Appropriations Act, 2001, Pub. L. No. 106-554, Appendix I, § 613, 114 Stat. 2763, 2763A-700 (2001).

<sup>19</sup>The data were released October 1, 2011. See Small Business Reauthorization and Assistance Act of 2004, Pub. L. No. 108-447, Div. K, § 152(c), 118 Stat. 2809, 3457 (2004).

<sup>20</sup>Areas that were redesignated after October 2008 were only eligible for a 3-year redesignation period.

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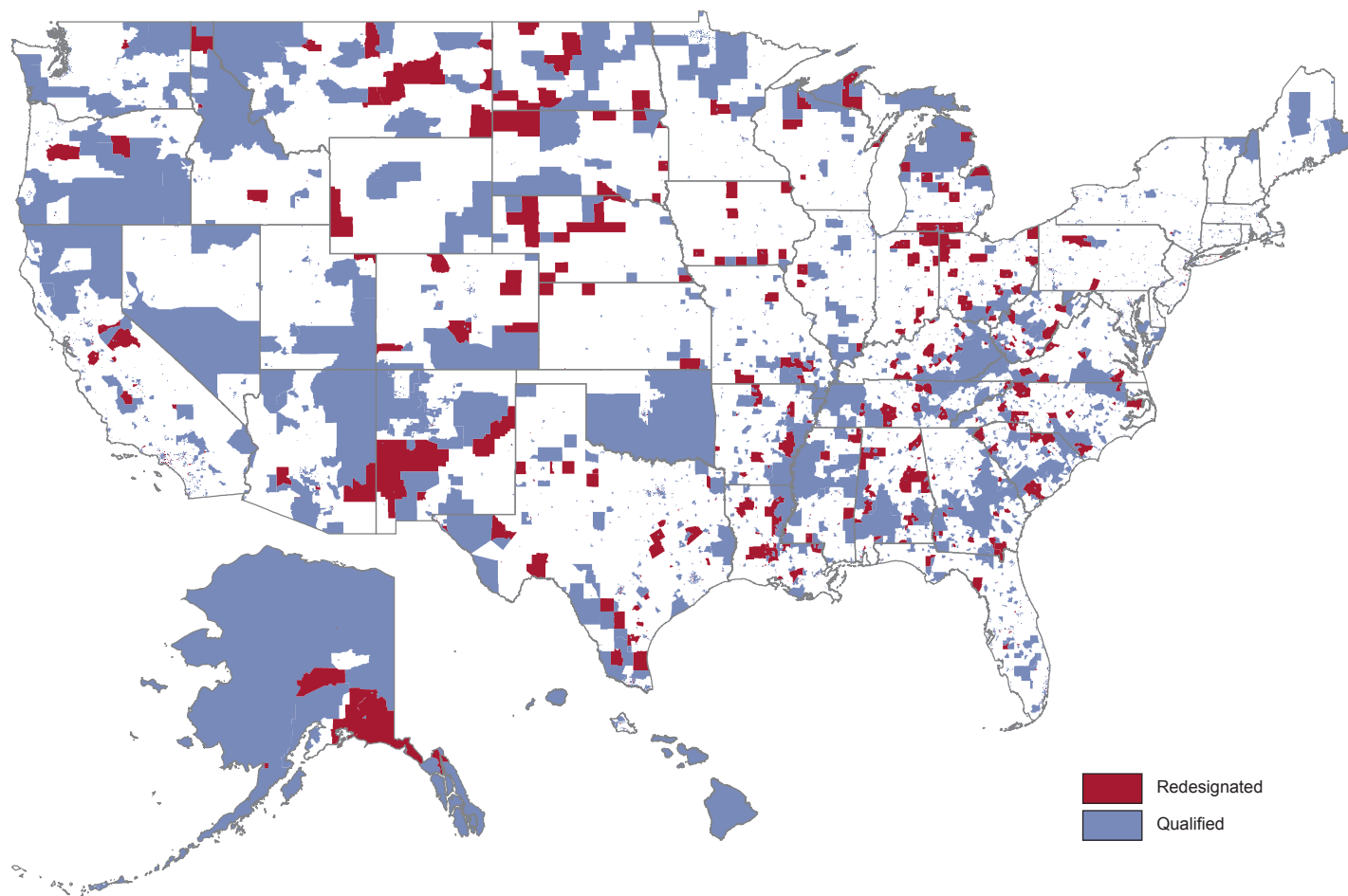
receiving the most recent unemployment data from BLS, SBA may change a nonmetropolitan county's designation from redesignated to qualified.

Qualified and redesignated areas generally are spread throughout the United States (see fig. 1). The map suggests that more qualified HUBZones are in the West and Southwest, but that is in part reflective of the larger geographic size of the nonmetropolitan counties in those regions. The map also suggests a higher concentration of areas within redesignated HUBZones in the East Coast and Midwest. For information about the characteristics of the HUBZones and differences in economic conditions (for example, as indicated by poverty and unemployment rates) among redesignated, qualified, and nonqualified areas, see appendix II.

**Figure 1: Qualified and Redesignated HUBZone Areas**

**Interactive graphic**

**Directions:** [Hover over either legend item to see the isolated view of that HUBZone area.](#)



Sources: GAO (analysis), Small Business Administration (data), and MapInfo (map). | GAO-15-234

According to our analysis, 83 percent of certified firms are located in a qualified area (see table 1). Most of the firms (578) that are located in a redesignated HUBZone are located in areas that will have their designations expire in 2015. When the redesignation status of an area expires, HUBZone firms in that area lose their program certification unless they relocate their principal office or, in some cases, their employees move to another HUBZone.

**Table 1: Number of Firms, and Number and Amount of Contracts Received for Firms in HUBZone Areas in Fiscal Year (FY) 2013, by Designation Status**

	Number of certified firms, as of June 2014		Number of contracts awarded to firms in area (FY13)		Amount of contract obligations to firms in area (FY13)	
	Total	Percent	Total	Percent	Total	Percent
Qualified areas	4,318	83%	11,042	80%	\$3,295,006,042	81%
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Redesignated until 2015	578	11	1,934	14	702,784,535	17
Redesignated until 2016	69	1	74	1	28,832,221	1
Redesignated until 2017	78	2	113	1	40,477,929	1
<b>Total</b>	<b>5,189</b>	<b>100%</b>	<b>13,729</b>	<b>100%</b>	<b>\$4,091,568,333</b>	<b>100%</b>

Source: GAO analysis of SBA data. | GAO-15-234

Notes: Percentages may not sum to 100 percent due to rounding.

## SBA's Communications about HUBZone Program Changes May Not Have Reached All Affected Firms

Generally, SBA relies on information posted on its website to communicate with interested parties about the HUBZone program. For instance, the HUBZone website includes links to the HUBZone map, frequently asked questions, and guidance to help firms apply for and maintain their certification. Firms can use the map of HUBZone areas to determine if an address or a particular area is designated as a HUBZone. More specifically, the website contains links to underlying data tables for the HUBZone map, and provides a potential applicant or program participant the ability to determine if a specific address is in a qualified HUBZone. Firms also can access a help desk by e-mail to get status information, help in resolving technical difficulties, or individualized assistance; obtain eligibility assistance through a twice-weekly interactive forum; and request a 15-minute appointment with a HUBZone analyst to discuss topics such as HUBZone policies and procedures, initial documents, or HUBZone applications. However, according to SBA officials, firms are primarily responsible for keeping themselves informed about the program so that they can remain eligible.

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## SBA's Review of the Accuracy of HUBZone Maps

In our June 2008 report, we found that SBA's HUBZone map contained ineligible areas and had not been updated to include eligible areas.<sup>21</sup> As a result, ineligible small businesses had participated in the program, and eligible businesses had not been able to participate. Consequently, we recommended that SBA take steps to correct and update the map used to identify HUBZone areas and implement procedures to ensure that the map would be updated with the most recently available data on a more frequent basis.

In response to our recommendation, SBA modified its contract with its mapping vendor to enable more frequent updating of the HUBZone map (annually). SBA officials stated that the accuracy of the map is checked twice after each upgrade, first by the mapping vendor and second by an SBA employee.

## SBA Notifications about Program Changes May Not Reach All Affected Firms

SBA's communications to firms about programmatic changes, including changes to the HUBZone map (area designations), generally have not been targeted or specific to individual firms and may not have reached all affected firms. Since February 2013, SBA has used a broadcast e-mail (which simultaneously sends the same message to multiple recipients) to distribute information about the program, including changes to the HUBZone maps. According to SBA officials, the e-mail list initially included all certified firms, but firms certified since the list was created have not been automatically added to the list. They and other interested parties must sign up (subscribe) to receive the e-mails through SBA's website, and as a result not all certified firms may have done so.

Through fiscal year 2014, SBA sent 13 e-mails through the system, covering topics such as changes made to the maps or the expiration of redesignated nonmetropolitan counties. Of the 13 e-mails, 9 focused on map-related issues. For example, a September 2014 e-mail notified subscribers that redesignations for 102 nonmetropolitan counties would expire on October 1, 2014. SBA also noted that there were 109 firms with principal offices in a county with expiring status. The e-mail included a link to the HUBZone map and a spreadsheet that showed the status of every county in January and May 2014, and encouraged firms to check their area's status. However, the e-mail did not identify the firms with principal

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<sup>21</sup> [GAO-08-643](#).



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offices in the counties that would lose redesignated status or identify the specific counties.

Furthermore, according to SBA officials, SBA began using a revised certification letter in October 2014 that includes links to the program's website and regulations, but unlike the previous certification letter that SBA sent to firms it does not include information on whether the firm is in a redesignated area or when that status will expire. According to HUBZone program policy, the approval letter should include language notifying the newly qualified firm of the possible expiration of the HUBZone.<sup>22</sup> According to SBA officials, the only time that a firm would be directly notified that it was located in a redesignated area would be when it received a notice of proposed decertification after the status of the area expired.<sup>23</sup> (We discuss the certification process later in the report.) Federal internal control standards require that management ensure there are adequate means of communicating with, and obtaining information from, external stakeholders that may have a significant impact on the agency achieving its goals.<sup>24</sup>

In a May 2008 report, SBA's Office of Advocacy stated that although HUBZone staff had been described as helpful and informative, there did not seem to be any systematic outreach or promotion of the program beyond responding to inquiries.<sup>25</sup> In October 2014, SBA announced the development of a new initiative (Destination: HUB) that is intended to promote and support HUBZone firms in federal contracting opportunities. The initiative will consist of three major components; first, an in-depth examination of successes and needs in the program; second, an analysis of best practices for successful public-private partnerships; and third, the

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<sup>22</sup>Of the 39 firms in our review, 6 were located in a redesignated area. For each of the 6 firms (which were approved for certification), the analyst noted in the file that the firm was located in a redesignated area and the approval letter to each firm included language about the location in a redesignated area. However, these files used the previous version of the approval letter.

<sup>23</sup>Half of the firms with which we talked were not very familiar with or were confused about the redesignation process, even when they were potentially affected by those processes.

<sup>24</sup>GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999).

<sup>25</sup>Henry Beale and Nicola Deas, *The HUBZone Program Report*, prepared at the request of the Small Business Administration Office of Advocacy, May 2008.

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launch of a broad grassroots educational initiative at the regional and national levels.

SBA officials said that SBA does not include a list of firms in the e-mails it sends because it wants every firm to be proactive and check its eligibility status. According to SBA officials, SBA's responsibility is to evaluate a firm's initial compliance and its ongoing eligibility (through recertifications, program examinations, and protests); firms have a responsibility to ensure that they remain eligible for the program. But the combination of relatively frequent changes to HUBZone designations, SBA's generally nonspecific communications to firms as illustrated by its certification letter, and the incomplete addressee list for the broadcast e-mails have increased the possibility that not all certified firms affected by such changes receive information about the changes or are made aware in a timely fashion of any effects on their program eligibility. We recognize that small businesses participating in the HUBZone program should be responsible for determining their eligibility, and they appear to have the ability to contact SBA to receive information specific to their situation. However, given the information SBA has at its disposal and the large number of HUBZone firms, SBA is in a position to better inform firms of changes affecting program eligibility.

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## SBA Has Improved Its Certification Reviews but Actions Related to Recertification Were Limited

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### Revised Certification Process Includes a Full Document Review, Which Helps to Ensure That Only Eligible Firms Participate in the Program

SBA revised its certification process in response to our June 2008 recommendation, and now requires firms to provide documentation and reviews this documentation to determine their eligibility for the HUBZone program.<sup>26</sup> As we reported in 2008, at that time SBA relied on data that firms entered in the online application system and performed limited verification of the self-reported information. Although agency staff had the discretion to request additional supporting documentation, SBA did not have specific guidance or criteria for such requests. We recommended that SBA develop and implement guidance to more routinely and consistently obtain supporting documentation upon application. The agency agreed with our recommendation and, according to SBA officials, since fiscal year 2009 SBA has required all firms to provide supporting documentation for information they enter in SBA's online application system. SBA then performs a full-document review on all applications as part of its initial certification process.

