

Congress of the United States
U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-0515

Memorandum

To: Members, Committee on Small Business
From: Committee Staff
Date: April 24, 2017
Re: Hearing: “Storm Watch: Making Sure SBA’s Disaster Loan Program is Prepared”

On Wednesday, April 26, 2017 at 11:00 a.m., the Committee on Small Business will meet in Room 2360 of the Rayburn House Office Building for the purpose of examining the U.S. Small Business Administration’s (SBA’s) Disaster Loan Program. The program offers loans to individuals and businesses of all sizes to help recover from declared disasters. The Committee will review the program to ensure that it is prepared for the next major disaster.

I. Introduction

While the Federal Emergency Management Agency (FEMA) provides immediate disaster assistance, SBA spearheads long term recovery through its Disaster Loan Program. This program provides *direct* loans to help businesses of all sizes, nonprofit organizations, homeowners, and renters to help repair and/or replace property damaged or destroyed in a federally declared or certified disaster. Because SBA’s disaster loans are the primary form of federal assistance for non-farm, private sector disaster loss, this program is the only form of SBA assistance not limited to small businesses.¹ The Disaster Loan Program—administered by the Office of Disaster Assistance—has been a part of SBA since the agency’s inception in 1953.²

SBA’s disaster loan portfolio includes: (1) Home and Personal Property Disaster Loans; (2) Business Physical Disaster Loans; and (3) Economic Injury Disaster Loans.³ These loans are mostly low-interest loans offered at a fixed rate for up to 30 years maturity. Approximately 80 percent of SBA’s disaster loans are awarded to individuals and households rather than small businesses.

¹ *About Office of Disaster Assistance*, U.S. SMALL BUS. ADMIN., <https://www.sba.gov/offices/headquarters/oda/about-us> (last visited April 11, 2017).

² *Id.*

³ *Types of Disaster Loans*, U.S. SMALL BUS. ADMIN., <https://www.sba.gov/loans-grants/see-what-sba-offers/sba-loan-programs/disaster-loans/types-disaster-loans> (last visited April 11, 2017).

II. SBA's Response to Past Disasters

The two natural disasters that most tested SBA's ability to effectively and efficiently respond were Hurricane Katrina in 2005⁴ and Hurricane Sandy in 2012.⁵ SBA struggled responding to both disasters. But in their wakes, SBA has improved its capacity to process and close disaster loan applications in a timely manner.

A. Hurricane Katrina

Hurricane Katrina exceeded SBA's capacity to handle disaster loan applications, resulting in an average processing time of 66 days for disaster business loans and 74 days for disaster home loans.⁶ In response, Congress passed a host of reform measures designed to improve disaster planning, public outreach, and capacity so that SBA is better able to respond to future disasters.

Specifically, Congress passed the Small Business Disaster Response and Loan Improvements Act of 2008.⁷ This Act contained 26 provisions requiring action by SBA.⁸ The Government Accountability Office (GAO) closely tracked SBA's progress implementing these provisions.⁹ In May 2010, GAO testified that SBA met 15 of the 26 requirements, and five provisions did not require any action at that time.¹⁰ Then in July 2015, GAO testified that SBA still had not implemented three provisions, specifically those requiring SBA to establish the Private Disaster Assistance Program, the Immediate Disaster Assistance Program, and the Expedited Disaster Assistance Business Loan Program.¹¹ These programs were intended to deploy more loan options more quickly to homeowners and small businesses.¹² At this time, it appears that SBA still has not fully implemented these programs.

⁴ For a more comprehensive discussion of SBA's response to Hurricane Katrina, please see the Committee's hearing memorandum on *Disaster Assistance: Is SBA Meeting the Recovery Needs of Disaster Victims? Hearing Before the H. Comm. on Small Business*, 112th Cong. (Nov. 30, 2011), available at http://smallbusiness.house.gov/uploadedfiles/11-30_hearing_memo.pdf.