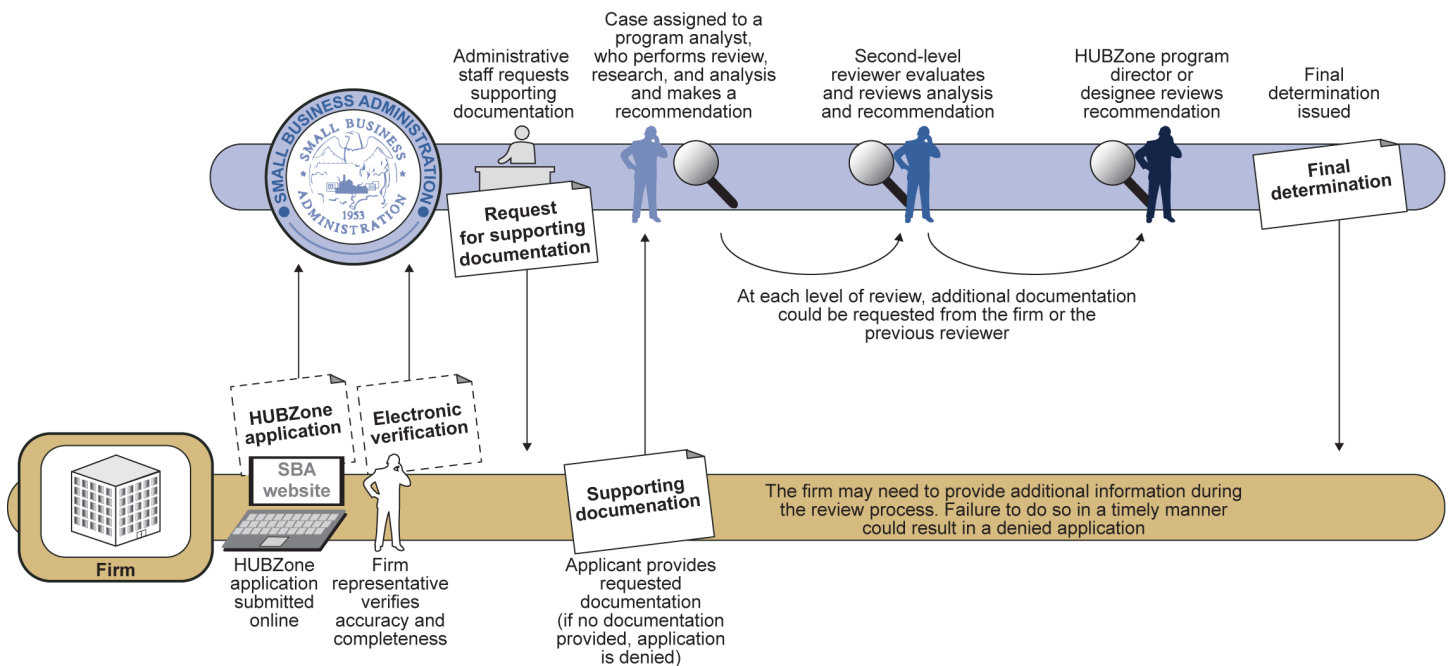
The current initial certification process comprises multiple steps (see fig. 2). For instance, after firms verify that the information they entered was complete and accurate, administrative staff request supporting documents from the applicant, including a lease agreement, map of employees' home addresses, personal and business tax returns, and payroll records. According to SBA officials, one staff reviews and analyzes the documents provided and makes a recommendation for the application and a second staff reviews the analysis and

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<sup>26</sup> [GAO-08-643](#).

recommendation.<sup>27</sup> Once a recommendation has been made, the HUBZone program director performs a final review before making a final determination. At the end of the process, SBA sends a signed letter to the applicant stating either that the firm is certified, or the basis for denial if the firm did not qualify. See appendix IV for summary statistics related to SBA's review of initial applications.

**Figure 2: HUBZone Application Review Process**



Source: GAO analysis of Small Business Administration information. | GAO-15-234

Our review of 39 application files SBA received from October 1, 2012, through September 30, 2013, indicates that SBA conducts full documentation review of the applications submitted by firms seeking

<sup>27</sup>SBA officials stated that, as part of their review of applications, SBA staff may perform additional independent research (such as a search of firms' websites or state government websites that contain information on firms incorporated in the state) to help ensure that applicants meet the eligibility requirements.

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certification.<sup>28</sup> For the 29 applications that were approved or denied, SBA staff prepared an analysis to support their recommendation to approve or deny the application.<sup>29</sup> For 18 of the 29 applications, SBA staff followed up with the applicant to obtain additional documentation; 12 of these applicants provided the documents and were approved, and the remaining 6 were denied because they did not.<sup>30</sup> Our review of the approval and denial letters relating to the 29 application files confirmed that the final determination and the effective dates entered into the system were the same.

We also found that SBA has not updated its SOP since 2009 when it began making changes to its certification processes, but expects to do so by the end of March 2015. Based on SBA's response to a recent OIG recommendation, the agency had planned to complete the update by September 2014.<sup>31</sup> The current SOP was last updated in November 2007 and therefore does not contain information about the full document review. According to SBA officials, to guide staff reviewing HUBZone certification packages, SBA currently uses guidance it developed that is specific to addressing situations that may arise during certification reviews. For example, the guidance discusses how to designate an employee of a HUBZone firm as located at a principal office when a

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<sup>28</sup>Our universe of 1,425 firms (based on applications submitted in fiscal year 2013) consisted of 528 firms that were approved, 418 that were denied, 470 that were withdrawn, and 9 that were decertified. The 39 files we reviewed included 19 applications that were initially approved, 10 that were denied, and 10 that were withdrawn. Included in the 19 approved applications were all 9 firms that had been decertified (in the pool of 1,425 firms).

<sup>29</sup>Twenty-nine of the 39 files had documentation of a full document review. Generally, an applicant firm may withdraw its application before submitting documentation; therefore, the 10 applications that were withdrawn did not undergo a document review. Similarly, according to SBA officials, some applications that are denied may not undergo a document review because the applicant firm did not provide documentation to SBA.

<sup>30</sup>A representative of one of the eight firms with whom we spoke noted that while the firm's application was under review by SBA, the firm did not receive any communication from SBA. However, when SBA contacted the firm requesting clarification or additional documentation, the firm was given only a couple of days to provide the requested information or would have its application denied.

<sup>31</sup>OIG Report No. 14-03. The OIG noted that the SOP was outdated and required that firms self-certify that they meet the program eligibility requirement although the process had changed to require a full documentation review. As a result, the OIG recommended that SBA update the HUBZone guidance based on the current certification process, which includes conducting a full review of supporting documentation.

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person works an equal amount of time in a principal office and a secondary office. The guidance also includes language that should be included in a final e-mail request to the applicant firm when the analyst determines that SBA needs to obtain clarification, additional documents, or both to complete its review of the application package. According to SBA officials, SBA had delayed updating the SOP because the agency intended to revise the HUBZone regulations first and then incorporate those changes into the SOP.

HUBZone trade association representatives told us that SBA has not always clearly communicated information about its review process to program applicants. They stated that the lack of clarity about SBA's certification review process likely could be solved through more education and communication. For example, they noted that after SBA changed the definition of an employee in May 2010 from an individual who was required to work 30 hours per week to an individual who worked 40 hours per month, the agency required that applicant firms provide documentation verifying that the employee worked during the previous month. However, according to the representatives, SBA then changed its interpretation to require that the employee worked during the period during which the application was submitted but did not communicate the change to the industry. According to SBA officials, SBA discusses the period that an employee must work in its frequently asked questions. While SBA defined an employee in its frequently asked questions, we did not find information related to the period that an employee must work to meet the eligibility requirement.

SBA officials told us that the agency again reviews the eligibility of some firms—generally, already certified firms—by conducting site visits to a select number of firms every year. In June 2008, we reported that SBA rarely conducted site visits during program examinations to verify a firm's information and recommended that the agency conduct more frequent site visits.<sup>32</sup> In response to that recommendation, according to SBA officials, SBA now conducts site visits on 10 percent of its portfolio of certified firms every year. According to the officials, the site visits are based on established criteria (such as the amount of HUBZone contract awards the firm has received) or done on an as-needed basis in connection with the review of an initial certification application or after

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<sup>32</sup>[GAO-08-643](#).

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receipt of a protest.<sup>33</sup> SBA officials told us that SBA uses a pass/fail system to describe the outcome of a site visit. In fiscal years 2013 and 2014, the officials told us that SBA selected 511 and 550 firms, respectively, for site visits. In fiscal 2013, SBA noted that 81 percent of the firms passed the site visit and 19 percent failed. For fiscal year 2014, SBA noted that 88 percent of the firms passed and 12 percent failed. According to SBA officials, SBA sends a notice of proposed decertification to firms that fail a site visit. (We discuss decertification in the next section.)

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### SBA May Propose Firms for Decertification If Eligibility Requirements Are Not Met

Once a firm is approved for participation in the HUBZone program, SBA may decertify the firm if SBA determines that the firm is no longer eligible for the program or if SBA is unable to verify the firm's continuing eligibility.<sup>34</sup> For example, firms in redesignated areas are proposed for decertification and are provided an opportunity to establish continued eligibility following the expiration of the area's redesignated status. For instance, a firm could prove its continued eligibility by showing that it had relocated its principal office to a qualified HUBZone area. These firms are ultimately decertified if they do not respond to the notice of proposed decertification by indicating that they are still eligible. According to SBA officials, the decertification process typically consists of three steps.

- SBA e-mails a notice of proposed decertification to the firm and allows the firm 30 days to respond.
- If the firm does not respond, SBA sends the notice of proposed decertification to the firm by certified mail.
- If the firm does not respond to the certified notice within 30 days, SBA then decertifies the firm on the following day.

Decertification also can occur in two other ways. A firm voluntarily can decertify if the firm determines that it no longer meets the program's eligibility requirements. SBA also can immediately decertify a firm during the protest process if, according to SBA officials, SBA determines that the

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<sup>33</sup>Other criteria that SBA uses to select firms for site visits include whether the firm was awarded a contract but was not visited in the prior year, awarded a contract and visited in the prior year, and certified in the previous fiscal year but had not received a contract award. The HUBZone protest process allows SBA, contracting officers, or any interested party to protest the qualified HUBZone status of an awardee or apparent awardee of a federal HUBZone contract.

<sup>34</sup>Agency officials stated that SBA also may decertify a firm if the firm fails to respond to the notice of proposed decertification.

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firm did not meet the eligibility requirements at the time of bid and award, or at the time of protest if the contract had not yet been awarded.<sup>35</sup> From fiscal year 2010 through fiscal year 2013, SBA reported 124 protests of HUBZone contracts, of which 46 (37 percent) were dismissed, 41 (33 percent) were sustained, and 37 (30 percent) were denied.<sup>36</sup>

SBA noted that it decertified 4,660 firms from fiscal year 2010 through fiscal year 2013. The vast majority of decertifications occurred from fiscal years 2010 through 2012. According to SBA officials, in fiscal year 2009, before conducting a legacy portfolio review, SBA asked firms to confirm their compliance with the program requirements or to voluntarily withdraw from the program.<sup>37</sup> The officials told us there were approximately 14,000 HUBZone firms that needed to validate their compliance with the program eligibility requirements. At that time, SBA notified the firms that the agency planned to conduct a full document review in 2009 or early 2010 to confirm compliance. According to SBA officials, many firms voluntarily withdrew from the program as a part of this effort. As shown in figure 3, our analysis of SBA data (for applications received from fiscal year 2010 through fiscal year 2013 for firms that were later decertified) showed that firms most frequently were decertified because their principal offices were

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<sup>35</sup>SBA requires that firms meet the eligibility requirement at the time of bid and when a contract is awarded. The HUBZone protest process allows SBA, contracting officers, or any interested party to protest the qualified HUBZone status of an awardee or apparent awardee of a federal contract. An interested party must submit its protest by close of business on the fifth business day after notification by the contracting officer of the apparent successful offeror. According to SBA officials, protests often revolve around the location of the firm's principal office or the requirement for employee residency in the HUBZone. Protested firms are allowed 5 business days to submit information in response to the protest before SBA makes a determination to decertify.

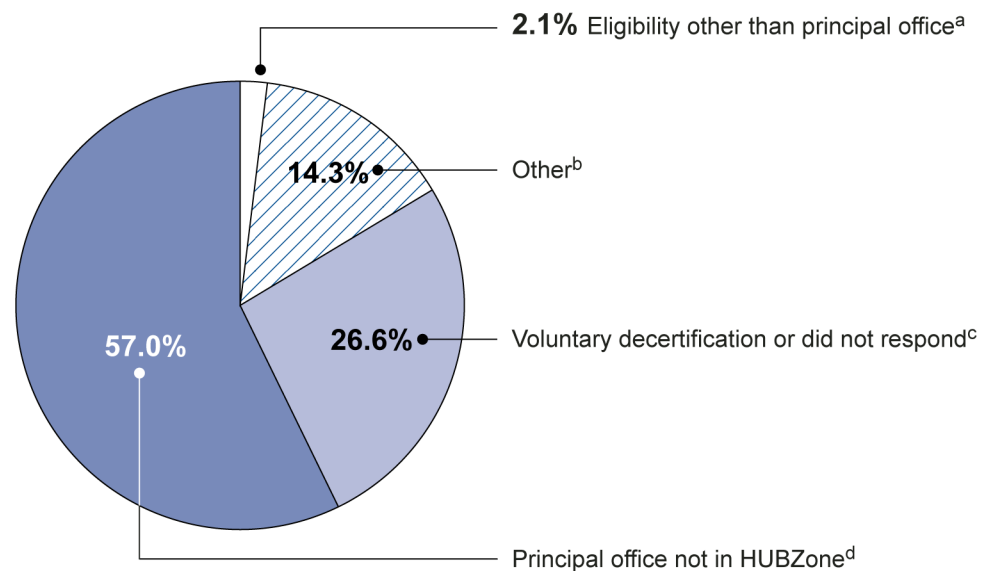
<sup>36</sup>In comparison, for fiscal years 2010 through 2013, SBA reported 345 protests for Service Disabled Veteran-Owned Small Business contracts of which 210 (61 percent) were dismissed, 61 (18 percent) were sustained, and 74 (22 percent) were denied. According to SBA officials, a denied protest occurs when SBA determines that the protested company is eligible for the award and the program.

<sup>37</sup>According to agency officials, the legacy portfolio review was conducted to validate that firms certified before SBA implemented full document review complied with the program's eligibility requirements.



not located in a HUBZone.<sup>38</sup> SBA also decertified about 2 percent of firms that applied to the program during that period because they did not meet the 35 percent employee residency requirement.

**Figure 3: Reasons for HUBZone Decertifications for Firms That Applied in Fiscal Years 2010–2013**



Source: GAO analysis of Small Business Administration data. | GAO-15-234

<sup>a</sup>This category includes 18 cases in which firms were decertified solely because they did not meet the requirement for employee residency and another 4 that were not small businesses.

<sup>b</sup>This category includes 144 cases that did not have any reason listed, and 5 “others” that a review of the comment fields revealed were mostly no longer in business.

<sup>c</sup>In 278 cases, we derived these reasons from the comment notes because the reason for the decertification was coded as “other.”

<sup>38</sup>We only reviewed the decertifications of applications SBA received between fiscal years 2010 and 2013 because SBA conducted its legacy portfolio review of firms that were certified prior to the fiscal year 2009 policy change that required a full document review for initial certification. According to agency officials, this legacy portfolio review resulted in the decertification of numerous firms. Applications received in 2014 likely would not have been decertified as of July 2014. There were 1,044 firms that applied in fiscal years 2010–2013 that became decertified. More than 70 percent (746) of these firms applied in 2010. Our review of 39 files found that of the 9 firms that were decertified, SBA decertified 6 because the firm’s principal office was no longer located in a qualified HUBZone. Three firms voluntarily decertified (2 because they no longer met the requirement for employee residency and 1 because it went out of business).

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<sup>d</sup>In addition to the 174 cases that only listed principal office as the reason, this category includes the 415 cases in which a voluntary decertification was listed as a second reason in the comments field that we reviewed and another 6 cases in which not meeting the employee eligibility requirement was indicated as a second reason.

Representatives from the HUBZone trade association noted that the employee residency requirement of 35 percent can make it difficult for a firm to stay in compliance with the program's regulations.<sup>39</sup> For example, according to the representatives, initiating and obtaining a contract may take a long time and maintaining many employees on the payroll without a contract can become a major overhead expense for firms. Furthermore, for smaller firms, losing one or two employees could result in noncompliance with the residency requirement. If firms do not maintain enough HUBZone-resident employees on payroll, they eventually lose their certification.

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## SBA Recertification Process Again Has Become Backlogged and Does Not Require Supporting Documentation

### Recurring Backlog of Recertifications

HUBZone recertifications once again have become backlogged. According to HUBZone regulations, firms wishing to remain in the program without any interruption must recertify their continued eligibility to SBA within 30 calendar days after the third anniversary of their date of certification and each subsequent 3-year period.<sup>40</sup> In June 2008, we reported that many firms were in the program for more than 3 years without being recertified.<sup>41</sup> We recommended that SBA establish a specific time frame for eliminating the backlog of recertifications and take

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<sup>39</sup>Under SBA's regulations, a HUBZone certified firm must ensure that at least 35 percent of its employees reside in a HUBZone and that it will "attempt to maintain" that level during the performance of any HUBZone contract it receives. Firms that fall below the 35 percent threshold are encouraged to voluntarily withdraw from the program, and can have an otherwise successful award protested and overturned.

<sup>40</sup>13 CFR §126.500.

<sup>41</sup>[GAO-08-643](#).

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the necessary steps to ensure that recertifications were completed in a more timely fashion in the future. In March 2009, we determined that SBA eliminated the backlog of recertifications by hiring contract staff, but had yet to implement necessary procedures to ensure that future recertifications were completed in a timely fashion.<sup>42</sup> At that time, SBA officials stated that their ongoing business process reengineering would include an assessment of the recertification process. Subsequently, in July 2012 SBA provided data illustrating that the backlog had not reoccurred and that they had recently obtained approval to replace those contract staff with 10 full-time equivalent (FTE) staff who would perform all future recertifications. We believed at that time that these steps would address the intent of our recommendation. However, SBA did not hire the 10 staff that were to replace the contract staff because, according to SBA officials, part of its funding authority was rescinded in 2013. As a result, according to SBA officials, as of September 2014 they faced a 1-year backlog for recertifying firms—that is, the agency was still recertifying firms that had their 3-year anniversaries in 2013.

SBA's current backlog indicates that it does not have processes in place to ensure that recertifications are completed in a timely fashion. SBA's current process for recertifying firms involves manual sorting of data from HCTS to identify firms whose 3-year anniversary is upcoming. Based on our analysis of SBA information for the most recent notification of firms, SBA notified almost 53 percent (375) of the firms past the deadline (that is, more than 30 days past the firms' 3-year anniversary).<sup>43</sup> We identified three firms that were last recertified in 2009. Similarly, one firm with which we spoke said it received the SBA notification 3 or more months after the 3-year anniversary.

According to SBA officials, the recertification backlog is due in part to limitations with HCTS and resource constraints. According to SBA officials, the recertification module in HCTS was designed to electronically review and approve recertification applications submitted online and alert SBA when it identified significant differences in the information firms submitted for recertification, but has not worked as intended.<sup>44</sup> As a result,

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<sup>42</sup> [GAO-09-532T](#).

<sup>43</sup> SBA provided a list of the 714 firms that received a recertification reminder in May 2014.

<sup>44</sup> As part of the recertification process, firms submit an update of the information submitted in their previous application for certification.

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the officials said that SBA has to manually identify firms that are due for recertification and only does so twice a year. According to agency officials, SBA began processing recertifications in batches in fiscal year 2013 because the agency lacked sufficient staff to do it more often.<sup>45</sup> As a result of this batching schedule, in some instances SBA has been notifying firms almost 6 months after their 3-year anniversary date. The officials also told us that they have chosen not to allow firms to initiate the recertification process, which would enable firms to recertify in a more timely way. They said that having a process in which firms would submit e-mails within 30 calendar days after their 3-year anniversary date would be inefficient due to the additional steps required. For instance, officials said that they would have to manually sort through the e-mails and remove any firms that were not due for recertification.

According to agency officials, SBA has requested funding in its fiscal year 2016 budget to enhance the current system. With this funding, SBA plans to investigate fixes for the recertification process. For example, these fixes may allow firms to submit recertification applications on their anniversary date and HCTS internal logic would ascertain compliance. For those that were noncompliant, the system could be configured to notify program staff that the recertification had to be reviewed or decertification proposed. However, it is not clear whether SBA will receive additional funding in fiscal year 2016 or changes can be made to HCTS that would allow the system to ascertain compliance with the program requirements. In the interim, SBA officials noted that the agency's goal in 2015 is to notify firms and process the recertifications on a monthly basis.

While SBA's intention is to conduct more timely recertifications, its limited efforts since 2008 to prevent backlogs have not been successful. Until SBA makes it a priority to address ongoing challenges with its recertification process and can develop an effective approach to recertify firms in a timely manner, the agency will continue to face reoccurring backlogs and risks associated with ineligible firms participating in the program.

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<sup>45</sup> Agency officials stated that as of fiscal year 2013, the program office was authorized 18 FTEs. Recently, four positions were vacated but the office was authorized to fill only two positions. As of October 2014, the program office had 16 FTEs.

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## SBA Relies on Firms' Attestations of Continued Eligibility

SBA relies on firms' attestations of continued eligibility and generally does not request supporting documentation during recertification. SBA officials told us that SBA currently only requires that firms submit a notarized recertification form stating that their eligibility information is accurate. However, internal control standards for the federal government call for ongoing monitoring of program activity and indicate that federal agencies should have control activities in place, such as verification, to ensure compliance with program requirements.<sup>46</sup> According to SBA officials, they do not believe they need to request supporting documentation from recertifying firms because all firms currently in the program have undergone a full document review, either when the firm initially applied or through the full document review SBA completed of its legacy portfolio review in fiscal year 2012, as previously discussed. While SBA officials noted that they have the authority to ask for supporting documentation when recertifying a firm, they have not done so. The SOP notes that agency staff may request and consider additional information, but it does not specify what circumstances warrant a request for supporting documentation. As previously noted, SBA officials said that the recertification process is affected by resource constraints. But as a result, SBA lacks reasonable assurance that only qualified firms are allowed to continue in the HUBZone program and receive preferential contracting treatment.

Moreover, while SBA's review of its legacy portfolio represented a comprehensive effort, it was a one-time review and took place between fiscal years 2010 and 2012. The characteristics of firms and the status of HUBZone areas—the bases for program eligibility—can often change, and need to be monitored. For example, the size of a firm and the residency location of its employees can change in 3 years. In addition, monitoring processes can take resource constraints into account. In March 2009, we found 10 of 19 firms we examined to be egregiously out of compliance with HUBZone program requirements and recommended that SBA consider incorporating a risk-based mechanism for conducting unannounced site visits as part of the screening and monitoring process.<sup>47</sup> Such a risk-based approach could be applied to SBA's recertification process to review and verify information from firms that appear to pose the most risk to the program.

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<sup>46</sup> [GAO/AIMD-00-21.3.1](#).

<sup>47</sup> [GAO-09-440](#).

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## Conclusions

Since we reported on the HUBZone program in 2008, SBA has implemented a number of actions both to better ensure that only eligible firms participate in the HUBZone program and address weaknesses with internal controls that we and the OIG identified. The frequency of changes to HUBZone designations present challenges for both firms and SBA. While SBA uses a number of mechanisms to communicate with firms about changes to HUBZone designations, these methods are insufficient as they are at a general level and not all firms may receive them. The communications are not specific to firms or HUBZone areas (for example, broadcast e-mails). Additionally, not all certified firms may be on the broadcast e-mail subscription list. As a result, not all firms may be aware of changes that would affect their continuing program eligibility.

SBA has strengthened its internal controls for initial HUBZone certifications but missed opportunities to address weaknesses in controls related to the recertification of firms. The current recertification process has a number of issues that continue to limit its effectiveness. First, SBA again has a significant backlog in processing recertifications and has not implemented a sustainable process. Second, SBA requires firms to wait until being notified before beginning recertification, but routinely notifies firms too late for the firms to meet the deadline established in HUBZone regulations. Finally, the current recertification process requires no supporting documentation—in effect, firms self-certify. SBA officials noted that resource constraints prevent a full documentation review of all recertifications and that staff can request supporting documentation (but SBA does not have guidance on when staff should request or verify documentation). While the backlog and inability of firms to start the process are concerns, the greater issue is the lack of ongoing eligibility review and verification during recertification.

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## Recommendations for Executive Action

To improve SBA's administration and oversight of the HUBZone program and reduce the risk that firms that no longer meet program eligibility criteria receive HUBZone contracts, the Administrator of SBA should take the following two actions:

- Establish a mechanism to better ensure that firms are notified of changes to HUBZone designations that may affect their participation in the program, such as ensuring that all certified firms and newly certified firms are signed up for the broadcast e-mail system or including more specific information in certification letters about how location in a redesignated area can affect their participation in the program.

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- Conduct an assessment of the recertification process and implement additional controls, such as developing criteria and guidance on using a risk-based approach to requesting and verifying firm information, allowing firms to initiate the recertification process, and ensuring that sufficient staff will be dedicated to the effort so that a significant backlog in recertifications does not recur.

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## Agency Comments

We sent a draft of this report to SBA for its review and comment. In response, SBA provided written comments, which are reproduced in appendix VI. SBA agreed with our recommendations and outlined steps it has taken or plans to take to address them. SBA stated that it has been analyzing existing resources to implement our recommendation on notifying firms of changes that could affect their participation in the program. SBA also said that by July 2015, it plans to implement an enhanced mechanism to better inform all certified and newly certified firms of HUBZone designation changes or, at least, explain how being in a redesignated area could affect program participation. In response to our recommendation on assessing the recertification process and implementing additional controls, SBA stated that it will assess the current process. In addition, SBA stated that by September 30, 2015, it plans to identify improvements to reduce the risk of fraud, waste, and abuse.

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If you or your staff have any questions concerning this report, please contact me at (202) 512-8678 or [shearw@gao.gov](mailto:shearw@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix VII.



William B. Shear  
Director, Financial Markets and  
Community Investment

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# Appendix I: Objectives, Scope, and Methodology

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This report examines the Historically Underutilized Business Zone (HUBZone) program of the Small Business Administration (SBA). More specifically, the report (1) describes HUBZone designations and how SBA communicates with interested parties about the program, and (2) examines SBA's certification and recertification processes for firms, including the extent to which SBA has implemented procedures to address recommendations previously made to improve these processes. In addition, we present information about selected characteristics of HUBZones, effects of hypothetical changes to criteria on HUBZone designations, HUBZone application processing, and selected characteristics of HUBZone firms in appendixes II, III, IV, and V, respectively.