⁵ For a more comprehensive discussion of SBA's response to Hurricane Sandy, please see the Committee's hearing memorandum on *The Calm Before the Storm: Oversight of SBA's Disaster Loan Program: Hearing Before the H. Comm. on Small Business*, 114th Cong. (July 8, 2015), available at http://smallbusiness.house.gov/uploadedfiles/7-8-2015_revised_memo.pdf.

⁶ *A Year Later: Lessons Learned and Progress Made After Hurricane Ike: Hearing Before the Sen. Comm. on Small Bus. and Entrepreneurship*, 111th Cong. (Sept. 25, 2009) (Testimony of Manuel Gonzalez, District Director, Houston District Office).

⁷ The Act was incorporated into part of Title XII of the Farm, Conservation and Energy Act, Pub. L. No. 110-246, 122 Stat. 1651. Specifically, the Small Business Disaster Response and Loan Improvements Act of 2008 (SBDRLIA) can be found in §§ 12051-12086, 122 Stat. at 2168-2185.

⁸ *Id.*

⁹ GOV'T ACCOUNTABILITY OFF., SMALL BUSINESS ADMINISTRATION CONTINUED ATTENTION NEEDED TO ADDRESS REFORMS TO THE DISASTER LOAN PROGRAM (May 19, 2010) (GAO-10-735T), available at <http://www.gao.gov/assets/130/124688.pdf>.

¹⁰ *Oversight of SBA Disaster Assistance Program: Hearing Before the Sen. Comm. on Small Bus. and Entrepreneurship*, 111th Cong. (May 19, 2010) (statement of William Shear, Director Financial Markets and Community Investment, Gov't Accountability Off.).

¹¹ *The Calm Before the Storm: Oversight of SBA's Disaster Loan Program: Hearing Before the H. Comm. on Small Business*, 114th Cong. (July 8, 2015).

¹² Pub. L. No. 110-246, 112 Stat. at 2180-2184.

B. Hurricane Sandy

Although improved from its response to Hurricane Katrina, SBA again struggled to quickly and effectively respond to Hurricane “Superstorm” Sandy. Similar to Hurricane Katrina, the overall response to the October 2012 hurricane prompted reviews, audits, and congressional action. For example, GAO examined SBA’s response on behalf of small businesses.¹³ In part, GAO found that SBA did not make its goal to process loan applications within 21 days, because SBA’s projections did not accurately anticipate the volume of early applications.¹⁴ GAO also noted SBA’s failure to implement the loan programs required in the Small Business Disaster Response and Loan Improvements Act of 2008.¹⁵

The SBA Office of Inspector General (OIG) issued several audit reports and has ongoing investigations work.¹⁶ Most recently, the OIG released an audit examining early-defaulted SBA disaster loans.¹⁷ The OIG found the overall early default rate on these loans was relatively low compared with other disasters.¹⁸ The OIG also found, however, that the Office of Disaster Assistance often approved loans without verifying borrowers’ eligibility or approved loans to borrowers who generally lacked creditworthiness or repayment ability.¹⁹ The OIG estimated that at least 361 of the 501 early-defaulted loans—totaling \$4.3 million—were not approved in accordance with SBA and/or federal requirements.²⁰ In response, SBA management asserted that its revised standard operating procedures (SOP) released July 2015 addressed the OIG’s findings and recommendations.²¹ The OIG acknowledged that the revised SOP improved SBA’s guidance and processes. That said, the OIG still concluded that the SOP neither resolved the OIG’s findings nor sufficiently addressed the OIG’s recommendations.²²

Congress also passed legislation amending the Small Business Act to help SBA better respond to the needs of Sandy victims. For example, the *Superstorm Sandy Relief and Disaster Loan Program Improvement Act of 2015* extended deadlines for Hurricane Sandy victims to apply for disaster loans,²³ required the Administrator to clarify policies and procedures to help

¹³ U.S. GOV’T ACCOUNTABILITY OFF., SMALL BUSINESS ADMINISTRATION: ADDITIONAL STEPS NEEDED TO HELP ENSURE MORE TIMELY DISASTER ASSISTANCE (Sept. 2014) (GAO-14-760) (hereinafter GAO 2014 Sandy Report), available at <http://www.gao.gov/assets/670/666213.pdf>.