To address both objectives, including how SBA notifies and communicates with interested parties about the HUBZone program, we reviewed previous GAO and SBA Office of Inspector General (OIG) reports; applicable statutes and regulations; and SBA documents, including Standard Operating Procedures, internal policy guidance for staff, process work guidelines, checklist of required documents, criteria used to select firms to undergo site visits, outreach and communication materials, goaling report, Congressional Budget and Performance report, and a new initiative that SBA created intended to boost HUBZones in the



federal marketplace.<sup>1</sup> We interviewed SBA staff and representatives from the HUBZone Contractors National Council—the HUBZone trade association.

We also interviewed representatives from local economic development agencies and from HUBZone firms. We selected a purposive sample of 16 HUBZone firms. To ensure a range of HUBZone firms, our sample included 8 firms that were currently certified, 4 firms that had been denied entry into the program, and 4 firms that were once certified but had been decertified.<sup>2</sup> Of the 16 firms, we interviewed 8, the findings from which cannot be generalized to the overall population of firms that have applied to the HUBZone program. To identify the firms, we relied on a multistage sampling approach:

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<sup>1</sup>The goaling report documents the achievements made towards awarding contracts to small businesses by each federal agency. In addition to reporting contracting information for the HUBZone program, the goaling report includes the total number and amount of eligible small business actions, the amounts that were small business actions, as well as the number and amount of contracts awarded through SBA's other small business contracting programs (Small Disadvantaged Businesses, 8(a), Veteran-Owned Small Businesses, Service Disabled Veteran-Owned Small Businesses, and Women Owned Small Businesses). Also see GAO, *Small Business Administration: Undercover Tests Show HUBZone Program Remains Vulnerable to Fraud and Abuse*, [GAO-10-920T](#) (Washington, D.C.: July 28, 2010); *Small Business Administration: Undercover Tests Show HUBZone Program Remains Vulnerable to Fraud and Abuse*, [GAO-10-759](#) (Washington, D.C.: June 25, 2010); *HUBZone Program: Fraud and Abuse Identified in Four Metropolitan Areas*, [GAO-09-440](#) (Washington, D.C.: Mar. 25, 2009); *HUBZone Program: Fraud and Abuse Identified in Four Metropolitan Areas*, [GAO-09-519T](#) (Washington, D.C.: Mar. 25, 2009); *Small Business Administration: Status of Efforts to Address Previous Recommendations on the HUBZone Program*, [GAO-09-532T](#) (Washington, D.C.: Mar. 25, 2009); *HUBZone Program: SBA's Control Weaknesses Exposed the Government to Fraud and Abuse*, [GAO-08-964T](#) (Washington, D.C.: July 17, 2008); *Small Business Administration: Additional Actions Are Needed to Certify and Monitor HUBZone Businesses and Assess Program Results*, [GAO-08-975T](#) (Washington, D.C.: July 17, 2008); and *Small Business Administration: Additional Actions Are Needed to Certify and Monitor HUBZone Businesses and Assess Program Results*, [GAO-08-643](#) (Washington, D.C.: June 17, 2008). Also see Small Business Administration, Office of Inspector General, *Opportunities Exist to Further Improve Quality and Timeliness of HUBZone Certifications*, 14-03 (Washington, D.C.: Nov. 19, 2013) and *HUBZone Program Examination and Recertification Processes*, 6-23 (Washington, D.C.: May 23, 2006).

<sup>2</sup>Of the 16 firms and representatives from the 4 economic development agencies and 1 Native American Tribe that we selected, we spoke with 8 firms and representatives from two of the four economic development agencies. Of the 8 firms we interviewed, 6 firms were currently certified, 1 firm had been denied, and 1 firm decertified. Of the remaining 11 entities, 2 declined to meet with us, 3 did not have a working telephone number, and 6 did not respond to our request.

- To select firms that were certified, we first selected four states, one from each of the four regions of the United States—West, Midwest, Northeast, and South. We used 2013 unemployment rates from the Bureau of Labor Statistics to select two states with higher unemployment rates and two states with unemployment rates lower than the U.S. average rate.<sup>3</sup> To ensure a mix of rural and urban states, we used 2010 Census data and calculated the percentage of each state that was rural and picked some states that had higher concentrations of rural areas. We also picked some states that had a large number of HUBZone certified firms, according to the Dynamic Small Business Search (DSBS) database, to ensure we had a sufficient number of firms from which to select firms to interview.
- We selected one county from each of the four states based on the number of certified firms located in each county that had been awarded federal contracts and firms that had not been awarded contracts in fiscal years 2010 through 2013 based on Federal Procurement Data System-Next Generation (FPDS-NG) data. We also considered the number of contracts awarded to the firms and the dollar amount of the contracts in fiscal year 2013 based on FPDS-NG data. In addition, we selected the county from each state that had a mix of certified firms with and without contracts and that had a high number of contracts awarded to firms in the county in fiscal year 2013, as compared with other counties in the state. For one state, we selected the county with the second-highest number of contracts because it represented a redesignated nonmetropolitan area.
- Within the selected counties, we selected four certified firms that had been certified in 2009 or later and had been awarded the most contracts among firms in the county from fiscal years 2010 through 2013. Based on the oldest certification date, we also selected four firms that had not received any contracts.
- Finally, we used applicant data from SBA's HUBZone Certification Tracking System (HCTS) to select four firms that were denied entry into the program and four firms that were decertified. We used the same four U.S. regions and randomly selected two firms from each region, one for each of the two categories.<sup>4</sup>

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<sup>3</sup>The U.S. unemployment rate in 2013 was 7.4 percent. The selected states had unemployment rates ranging from 5.3 to 8.9 percent.

<sup>4</sup>There were no decertified firms from the Northeast region. Therefore, we selected 2 decertified firms from the Midwest region, which had the largest number of decertified firms.

To examine how SBA designates HUBZones, selected characteristics of the areas, and how potential changes to designation criteria would affect HUBZones and firms, we reviewed applicable statutes and regulations, such as the HUBZone Act of 1997.<sup>5</sup> We also reviewed prior GAO, Congressional Research Service, and SBA OIG reports on the HUBZone program.<sup>6</sup> We accessed the list of qualified and redesignated areas from SBA's HUBZone website and plotted them using Mapinfo.<sup>7</sup> We also downloaded the list of certified firms as of June 16, 2014, and plotted those firms into their corresponding HUBZones.<sup>8</sup> According to SBA officials, firms may have more than one profile and address in DSBS and there is no way within the system to identify which address represents a principal office. Consequently, the numbers we report are based on the

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<sup>5</sup>HUBZone Act of 1997, Pub. L. No. 105-135, Title VI, 111 Stat. 2592, 2627-36 (1997).

<sup>6</sup>Congressional Research Service, *Small Business Administration HUBZone Program*, CRS R41268 (Washington, D.C.: Dec. 17, 2013); and GAO, *Small Business Administration: Undercover Tests Show HUBZone Program Remains Vulnerable to Fraud and Abuse*, [GAO-10-920T](#) (Washington, D.C.: July 28, 2010); *Small Business Administration: Undercover Tests Show HUBZone Program Remains Vulnerable to Fraud and Abuse*, [GAO-10-759](#) (Washington, D.C.: June 25, 2010); *HUBZone Program: Fraud and Abuse Identified in Four Metropolitan Areas*, [GAO-09-440](#) (Washington, D.C.: Mar. 25, 2009); *HUBZone Program: Fraud and Abuse Identified in Four Metropolitan Areas*, [GAO-09-519T](#) (Washington, D.C.: Mar. 25, 2009); *Small Business Administration: Status of Efforts to Address Previous Recommendations on the HUBZone Program*, [GAO-09-532T](#) (Washington, D.C.: Mar. 25, 2009); *HUBZone Program: SBA's Control Weaknesses Exposed the Government to Fraud and Abuse*, [GAO-08-964T](#) (Washington, D.C.: July 17, 2008); *Small Business Administration: Additional Actions Are Needed to Certify and Monitor HUBZone Businesses and Assess Program Results*, [GAO-08-975T](#) (Washington, D.C.: July 17, 2008) and *Small Business Administration: Additional Actions Are Needed to Certify and Monitor HUBZone Businesses and Assess Program Results*, [GAO-08-643](#) (Washington, D.C.: June 17, 2008). Also see Small Business Administration, Office of Inspector General, *Opportunities Exist to Further Improve Quality and Timeliness of HUBZone Certifications*, 14-03 (Washington, D.C.: Nov. 19, 2013); and *HUBZone Program Examination and Recertification Processes*, 6-23 (Washington, D.C.: May 23, 2006).

<sup>7</sup>The HUBZone designations were last updated on May 1, 2014. The lists of qualified and redesignated areas, by HUBZone type, are posted on SBA's website at <https://www.sba.gov/content/hubzone-maps>.

<sup>8</sup>The list of firms was accessed through DSBS at <http://dsbs.sba.gov/>. DSBS offers an electronic search engine for contracting officers and serves as a marketing tool for small businesses that register with the system. It contains the profiles of thousands of small firms. We were unable to locate 573 firms within qualified HUBZones. According to HUBZone regulations, the only office location which must be located in a HUBZone is the location where the greatest number of employees perform their work. The 573 firms were excluded from the analysis.

addresses in the DSBS profiles.<sup>9</sup> We were unable to plot 573 firms in a HUBZone.<sup>10</sup> For the firms we could plot, we matched these certified firms with federal procurement data from FPDS-NG to identify the number and amount of contracts that the firms received from fiscal year 2010 to fiscal year 2013. We used these data sources to identify characteristics of the different HUBZone types, such as the number of firms in the different HUBZone types as well as the contract dollars those firms received. To identify economic characteristics of the different HUBZone types, we reviewed selected economic indicators, such as the poverty and unemployment rates, and the median housing income and housing value for the different HUBZone types. We used data from the Census Bureau's American Community Survey (ACS) and unemployment data from the Bureau of Labor Statistics (BLS).<sup>11</sup> After reviewing related documentation or interviewing knowledgeable agency officials, we deemed the DSBS, FPDS-NG, Census Bureau, BLS, and SBA data sufficiently reliable for the purposes of describing the characteristics of HUBZones, participating firms, and their contracting. To determine the impact of hypothetical changes to HUBZone criteria, we reviewed county-level unemployment data from BLS. We applied different criteria to the data to determine the impact that the changes would have on the number of eligible counties, by state. For example, we used a 5- and 10-year average unemployment rate instead of the 1-year rate that SBA currently uses to determine the eligibility for nonmetropolitan counties. To determine the impact of the statutory 20 percent cap imposed on census tracts as part of the Low-Income Housing Tax Credit (LIHTC) program, we analyzed 2014 data

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<sup>9</sup>We identified 456 firms that had more than one profile listed in DSBS. For example, one firm had 13 different profiles in DSBS while a second had 10 profiles.

<sup>10</sup>The 573 firms received 834 contracts and \$396,182,258 in contract obligations in fiscal year 2013.

<sup>11</sup>ACS is an ongoing survey on topics such as social, economic, demographic, and housing characteristics of the U.S. population. The 5-year estimates from ACS are "period" estimates that represent data collected over a period of time. The primary advantage of using multiyear estimates is the increased statistical reliability of the data for less populated areas and small population subgroups. The most recent 5-year estimate covers 2008-2012. Because ACS data are based on probability samples, estimates are formed using the appropriate estimation weights provided with each survey's data. Because each of these samples follows a probability procedure based on random selection, they represent only one of a large number of samples that could have been drawn. Since each sample could have provided different estimates, we express our confidence in the precision of our particular sample's results as a 90 percent confidence interval. This is the interval that would contain the actual population value for 90 percent of the samples we could have drawn.

from the Department of Housing and Urban Development (HUD) and applied the algorithm that HUD uses to determine if a census tract qualifies, and then stopped applying the criteria prior to the imposition of the 20 percent cap.<sup>12</sup> We compared the number of areas that would qualify under both scenarios.

To examine SBA's certification and recertification processes for firms and the extent to which SBA addressed previous recommendations, we reviewed SBA's certification and recertification processes for certifying firms, including its policies and procedures for certifying and monitoring firms. To test whether SBA had implemented procedures to help ensure that only eligible firms participate in the program, we reviewed a purposive sample of 39 application case files.<sup>13</sup> To select these files, we used data from HCTS to identify the universe of applications SBA received from October 1, 2012, to September 30, 2013. We grouped these files into four outcome categories—approved, denied, withdrawn, and decertified and randomly selected 10 from each category.<sup>14</sup> We reviewed these case files and collected information using a data collection instrument (DCI) to gather information such as whether SBA staff prepared an analysis summary; analyzed information, including supporting documentation, to determine if the applicants met the program eligibility requirements; sent follow-up communications to request additional documentation; and performed a second review before making a final determination on the application. We also determined the date on which the application was received and the date of final determination. The findings from this limited review of 39 case files cannot be generalized to the overall population of applications received in fiscal year 2013.