¹⁴ *Id.* at 15–22.

¹⁵ *Id.* at 39–42.

¹⁶ *See, i.e.*, U.S. SMALL BUS. ADMIN. OFF. OF INSPECTOR GEN., EFFECTIVENESS AND TIMELINESS OF HURRICANE SANDY DISASTER LOAN CLOSING AND DISBURSEMENT PROCESSES (Aug. 2014), available at <https://www.sba.gov/sites/default/files/oig/Audit%20Report%202014-16%20-%20Effectiveness%20and%20Timeliness%20of%20the%20Hurricane%20Sandy%20Disaster%20Loan%20Closing%20and%20Disbursement%20Processes.pdf>; U.S. SMALL BUS. ADMIN. OFF. OF INSPECTOR GEN., SBA’S EVALUATION OF PRINCIPAL’S REPAYMENT ABILITY FOR HURRICANE SANDY BUSINESS LOANS (Feb. 2015), available at https://www.sba.gov/sites/default/files/oig/Use_of_Principals_Income_-_Final_Report.pdf.

¹⁷ U.S. SMALL BUS. ADMIN. OFF. OF INSPECTOR GEN., EARLY-DEFAULTED HURRICANE SANDY DISASTER LOANS 1 (Aug. 15, 2016), (hereinafter SBA OIG 2016 Report), available at https://www.sba.gov/sites/default/files/oig/16-18_-_Sandy_Early_Default_Final_Report.pdf.

¹⁸ *Id.* at 4, 9, 11.

¹⁹ *Id.* at 4.

²⁰ *Id.* at Exec. Summary.

²¹ *Id.* at Appendix II.

²² *Id.* at 12.

²³ Pub. L. No. 114–88, §1101, 129 Stat. 687-688 (2015).

loan applicants better understand the process,²⁴ and required the Administrator to improve SBA's disaster plan to specifically address situations where SBA experiences an extremely high volume of loan applications.²⁵

Congress also passed the *Recovery Improvements for Small Entities (RISE) After Disaster Act of 2015*.²⁶ This law authorized SBA to provide up to two years of additional financial assistance, on a competitive basis, to Small Business Development Centers (SBDCs), Women's Business Centers (WBCs), SCORE, or similar entities, to help small businesses recover after a presidentially-declared major disaster.²⁷ The RISE After Disaster Act also increased the amount for which collateral is necessary from \$14,000 to \$25,000 for three years after the passage of this Act²⁸ and authorized SBDCs to provide assistance to small businesses outside the SBDC's state if the small business is in a declared major disaster area.²⁹

III. Ongoing Issues

Although the SBA's Disaster Loan Program has improved—especially in the wakes of Hurricane Katrina and Hurricane Sandy—SBA needs to continue improving to ensure it is truly prepared for the country's next major natural disaster. Below are some issues that need SBA's particular attention to strengthen its disaster preparedness.

A. SBA Loan Processing Times

Most fundamentally, the SBA's Disaster Loan Program is supposed to provide loans in a timely manner to disaster victims. But the program's most important deliverable has eluded SBA, especially in the aftermath of major natural disasters. As stated earlier, in the wake of Hurricane Katrina, it took SBA an average of 66 days to process disaster business loans and 74 days to process disaster home loans. After Katrina, SBA improved its loan application, simplifying it and moving it online. But in its response to Hurricane Sandy, SBA was still unable to meet its goal to process loan applications within 21 days.³⁰ Instead, on average, it took SBA 45 days to process physical business loan applications and 38 days to process economic injury loan applications.³¹ Further, if the loan applications were approved, it took SBA an additional 66 days to close physical disaster business loans and 43 days for economic injury loan applications.³² SBA needs to continue to make strides to reduce processing times to provide timely assistance to disaster victims.