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<sup>12</sup>The statutory provisions governing the LIHTC program limit the amount of qualified census tracts in any Metropolitan Statistical Area (MSA) or Primary Metropolitan Statistical Area (PMSA) so that they together do not contain more than 20 percent of the total population of the MSA or PMSA.

<sup>13</sup>Our universe of 1,425 firms (based on applications submitted in fiscal year 2013) consisted of 528 firms that were approved, 418 that were denied, 470 that were withdrawn, and 9 that were decertified. The 39 files we reviewed included 19 applications that were initially approved, 10 that were denied, and 10 that were withdrawn. Included in the 19 approved applications were all 9 firms that had been decertified among the 1,425 firms.

<sup>14</sup>While decertification is not one of the outcomes of an initial application, it is an event that occurs when a certified firm no longer meets the program eligibility requirements.

We developed the DCI after reviewing SBA's regulations, its description of the HUBZone current certification process, and the HUBZone policy guidance, document request checklist, and process work guidelines. Two GAO team members independently entered information from one sample case file using the DCI and compared the results. After the two team members agreed on the final fields to be used in the DCI, they entered information from the case files into the DCI. A third staff member verified the accuracy of the entries.

Using HCTS data, we analyzed data about firms for which applications were received from fiscal years 2008 through 2013, by year of receipt, to determine (1) the number of applications approved, denied, or withdrawn; (2) the number of firms that had been recertified; (3) the number that had been decertified; (4) the length of time it took SBA to approve applications; and (5) the reasons firms were decertified. We also analyzed HCTS data to examine the characteristics of HUBZone applicant firms, including the industry codes and number of employees. A copy of the HCTS data was originally provided to GAO in Oracle format and was the most current version as of July 2014. These data were then read in using SAS software to allow for analysis. Before conducting the analysis, a GAO data analyst reviewed the data for inconsistencies and completeness. As a part of this work, inconsistencies related to the effective dates of different processes were discovered. We determined that the data were sufficiently reliable for the analysis we report by reviewing related documentation, interviewing knowledgeable officials, and electronic testing of the data, but there were internal inconsistencies that limited our reporting. Specifically, in some cases, there were conflicting outcomes or dates that appeared to be out of sequence or illogical. In particular, the dates associated with events in the certification review processes were found to be unreliable. To clarify, GAO met with SBA and learned that the inconsistencies were related to manual data entry processes that were required since fiscal year 2006 because of deficiencies discovered in the software related to the recertification module in HCTS. We concluded that while the actual outcomes were reliable enough to report, the data that relied on the effective dates of these outcomes were not sufficiently reliable to report.

To identify the eligibility-related reasons for decertification, we analyzed the reason field contained in HCTS for applications received from 2010 to

2013 that were later decertified.<sup>15</sup> Because a large percentage of these applications had “other” for their recorded reason, we conducted a review of the comments field to code for the possible other reasons.<sup>16</sup> To conduct that review, the GAO data analyst did a string search of the text using keywords such as “35 percent” and “principal office” and identified one additional category and added additional cases to existing reasons. An analyst reviewed a subset of the coding to ensure accuracy.

To determine whether SBA implemented procedures to help ensure that only eligible firms continue to participate in the program, we assessed SBA’s recertification process. We reviewed SBA’s regulations on recertification and information from HCTS relating to firms’ certification anniversary dates and SBA’s e-mail notification for firms to recertify.<sup>17</sup> We assessed the reliability of the data on these processes by interviewing officials knowledgeable about the data and performing electronic data testing to detect errors in completeness and reasonableness. We determined that they were sufficiently reliable for the purpose of identifying the amount of time between a firm’s prior certification and SBA’s notice about recertification. We compared SBA’s certification and recertification processes with federal internal control standards for collecting documentation and verifying information.<sup>18</sup>

We conducted this performance audit from April 2014 to February 2015 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.

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<sup>15</sup>We only reviewed the decertifications of firms from which SBA received applications from fiscal years 2010 through 2013 because SBA conducted its legacy portfolio review in fiscal 2010, which resulted in the decertification of numerous firms. Applications submitted 1 year later would be less likely to be decertified as a result of this review, and would be decertified for reasons more typical to SBA’s normal operations.

<sup>16</sup>According to SBA officials, analysts only can record one reason for decertifying firms. If an analyst wants to record additional information, they must choose “other” and record in the comments section the reason for the decertification.

<sup>17</sup>SBA provided a list of the 714 firms that received a recertification reminder in May 2014.

<sup>18</sup>[GAO/AIMD-00-21.3.1.](#)

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# Appendix II: Characteristics of HUBZones

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There are four different types of qualified HUBZone areas as defined by federal statute.

- **Qualified census tracts.** The qualified census tracts are the same as those determined by HUD for the LIHTC program. The current criteria are any census tract that is designated by HUD and, for the most recent year for which census data are available on household income in such tract, has (1) at least 50 percent of households with income below 60 percent of the median gross income of the MSA (in metropolitan census tracts) or for all nonmetropolitan areas of the state (in nonmetropolitan census tracts) or (2) a poverty rate of at least 25 percent. The LIHTC program limits the amount of qualified census tracts in any MSA or PMSA so that they together do not contain more than 20 percent of the total population of the MSA or PMSA. As such, it is possible for a tract to meet one or both of the criteria, but not be designated as a qualified census tract.
- **Qualified nonmetropolitan county.** A qualified nonmetropolitan county is any county that was not located in an MSA at the time of the most recent census. To qualify, the (1) median household income for the county must be less than 80 percent of the nonmetropolitan state median household income, based on the most recent data available from the Bureau of the Census; or (2) the unemployment rate is not less than 140 percent of the average unemployment rate for the United States or for the state in which such county is located, whichever is less, based on the most recent data available from the Secretary of Labor. SBA uses a 5-year median income, as determined through the ACS. The most recent update reflected data from 2008-2012. The unemployment rate is derived from data released annually by BLS and is typically sent to SBA during May, June, or July. Additionally, nonmetropolitan counties can qualify if they include a difficult development area, as designated by HUD, within Alaska, Hawaii, or any territory or possession of the United States outside of the 48 contiguous states.<sup>1</sup>

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<sup>1</sup>Difficult development areas are designated annually, typically in September or October, by the Secretary of HUD in accordance with Section 42(d)(5)(B)(iii) of the Internal Revenue Code, which applies to the LIHTC program. This section of the Internal Revenue Code defines difficult development areas as “any area designated by the Secretary of HUD as an area which has high construction, land, and utility costs relative to area median gross income.”



- **Qualified Indian land.** Lands within the boundaries of Indian reservations may qualify as a HUBZone area.<sup>2</sup> The Bureau of Indian Affairs provides data delineating these areas.
- **Qualified base closure area.** HUBZone eligibility is extended for 5 years to lands within the external boundaries of a military installation closed through a privatization process under the authority of various base closure laws. The military base's HUBZone eligibility commences on the effective date of the law (Dec. 8, 2004) if the military base already was closed at that time, or on the date of formal closure if the military base was still operational at that time. According to SBA officials, no HUBZone firms are located in these areas because it is very difficult for firms to meet the 35 percent residency requirement. Additionally, the SBA officials noted that, according to statute, the areas are only eligible for 5 years from the date of base closure, and it may take several years before the area is able to receive business leases, leaving applicant firms with only 1 to 2 years of eligibility.

According to our analysis, about 2,600 of the approximately 5,200 certified firms were in a qualified or redesignated census tract, as of June 2014 (see table 2).<sup>3</sup> Additionally, about 12 percent of the firms were located simultaneously in at least two types of HUBZones. Most commonly, firms were located in both a qualified census tract and qualified nonmetropolitan county (311 firms) or a qualified census tract and Indian land (107 firms). However, about 88 percent of HUBZones—including all the base realignment and closure areas—did not contain any certified firms (that we could geographically code).

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<sup>2</sup>Trust lands acquired by an Indian reservation or tribe after December 21, 2000, do not qualify as HUBZones, unless they are part of a former reservation, or they are contiguous to areas that were trust lands prior to December 21, 2000.

<sup>3</sup>We were unable to identify the HUBZone locations for 573 firms, which are excluded from the counts.

Table 2: Selected Characteristics of HUBZones, by Type

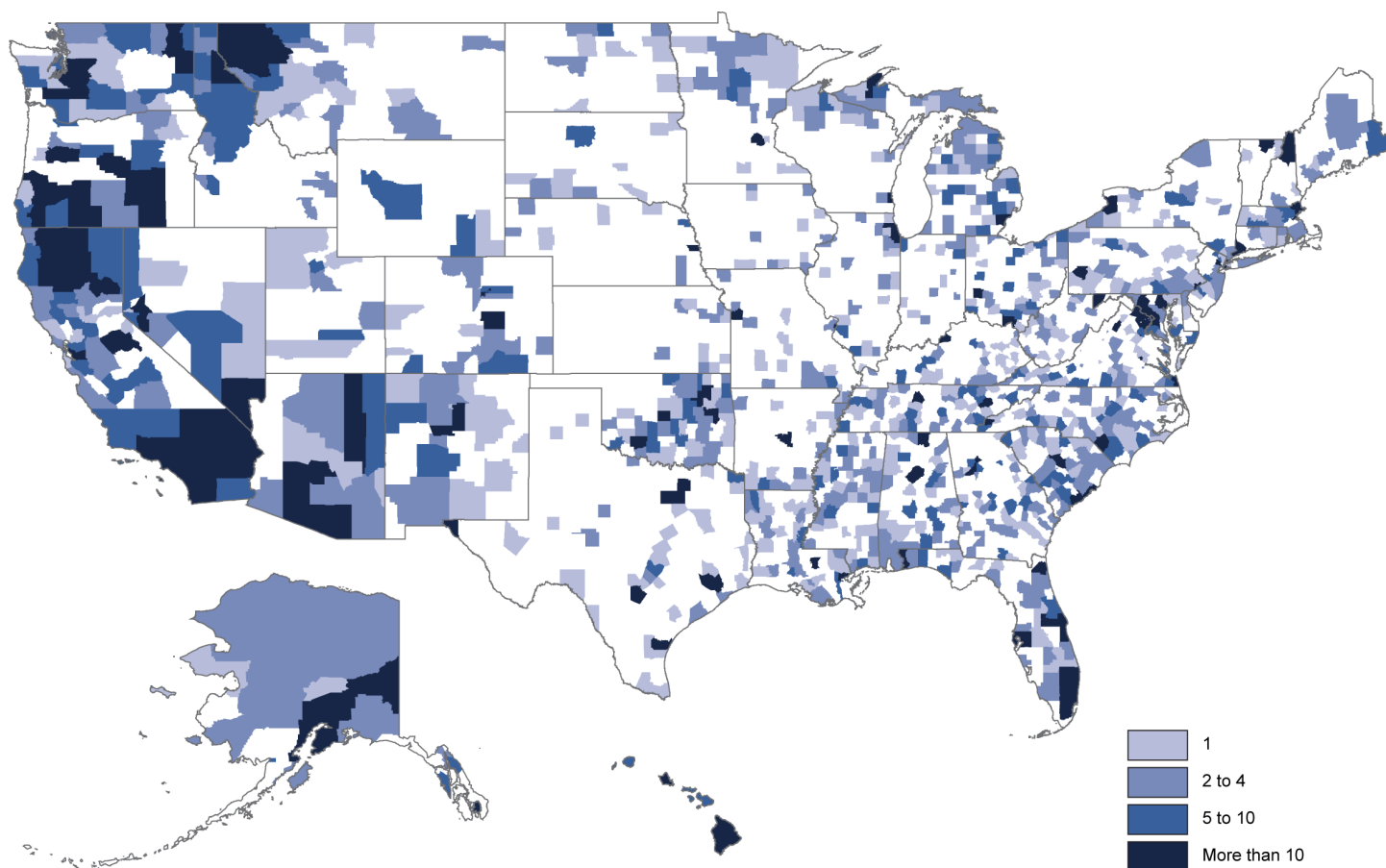
HUBZone type	Number of areas, as of June 2014	Number of certified firms, as of June 2014	Percent of type with 0 certified firms	Percent of type with five or more certified firms	Number of contracts awarded to firms in area, FY13	Amount of contract obligations firms in area, FY13 (dollars in millions)
Census tracts						
Qualified	13,635	2,077	90%	0	7,081	\$2,124
Redesignated	3,377	520	92	1	1,842	695
Nonmetropolitan counties						
Qualified	546	1,641	40	17	2,407	784
Redesignated	250	351	51	11	845	101
Qualified Indian land	618	600	83	4	1,554	387
Qualified base closure area	115	0	100	0	0	0
<b>Total</b>	<b>18,541</b>	<b>5,189</b>	<b>88</b>	<b>1</b>	<b>13,729</b>	<b>\$4,092</b>

Source: GAO analysis of SBA data. | GAO-15-234

Notes: Totals may not sum due to rounding; FY refers to fiscal year.

In fiscal year 2013, certified firms received, on average, about \$789,000 through HUBZone contracts. Firms in qualified census tracts received about \$1 million in contracts, with those in redesignated areas receiving about \$300,000 more, each. Firms in all redesignated areas were obligated almost \$800 million in federal contracts in fiscal year 2013. Overall, 211 firms comprised the top 10 percent, in terms of the size of contracts received, while almost 4,300 comprised the bottom 10 percent.

As shown in figure 4, there are certified firms in all 50 states. In general, counties in the West had more certified firms, on average, than counties elsewhere in the United States.

**Figure 4: Density of Certified HUBZones Firms (by County), as of June 2014**

Sources: GAO (analysis), Small Business Administration (data), and MapInfo (map). | GAO-15-234

As shown in table 3, California, New York, and Texas had the largest number of qualified areas. California, Oklahoma, Texas, and Virginia all had more than 200 certified firms, with California having the most (477).

**Table 3: Number of HUBZones, Certified Firms, and Contract Obligations, by State, as of June 2014**

	Number of qualified areas	Number of certified firms	Amount obligated, FY13
Alabama	405	104	78,586,364
Alaska	280	159	\$88,487,940
American Samoa	17	.	.
Arizona	378	77	41,299,272
Arkansas	203	35	10,483,902
California	2,079	477	564,100,738
Colorado	264	79	15,829,213
Connecticut	188	17	1,442,952
Delaware	27	3	466,705
District of Colombia	109	155	109,485,403
Florida	809	186	234,340,665
Georgia	560	162	174,072,543
Guam	28	167	128,964,221
Hawaii	88	71	75,766,553
Idaho	51	89	83,909,574
Illinois	744	76	19,892,482
Indiana	330	30	2,707,780
Iowa	104	22	13,017,698
Kansas	128	18	14,463,737
Kentucky	374	73	82,357,023
Louisiana	430	86	41,587,386
Maine	42	15	5,495,869
Maryland	276	161	139,008,297
Massachusetts	368	49	54,448,247
Michigan	701	185	116,704,791
Minnesota	204	41	8,308,223
Mississippi	257	105	54,023,857
Missouri	326	66	36,285,986
Montana	82	145	10,606,722
Nebraska	111	27	28,582,530
Nevada	128	47	48,513,669
New Hampshire	24	28	16,120,234
New Jersey	387	37	23,556,400
New Mexico	171	80	67,873,829

	Number of qualified areas	Number of certified firms	Amount obligated, FY13
New York	1,296	105	178,704,178
North Carolina	512	159	80,755,973
North Dakota	62	19	6,323,891
Northern Mariana Islands	13	8	205,331
Ohio	816	155	97,311,847
Oklahoma	321	335	278,823,395
Oregon	133	165	41,318,162
Pennsylvania	828	82	26,148,010
Puerto Rico	340	24	29,650,270
Rhode Island	60	4	13,029,555
South Carolina	302	110	47,818,818
South Dakota	69	20	5,363,314
Tennessee	419	130	137,520,766
Texas	1,518	249	292,180,004
Utah	92	23	38,299,082
Vermont	19	13	3,365,441
Virgin Islands	14	21	749,173
Virginia	342	242	311,491,440
Washington	269	146	44,970,704
West Virginia	183	50	48,611,616
Wisconsin	240	39	17,988,294
Wyoming	20	18	148,266
<b>Total</b>	<b>18,541</b>	<b>5,189</b>	<b>\$ 4,091,568,333</b>

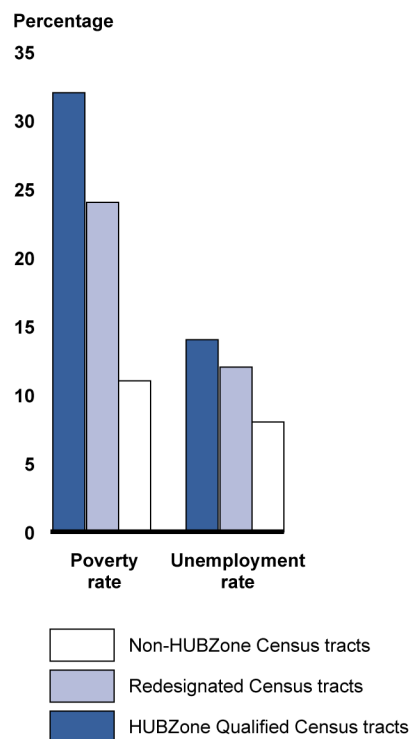
Source: GAO analysis of SBA data. | GAO-15-234

Note: FY refers to fiscal year.

## Economic Characteristics of HUBZones

Our analysis of the economic conditions of qualified and redesignated areas as of 2012 found that redesignated areas had, on average, economic conditions between those of qualified and nonqualified areas. For example, as shown in figure 5, qualified census tracts had poverty and unemployment rates of 32 percent and 14 percent, respectively, while nonqualified census tracts had poverty and unemployment rates of 11 percent and 8 percent, respectively. In contrast, the poverty rate in redesignated census tracts was 24 percent while the unemployment rate was 12 percent.

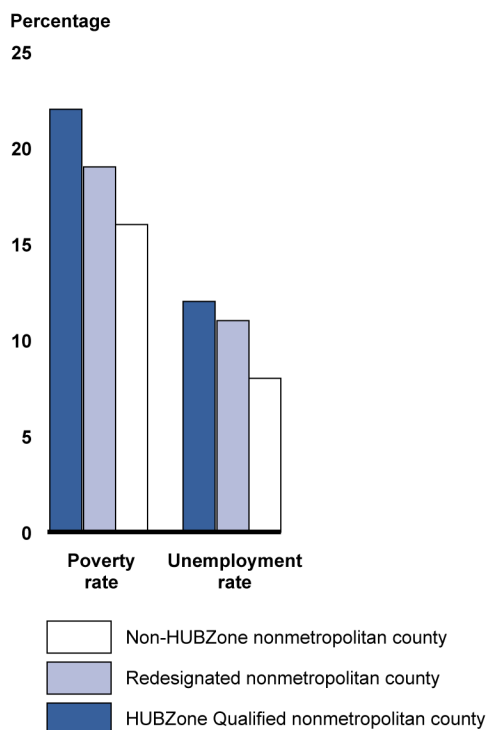
**Figure 5: Comparison of Unemployment and Poverty Rates by Census Tract HUBZone Eligibility Status, as of 2012**



Source: GAO analysis of Bureau of Labor Statistics and American Community Survey data. | GAO-15-234

As shown in figure 6, a similar pattern exists for qualified, redesignated, and nonqualified nonmetropolitan counties.

**Figure 6: Comparison of Unemployment and Poverty Rates by Nonmetropolitan County HUBZone Eligibility Status, as of 2012**



Source: GAO analysis of Bureau of Labor Statistics and American Community Survey data. | GAO-15-234

As shown in table 4, our analysis of various economic indicators for qualified, redesignated, and non-HUBZone areas found that qualified areas had, on average, higher poverty and unemployment rates, and lower median household income and housing values than either redesignated or non-HUBZone areas. Redesignated areas had, on average, economic indicators between those of qualified and not qualified areas.

**Table 4: Comparison of Selected Economic Indicators for Census Tracts (HUBZone and Non-HUBZone), as of 2012**

	<b>Percent in poverty</b>	<b>Unemployment rate</b>	<b>Average median household income</b>	<b>Average median housing value</b>
HUBZone qualified census tracts	31.5%	13.9%	\$32,200	\$158,701
Redesignated census tracts	23.6	12	40,383	207,738
Non-HUBZone census tracts	11	8.3	63,643	243,259

Source: American Community Survey (data).| GAO-15-234

Note: ACS is an ongoing survey that covers topics such as the social, economic, demographic, and housing characteristics of the U.S. population. The 5-year estimates from ACS represent data collected over a period of time. The primary advantage of using multiyear estimates is the increased statistical reliability of the data for less populated areas and small population subgroups. The most recent 5-year estimate covers 2008-2012.

As shown in figure 7, about 55 percent of qualified census tracts had poverty rates of 30 percent or more. In contrast, almost 76 percent of redesignated census tracts had poverty rates between 10 percent and 29.9 percent. Similarly, almost 72 percent of qualified census tracts had unemployment rates greater than 10 percent, whereas about 40 percent of redesignated areas and 70 percent of nonqualified areas had unemployment rates of less than 10 percent.



**Figure 7: Comparison of Selected Economic Indicators for Census Tracts (HUBZone and Non-HUBZone), as of 2012**

		Qualified census tracts		Redesignated census tracts		Non-HUBZone census tracts	
		Number	Percentage	Number	Percentage	Number	Percentage
Poverty rate by census tracts	Less than 10%		553 3.6		62 5.3 <sup>a</sup>		28,054 50.4
	10.0 - 19.9%		1,809 11.8		324 27.9		20,580 37.0
	20.0 - 29.9%		4,487 29.3		555 47.8		6,120 11.0
	30.0 - 39.9%		4,617 30.1		173 14.9 <sup>a</sup>		775 1.4
	40% or more		3,857 25.2		48 4.1 <sup>a</sup>		152 0.3 <sup>a</sup>
Unemployment rate by census tracts	Less than 5%		899 5.9		102 9.0 <sup>a</sup>		12,096 21.7
	5.0 - 9.9%		3,419 22.4		349 30.6		26,877 48.3
	10.0 - 14.9%		4,329 28.4		349 30.6		12,313 22.1
	15.0 - 19.9%		3,197 20.9		204 17.9		3,385 6.1
	20% or more		3,422 22.4		135 11.9 <sup>a</sup>		977 1.8
Ratio of income to state average by census tracts	Less than 40%		2,256 14.7		11 1.0 <sup>a</sup>		28 0.1 <sup>a</sup>
	40.0 - 49.9%		2,807 18.3		74 6.4 <sup>a</sup>		172 0.3 <sup>a</sup>
	50.0 - 59.9%		3,411 22.3		207 18.0		1,042 1.9
	60.0 - 69.9%		2,941 19.2		254 22.0		2,991 5.4
	70% or more		3,901 25.5		606 52.6		51,573 92.4
Ratio of home value to state average by census tracts	Less than 40%		2,397 16.1		124 11.1		1,569 2.8
	40.0 - 49.9%		2,070 13.9		110 9.8 <sup>a</sup>		2,149 3.9
	50.0 - 59.9%		2,220 14.9		153 13.7		3,352 6.0
	60.0 - 69.9%		1,994 13.4		136 12.1 <sup>a</sup>		4,677 8.4
	70% or more		6,225 41.8		597 53.3		43,839 78.9

Source: American Community Survey (data). | GAO-15-234

<sup>a</sup>Estimated number of tracts have 90 percent confidence intervals no wider than +/- 31 tracts. All other tract estimates have 90% confidence intervals within +/- 10% of the estimate itself. All percentage estimates have 90 percent confidence intervals within +/- percentage points of the estimate itself.

Similarly, our analysis of various nonmetropolitan counties found that redesignated areas had, on average, economic indicators between those of qualified and not qualified areas (see table 5). However, redesignated nonmetropolitan counties had a lower average median housing value than either qualified or not-qualified HUBZone counties.

**Table 5: Comparison of Selected Economic Indicators for Nonmetropolitan Counties (HUBZone and Non-HUBZone), as of 2012**

	Percent in poverty	Unemployment rate	Average median household income	Average median housing value
HUBZone qualified counties	22.2%	11.9%	\$36,193	\$104,515
Redesignated counties	18.5	10.7	40,030	95,794
Non-HUBZone counties	15.8	8.1	44,410	115,026

Source: American Community Survey (data). | GAO-15-234

As shown in figure 8, about 16 percent of qualified nonmetropolitan counties had poverty rates of at least 30 percent. In contrast, less than 1 percent of redesignated or nonqualified nonmetropolitan counties had a poverty rate of at least 30 percent. Similarly, 22 percent of qualified areas had an unemployment rate of at least 15 percent, while about 7 percent of redesignated counties and 1 percent of nonqualified counties had a similar level.

**Figure 8: Comparison of Selected Economic Indicators for Nonmetropolitan Counties, by Qualification Status, as of 2012**

		Qualified nonmetropolitan counties		Redesignated nonmetropolitan counties		Non-HUBZone nonmetropolitan counties	
		Number	Percentage	Number	Percentage	Number	Percentage
Poverty rate by non-metropolitan counties	Less than 10%	15	2.9 <sup>a</sup>	16	6.4 <sup>a</sup>	187	14.6
	10.0 - 19.9%	202	38.5	145	58.0	865	67.6
	20.0 - 29.9%	225	42.9	87	34.8	223	17.4
	30.0 - 39.9%	69	13.2 <sup>a</sup>	2	0.8 <sup>a</sup>	4	0.3 <sup>a</sup>
	40% or more	13	2.5 <sup>a</sup>	0	0.0	0	0.0
Unemployment rate by non-metropolitan counties	Less than 5%	36	6.9 <sup>a</sup>	42	17.0 <sup>a</sup>	334	26.1
	5.0 - 9.9%	165	31.6	96	38.9 <sup>a</sup>	713	55.8
	10.0 - 14.9%	206	39.5	92	37.2 <sup>a</sup>	219	17.1
	15.0 - 19.9%	92	17.6 <sup>a</sup>	15	6.1 <sup>a</sup>	11	0.9 <sup>a</sup>
	20% or more	23	4.4 <sup>a</sup>	2	0.8 <sup>a</sup>	1	0.1 <sup>a</sup>
Ratio of income to state non-metropolitan areas average by non-metropolitan counties	Less than 40%	1	0.2 <sup>a</sup>	0	0.0	0	0.0
	40.0 - 49.9%	15	2.9 <sup>a</sup>	0	0.0	1	0.1 <sup>a</sup>
	50.0 - 59.9%	75	14.3 <sup>a</sup>	2	0.8 <sup>a</sup>	2	0.2 <sup>a</sup>
	60.0 - 69.9%	144	27.5	29	11.6 <sup>a</sup>	55	4.3 <sup>a</sup>
	70% or more	289	55.2	219	87.6	1,222	95.5
Ratio of home value to state nonmetropolitan areas average by nonmetropolitan counties	Less than 40%	47	9.0 <sup>a</sup>	10	4.0 <sup>a</sup>	53	4.1
	40.0 - 49.9%	99	18.9	42	16.8 <sup>a</sup>	117	9.1
	50.0 - 59.9%	111	21.2	49	19.6 <sup>a</sup>	223	17.4
	60.0 - 69.9%	114	21.8	49	19.6 <sup>a</sup>	245	19.1
	70% or more	152	29.1	100	40.0	642	50.2

Source: American Community Survey (data). | GAO-15-234

<sup>a</sup>Estimated number of counties have 90 percent confidence intervals no wider than +/- 13 counties. All other county estimates have 90% confidence intervals within +/- 10% of the estimate itself. All percentage estimates have 90 percent confidence intervals within +/- percentage points of the estimate itself.