²⁴ *Id.* at §§1103, 1104.

²⁵ *Id.* at §1105.

²⁶ Recovery Improvements for Small Entities After Disaster Act of 2015, Pub. L. No. 114–88, 129 Stat. at 689.

²⁷ *Id.* at §2101.

²⁸ *Id.* at §2102.

²⁹ *Id.* at § 2103.

³⁰ GAO 2014 Sandy Report, *supra* note 13, at 15.

³¹ *Id.* at 16.

³² *Id.* at 18.

B. Eligibility and Creditworthiness

Although it is paramount that SBA reduce loan processing time, it must also guard against waste, fraud, and abuse in the program to protect taxpayer dollars. For example, the SBA OIG recently reported that SBA too often approved loans without either verifying borrowers' eligibility or ensuring their creditworthiness and repayment ability.³³ The SBA OIG has and continues to investigate fraud in the Disaster Loan Program. Currently, the OIG has approximately 25 open investigations related to Hurricane Sandy loans.³⁴ Typical fraud schemes include misuse of loan proceeds, falsely claiming eligibility (i.e., claiming vacation home is a primary residence to obtain a home loan), and submitting false invoices and/or statements of expenditures.³⁵ If SBA implements the OIG's recommendations from its August 2016 report,³⁶ the instances of fraud should decrease.

C. Communication Post-Disaster

SBA must continue to improve its post-disaster communication to strike the fine balance between providing enough information so that victims can make decisions, but not so much information as to overwhelm and confuse. For disaster victims, the days and weeks following a disaster are shocking, traumatic, and painful. For example, in a recent report, GAO found that SBA had not made loan-related information and requirements easily accessible and consistent.³⁷ Further, SBA has written and electronic materials about the disaster loan process, but applicants cannot easily find or access these materials from SBA's website.³⁸ GAO recommended that SBA better integrate disaster-loan-related information on its website.³⁹ SBA also needs to improve the consistency of its information, including the loan process, required documents for loan applicants, and estimated time frames in both paper and electronic resources.⁴⁰ To better administer its disaster loan program, SBA must continue to address how to quickly deliver instructive yet succinct information to disaster victims.

IV. Conclusion

SBA's Disaster Loan Program necessarily improved following Hurricane Katrina and Hurricane Sandy. The oversight community, including Congress, GAO, and the SBA OIG, has made several recommendations and taken legislative action to help SBA improve its disaster loan program. And for its part, SBA has largely implemented these recommendations and legislative provisions. But the true test remains when the next major disaster strikes and how SBA responds to help small businesses and homeowners recover.

³³ SBA OIG 2016 Report, *supra* note 17 at Exec. Summary.

³⁴ Staff briefing with H. Comm. on Small Bus. and Small Bus. Admin., Off. of Inspector Gen. (March 28, 2017).

³⁵ *Id.*

³⁶ As noted above in Section II.B, SBA claimed that its revised standard operating procedures released July 2015 addressed the SBA OIG's recommendations in its August 2016 audit report. The SBA OIG, however, found that while the revised SOP helped, it did not fully address the OIG's recommendations.

³⁷ U.S. GOV'T ACCOUNTABILITY OFF., SMALL BUSINESS ADMINISTRATION: AGENCY HAS CONTROLS TO COMPLY WITH PAPERWORK REDUCTION ACT BUT COULD IMPROVE ACCESSIBILITY AND CONSISTENCY OF DISASTER LOAN INFORMATION 19–22 (Nov. 2016) (GAO-17-67), available at <http://www.gao.gov/assets/690/681181.pdf>

³⁸ *Id.* at 19.

³⁹ *Id.*

⁴⁰ *Id.* at 22–27.