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# Appendix III: Impact of Hypothetical Changes to HUBZone Criteria on HUBZone Designations

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We applied hypothetical changes to selected statutory criteria for designating HUBZones to illustrate how such changes could affect the number of eligible areas. As we reported in 2008, establishing new HUBZone areas could provide economic benefits to these new areas, but also could result in diffusion—decreased targeting of areas of greatest economic distress—by lessening the competitive advantage upon which small businesses may rely to thrive in economically distressed communities.<sup>1</sup>

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## Impact of Adjustments in the Unemployment Rate Used

As discussed earlier in this report, one of the ways in which a nonmetropolitan county can qualify as a HUBZone is based on its unemployment rate. More specifically, the unemployment rate for the nonmetropolitan county must not be less than 140 percent of the average unemployment rate for the United States or for the state in which the county is located, whichever is less, based on the most recent data available from the Department of Labor.<sup>2</sup> Adjustments could make this definition more uniform across all of the states.

Under the current definition, two counties in different states with the same unemployment rate would not necessarily both qualify as HUBZones, depending on the unemployment rate of the state in which they are located. In general, every county in a state with an unemployment rate less than the U.S. average would qualify as a HUBZone if its unemployment rate was at least 140 percent of the state's (even if it was less than the U.S. average). In contrast, counties in states with unemployment rates higher than the U.S. average must have an unemployment rate at least equal to 140 percent of the U.S. average to qualify as a HUBZone.

We analyzed the impact on the number of nonmetropolitan counties that could qualify under a variety of adjustments to the current definition.

- **Current definition.** Under the current definition, 424 nonmetropolitan counties would qualify as a HUBZone.

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<sup>1</sup>[GAO-08-643](#).

<sup>2</sup>The unemployment rates in 2013 ranged from 2.9 percent (North Dakota) to 9.8 percent (Nevada), while the U.S. average was 7.4 percent. SBA updates these designations each May using the previous year's unemployment rate.

- **Lowest state unemployment rate.** If 140 percent of the lowest state unemployment rate (2.9 percent) was applied to all counties and states, almost 1,700 counties would qualify. Under this scenario, for example, Texas would go from 16 qualified nonmetropolitan counties to almost 150.
- **Highest state unemployment rate.** If 140 percent of the highest state unemployment rate (9.8 percent) was applied to all counties and states, there would only be 54 qualified nonmetropolitan counties nationwide. Thirty-four states would not have any qualified nonmetropolitan counties, while Kentucky and Mississippi would have the most, with 9 each.
- **Applying U.S. average unemployment rate.** If 140 percent of the U.S. average unemployment rate (7.4 percent) was applied uniformly to all counties and states, 301 nonmetropolitan counties would qualify.
- **Average of all state unemployment rates.** If 140 percent of the average of all state unemployment rates (6.8 percent) was used, about 450 counties would qualify.<sup>3</sup> Under this scenario, states with relatively high unemployment rates would have additional nonmetropolitan counties (such as Georgia, which would have 17 additional qualifying counties), while states with relatively low unemployment rates would have fewer qualifying counties (such as Virginia, which would have 20 fewer).

In addition to comparing all nonmetropolitan counties against the same unemployment rate, the qualifying criteria could be changed from the current standard (data from 1 year) to use a 5- or 10-year average unemployment rate to determine if a nonmetropolitan county qualified for the program.<sup>4</sup> Such a change could minimize the wide variations that can occur by using the 1-year rates. For example, the average unemployment rates that equaled 140 percent of the U.S. unemployment rate ranged from 6.4 percent in 2006 and 2007 to 13.4 percent in 2010. Similarly, the difference between the states with the highest and lowest unemployment rates ranged from 6 percentage points in 2004 to about 14 percentage points in 2010. However, using a 5- or 10-year average unemployment rate would result in fewer counties qualifying as a HUBZone.

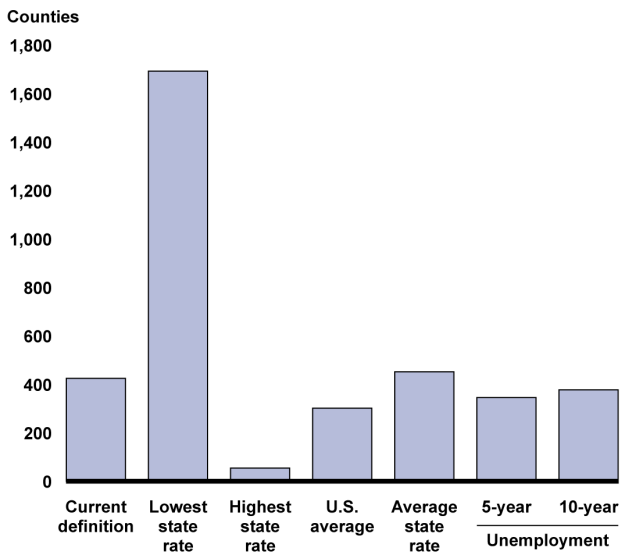
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<sup>3</sup>Both the average and median state unemployment rates in 2013 were 6.8 percent.

<sup>4</sup>As discussed earlier, SBA uses a 5-year average median household income as one method to determine if a nonmetropolitan county qualifies as a HUBZone.

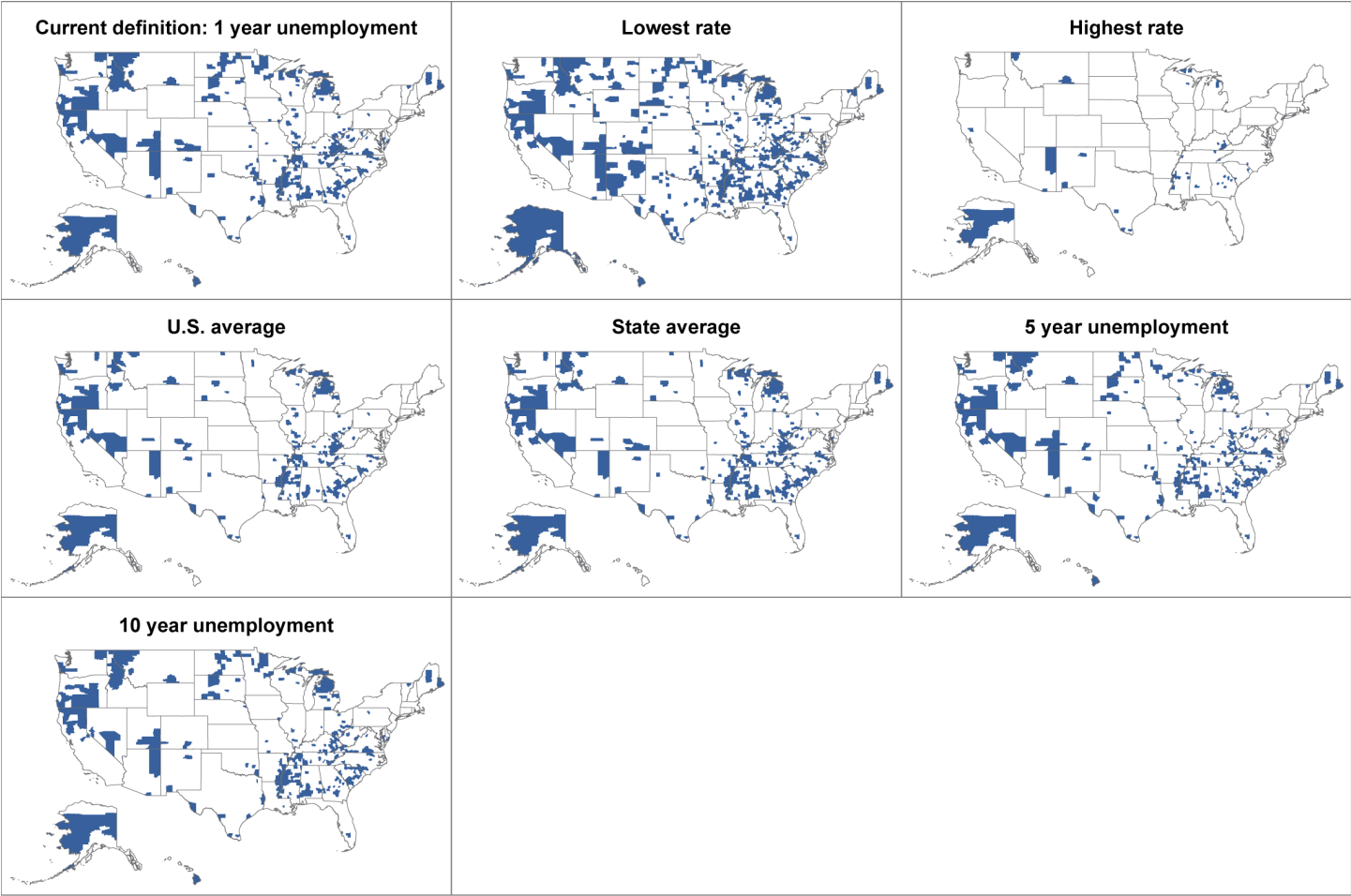
- **Using a 5-year unemployment rate.** If a 5-year average unemployment rate were used, 345 nonmetropolitan counties would qualify. With the change from 1- to 5-year, additional counties in 6 states would become eligible, while the number of eligible counties in 21 states would decrease. The net number of affected counties would range from 6 added to 15 eliminated.
- **Using a 10-year unemployment rate.** If a 10-year average unemployment rate were used, 377 nonmetropolitan counties would qualify. Under this adjustment, 10 states would have more counties eligible and 18 would have fewer. See figures 9 and 10 for a summary of the impact of each potential change on the number of qualified nonmetropolitan counties.

**Figure 9: Effect on Nonmetropolitan Counties of Using Different Unemployment Criteria**



Source: GAO analysis. | GAO-15-234

Figure 10: Map of Nonmetropolitan Counties under Different Unemployment Criteria



Source: MapInfo. | GAO-15-234

As shown in table 6, the impact of the hypothetical changes on the number of qualified nonmetropolitan counties in the individual states varies.

**Appendix III: Impact of Hypothetical Changes  
to HUBZone Criteria on HUBZone Designations**

**Table 6: Number of Nonmetropolitan Counties by State That Would Qualify If Different Unemployment Rates Were Used**

State	Current definition (1- year rate)	Lowest state rate applied to all states	Highest state rate applied to all states	U.S. average	Average state rate	5-year average	10-year average
Alabama	12	38	1	6	11	13	14
Alaska	12	25	5	9	11	11	12
Arizona	3	7	3	3	3	3	3
Arkansas	11	55	0	11	15	9	12
California	13	21	1	13	15	14	13
Colorado	5	41	0	3	5	3	3
Connecticut	0	1	0	0	0	0	0
Delaware	0	0	0	0	0	0	0
Florida	1	23	0	1	1	1	1
Georgia	33	85	6	33	50	26	17
Hawaii	1	2	0	0	0	1	1
Idaho	8	31	0	5	6	6	7
Illinois	17	62	0	17	28	2	5
Indiana	0	48	0	0	3	1	1
Iowa	3	61	0	0	0	2	2
Kansas	2	40	0	0	0	2	0
Kentucky	30	85	9	30	40	20	25
Louisiana	7	29	1	3	7	7	7
Maine	2	11	0	0	2	2	3
Maryland	1	5	0	0	1	1	1
Massachusetts	0	3	0	0	0	0	0
Michigan	35	57	5	35	42	30	40
Minnesota	10	53	0	1	1	5	10
Mississippi	29	65	9	29	39	21	32
Missouri	2	81	0	0	2	4	3
Montana	8	38	2	4	6	8	8
Nebraska	3	14	0	0	0	2	1
Nevada	5	12	0	5	6	5	2
New Hampshire	0	7	0	0	0	0	0
New Jersey	0	0	0	0	0	0	0
New Mexico	2	25	2	2	2	2	2
New York	0	24	0	0	1	0	0
North Carolina	14	54	2	14	27	16	13
North Dakota	13	13	0	1	1	8	10

**Appendix III: Impact of Hypothetical Changes  
to HUBZone Criteria on HUBZone Designations**

State	Current definition (1- year rate)	Lowest state rate applied to all states	Highest state rate applied to all states	U.S. average	Average state rate	5-year average	10-year average
Ohio	8	50	0	8	15	8	12
Oklahoma	6	42	0	0	1	3	3
Oregon	8	23	0	8	10	8	9
Pennsylvania	1	30	0	1	1	1	1
Rhode Island	0	0	0	0	0	0	0
South Carolina	9	20	2	9	14	15	16
South Dakota	10	19	0	3	3	9	9
Tennessee	29	53	2	29	39	20	25
Texas	16	148	3	7	12	14	10
Utah	4	14	0	1	1	4	4
Vermont	1	10	0	0	0	1	1
Virginia	29	53	0	1	9	24	25
Washington	5	18	0	5	6	4	5
West Virginia	9	34	0	2	8	6	6
Wisconsin	7	46	1	2	7	3	3
Wyoming	0	16	0	0	0	0	0
<b>Total</b>	<b>424</b>	<b>1,692</b>	<b>54</b>	<b>301</b>	<b>451</b>	<b>345</b>	<b>377</b>

Source: GAO. | GAO-15-234.

## Impact of Removing Limit in Census Tracts

Currently, HUBZone-qualified census tracts are those census tracts designated by HUD.<sup>5</sup> Statutory provisions governing the LIHTC program limit the amount of qualified census tracts in any MSA or PMSA to no more than 20 percent of the total population of the MSA or PMSA.<sup>6</sup> Consequently, some census tracts that may qualify for the HUBZone program based on the area's median household income or poverty rate might not be designated as qualified census tracts because of the population cap, and are therefore not included in the HUBZone program.

<sup>5</sup>LIHTC provides tax credits for building and rehabilitating rental housing that is affordable to low-income households. The Internal Revenue Service and state housing finance agencies jointly administer the program. HUD is not an administering agency for the LIHTC program, but collects information on projects and tenants for its LIHTC database, the most comprehensive public source of information on LIHTC projects.

<sup>6</sup>For purposes of the rule, all nonmetropolitan areas in a state are treated as if they constituted a single metropolitan area. See 26 U.S.C §42(d)(5)(B)(ii)(III). As previously discussed, SBA reassesses the status of nonmetropolitan counties more frequently than it reassesses the status of census tracts.



Our analysis of data HUD used for its 2014 designations found that about 2,400 more census tracts would qualify as HUBZone areas if the 20 percent cap were not in place, an increase of 15 percent from the current number of qualified tracts.<sup>7</sup> Eight states or territories would have at least 20 percent more qualified areas if all eligible tracts were included.

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<sup>7</sup>As of June 2014, there were 17,012 qualified and redesignated census tracts. About 2,600 certified firms were located in these qualified or redesignated census tracts, as of June 2014.

# Appendix IV: Summary Data Relating to HUBZone Application Processing

According to our analysis of data for applications received by SBA during fiscal years 2008-2013, the number of applications submitted by firms declined significantly from 2009 through 2011 (from a high of about 4,500 in 2009 to under 1,500 in 2013).<sup>1</sup> Since 2009, the application approval rate also declined. For example, SBA approved about 32 percent of the approximately 4,000 applications submitted in 2010 (shortly after the new process was implemented), while it approved almost 53 percent of the approximately 3,000 applications submitted in 2008 under the previous process (see table 7 and fig. 11). In general, a higher percentage of applications have been withdrawn since SBA implemented the revised process—more than 50 percent of applications for every year except 2013.<sup>2</sup> According to SBA officials, firms can withdraw an application or SBA can close it if it is believed that the firm will not meet program requirements.<sup>3</sup>

**Table 7: Number and Status of Applications for HUBZone Program Submitted in Fiscal Years 2008-2013**

	2008	2009	2010	2011	2012	2013
Applications submitted	2,977	4,511	4,051	3,259	2,015	1,425
Application approved (percent)	1,568 (52.7%)	1,368 (30.3%)	1,314 (32.4%)	898 (27.6%)	694 (34.4%)	535 (37.5%)
Applications withdrawn (percent)	1,276 (42.9%)	2,409 (53.4%)	2,098 (51.8%)	1,965 (60.3%)	1,144 (56.8%)	468 (32.8%)
Applications denied (percent)	133 (4.5%)	734 (16.3%)	639 (15.8%)	396 (12.2%)	177 (8.8%)	422 (29.6%)

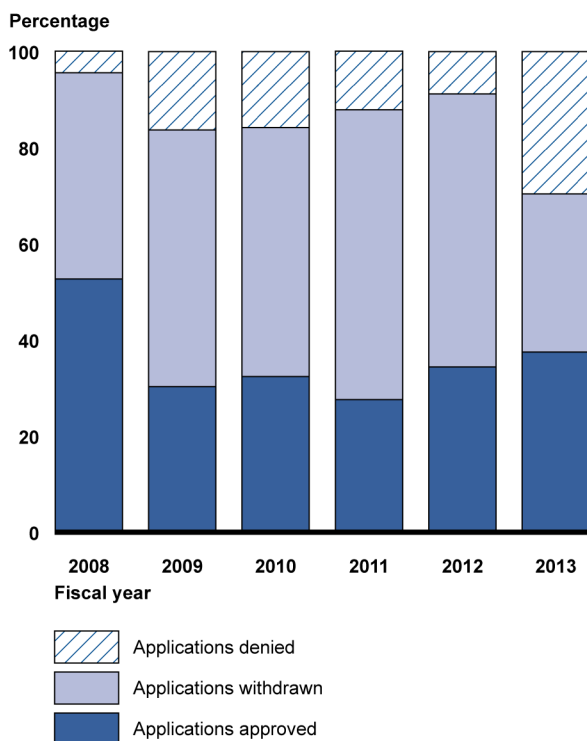
Source: GAO analysis of Small Business Administration data. | GAO-15-234

<sup>1</sup>With the release of 2010 Census data in October 2011, a large number of previously redesignated HUBZone areas lost their designation. Consequently, there were fewer qualified areas from which firms could apply and their employees could reside and be eligible for the program.

<sup>2</sup>Withdrawing an application allows firms to modify their application in order to be eligible without waiting to reapply. Denied applicants or those that were decertified may reapply for certification 90 calendar days after the date of denial or decertification if they believe they have addressed the reasons for the denial or decertification and meet the eligibility requirements.

<sup>3</sup>SBA officials explained that SBA cannot unilaterally withdraw an application but “closes” an application if a situation arises whereby the issue cannot be resolved in a short time. After a firm submits its electronic verification and can no longer make changes to its application, the firm can request that SBA withdraw the application on its behalf.

**Figure 11: Status of Applications for HUBZone Program Submitted in Fiscal Years 2008-2013, by Percentage**



Source: GAO analysis of Small Business Administration data. | GAO-15-234

According to SBA officials, SBA's goal is to process an application within 90 days. Our analysis of SBA data found that it took SBA more than 90 days to process most of the applications approved since fiscal year 2008. As shown in table 8, of the applications SBA received in fiscal years 2008-2013, about 27 percent were processed in 90 or fewer days while 73 percent took more than 90 days to process.<sup>4</sup> SBA reported that in

<sup>4</sup>According to representatives from the HUBZone trade association, the number of firms participating in the program has been shrinking and the length of the certification process hampers SBA's ability to rebuild its HUBZone portfolio. Additionally, they told us that SBA no longer has sufficient staff to interact with interested parties that would like to obtain basic information about the program in advance of submitting an application, leading to many unqualified firms applying for the program and the inefficient use of staff time.

fiscal years 2013 and 2014 it took an average of 103 and 123 days, respectively, to process any application regardless of outcome.<sup>5</sup>

**Table 8: Processing Time for Applications Submitted in Fiscal Years 2008-2013**

	2008	2009 <sup>a</sup>	2010	2011	2012	2013	Total
90 or fewer days (Percent)	765 (48.8%)	19 (1.4%)	206 (15.7%)	339 (37.8%)	315 (45.4%)	56 (10.5%)	1,700 (26.7%)
More than 90 days (Percent)	803 (51.2%)	1,349 (98.6%)	1,108 (84.3%)	559 (62.3%)	379 (54.6%)	479 (89.5%)	4,677 (73.3%)

Source: GAO analysis of Small Business Administration data. | GAO-15-234

<sup>a</sup>SBA began implementing its full document review during fiscal year 2009.

According to the officials, SBA has completed a review of its certification process and plans to implement changes to improve and more accurately reflect its processing time. For example, according to SBA officials, SBA has been considering requiring that the program analyst, instead of administrative staff, request supporting documentation from the applicant firms. Furthermore, the official explained that SBA has been considering changing when it starts calculating the processing time. Currently, SBA begins to calculate the processing time when a high-ranking official from the firm electronically validates the application. However, SBA cannot begin its review until it receives supporting documents from the firm, which can take weeks. Consequently, SBA has been considering changing the start date to when it receives the supporting documents.

<sup>5</sup>The average processing time reported by SBA also includes time to process applications that were withdrawn and denied. However, our analysis pertained only to applications that were approved.

# Appendix V: Characteristics of HUBZone Certified Firms as of 2014

According to our analysis of SBA data for approved applications submitted during fiscal years 2008-2013, HUBZone firms vary in size and types of services and products provided.<sup>1</sup>

- **Number of employees.** The number of employees at HUBZone firms ranged from 1 to 496, with a median of 4 employees for all years except 2009 and 2010, in which the median was 5.
- **Industries in which firms operated.** Table 9 lists the top 10 industries based on the number and percentage of approved HUBZone firm applications.<sup>2</sup>

**Table 9: Top 10 Industries, Based on HUBZone Firm Applications Approved in Fiscal Years 2008-2013**

Industry (North American Industry Classification System code)	Number of applications	Percentage of applications
Commercial and institutional building construction	624	9.8
Highway, street, and bridge construction	275	4.3
Engineering services	250	3.9
Site preparation contractors	240	3.8
Other heavy and civil engineering construction	197	3.1
Administrative management and general management consulting services	193	3.0
Electrical contractors and other wiring installation contractors	178	2.8
Support activities for forestry	154	2.4
Water and sewer line and related structures construction	128	2.0
Machine shops	124	1.9

Source: GAO analysis of Small Business Administration data. | GAO-15-234

Note: Analysis based on the number of applications approved by SBA from fiscal year 2008 through fiscal year 2013, as recorded in HCTS. According to SBA officials, the industry code is only recorded for approved applications.

<sup>1</sup>We analyzed data from SBA's HCTS as of July 2014. HCTS contains information on firms that have applied to participate in the HUBZone program.

<sup>2</sup>We analyzed data based on the firm's North American Industry Classification System codes (a classification system and data analysis tool developed by the federal government that groups businesses based on similarities in the processes they use to produce goods or services).

# Appendix VI: Comments from the Small Business Administration



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

January 13, 2015

William B. Shear  
Director  
Financial Markets and Community Investment  
U.S. Government Accounting Office  
Washington, DC 20548

Dear Mr. Shear:

Thank you for providing the U.S. Small Business Administration (SBA) with a copy of the Government Accountability Office (GAO) report titled "Opportunities Exist to Further Improve HUBZone Oversight." In this report, GAO recommends that SBA should (1) establish a mechanism to better ensure firms are notified of changes that could affect their participation in the program, and (2) assess the recertification process and implement additional controls, such as criteria and guidance for a risk-based approach to requesting and verifying information during recertification.

SBA agrees with the recommendations provided in the GAO report. Specifically:

- GAO recommends that SBA establish a mechanism to better ensure that firms are notified of changes to HUBZone designations that may affect their participation in the program, such as ensuring that all certified firms and newly certified firms are signed up for the broadcast e-mail system or including more specific information in certification letters about how location in a redesignated area can affect their participation in the program.

SBA is analyzing existing resources and by July 2015, SBA will implement an enhanced mechanism to better inform all certified firms and newly certified firms of HUBZone designation changes or, at least, explain how a redesignated area can affect their participation in the program.

- GAO recommends that SBA conduct an assessment of the current recertification process and implement additional controls to reduce the risk that firms that no longer meet program eligibility criteria receive HUBZone contracts, such as developing criteria and guidance on using a risk-based approach to requesting and verifying firm information during the recertification process, allowing firms to initiate the recertification process, and ensuring that there is sufficient staff dedicated to the effort so that a significant backlog in recertifications does not recur.

SBA will conduct an assessment of the current recertification process. By September 30, 2015, it will identify areas of improvement in order to further reduce the risk of fraud waste and abuse. SBA continues to exercise its regulatory authority to investigate firms when it cannot verify a qualified HUBZone SBC's eligibility or determines that the concern is no longer eligible for the Program (13 CFR 126.503).

Thank you for the opportunity to comment on this report.

Sincerely,

A handwritten signature in black ink, appearing to read "John A. Shoraka".

John A. Shoraka  
Associate Administrator  
Office of Government Contracting and Business Development

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# Appendix VII: GAO Contact and Staff Acknowledgments

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## GAO Contact

William B. Shear, (202) 512-8678 or [shearw@gao.gov](mailto:shearw@gao.gov)

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## Staff Acknowledgments

In addition to the contact above, Harry Medina (Assistant Director), Daniel Newman (Analyst-in-Charge), Pamela Davidson, Cynthia Grant, Julia Kennon, Yola Lewis, John McGrail, John Mingus, Marc Molino, Caroline Neidhold, Gloria Proa and Barbara Roesmann made key contributions to this report.

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