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SMALL BUSINESS ADMINISTRATION

Progress Continues in Addressing Reforms to the Disaster Loan Program

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U.S. Government Accountability Office





Highlights of [GAO-12-253T](#), a testimony before the Committee on Small Business, House of Representatives

Why GAO Did This Study

After the Small Business Administration (SBA) was widely criticized for its performance following the 2005 Gulf Coast hurricanes, the agency took steps to reform its Disaster Loan Program. Congress also enacted the Small Business Disaster Response and Loan Improvements Act of 2008 (Act), which places new requirements on SBA to better ensure it is prepared to respond to catastrophic disasters.

This testimony discusses SBA's progress in addressing certain requirements of the Act and recommendations in a 2009 GAO report to improve the Disaster Loan Program.

In completing this statement, GAO reviewed and updated, as appropriate, the July 2009 report, *Small Business Administration: Additional Steps Should Be Taken to Address Reforms to the Disaster Loan Program and Improve the Application Process for Future Disasters* ([GAO-09-755](#)). In that report, GAO recommended that SBA should fulfill the Act's region-specific marketing and outreach requirements; complete its annual report to Congress; issue an updated Disaster Recovery Plan; develop an implementation plan for remaining requirements; and develop procedures to further improve the application process for the Disaster Loan Program. SBA generally agreed with the recommendations and stated the agency's plan to incorporate them into its ongoing efforts to implement the Act and improve the application process.

View [GAO-12-253T](#). For more information, contact William Shear at (202) 512-8678 or shearw@gao.gov.

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What GAO Found

SBA has continued to make progress in addressing provisions of the Act, although continued attention to certain provisions will be important for sustained progress. As of November 2011, SBA met requirements for 16 of 26 provisions of the Act and partially addressed 6. Four provisions do not require any action at this time. For example, SBA updated its Disaster Recovery Plan annually, most recently in June 2011, consistent with our prior recommendation. SBA also has taken steps to address the Act's requirements for region-specific marketing and outreach. The agency has begun a dialogue with the state directors of Small Business Development Centers in the Gulf Coast about disseminating disaster planning information in the five most hurricane-prone states before the hurricane season. Additionally, SBA officials told GAO they have issued some public service announcements in disaster-prone areas. SBA has issued annual reports to Congress on disaster assistance in 2009, 2010, and 2011, as required by the Act and as GAO recommended. However, to fully address statutory requirements the agency must make extensive changes to current programs or implement new programs. In particular, SBA plans to implement pilots before finalizing regulations for two programs that would involve private lenders making short-term loans to applicants awaiting assistance. As GAO reported in May 2010, SBA officials told GAO that they formed a work group to develop these pilots.

SBA has taken steps to implement three of five recommendations from GAO's 2009 report. However, in 2009 GAO recommended the agency develop an implementation plan and report to Congress on its progress in addressing all of the Act's requirements. In November 2011 GAO met with SBA officials, but they did not provide evidence indicating that the agency had begun implementing this recommendation. In 2009, GAO also recommended that SBA develop and implement a formal process to identify problems in the disaster loan application process and make improvements for future applicants. SBA agreed with the recommendation to improve the application process and according to its 2011 annual report on disaster assistance, the loan process has been streamlined and the agency continues to enhance the electronic loan application so it has greater functionality with the Disaster Credit Management System. SBA officials told GAO that results in customer satisfaction surveys relating to the application process have improved over time, but SBA has not provided information on how it would implement a formal process to address identified problem areas in the disaster loan application process. In its 2009 report, GAO interviewed individuals and reviewed results from SBA's 2008 Disaster Loan Program Customer Satisfaction Survey which provided some positive feedback about SBA's performance following disasters such as the 2008 Midwest floods and Hurricane Ike. However, interviewees and survey results indicated areas for improvement such as reducing the paperwork burden. Agency officials told GAO they listened to customer feedback, but the agency still appears not to have a formal process for identifying problems in the application process and making needed improvements.

Chairman Graves, Ranking Member Velazquez, and
Members of the Committee:

I am pleased to be here today to discuss our work on reforms made to the Small Business Administration's (SBA) Disaster Loan Program. As you know, SBA plays a critical role in assisting the victims of natural and other declared disasters. SBA provides financial assistance through its Disaster Loan Program to help homeowners, renters, businesses of all sizes, and nonprofits recover from disasters such as earthquakes, hurricanes, and terrorist attacks.

After the 2005 Gulf Coast hurricanes, SBA faced an unprecedented demand for disaster loans, while also being confronted with a significant backlog of applications; therefore, hundreds of thousands of loans were not disbursed in a timely way. Many criticized SBA for a slow and confusing response to the disasters—one that exposed many deficiencies in the agency's Disaster Loan Program and demonstrated the need for reform. As a result, Congress and SBA agreed that the program needed significant improvements. Since then, SBA has taken several steps to reform its Disaster Loan Program including creating an online loan application, increasing the capacity of its Disaster Credit Management System, and developing and updating a Disaster Recovery Plan (DRP).¹ In June 2008, Congress enacted the Small Business Disaster Response and Loan Improvements Act (Act), which places new requirements on SBA to ensure that it is prepared for future catastrophic disasters.² SBA has continued to face additional demand for disaster loans following major disasters, including Hurricane Ike and the Midwest floods in 2008, and major floods and tornadoes affecting several states in 2011.

My statement today is based on new information that updates our 2009 report and May 2010 testimony, which updated information on SBA's progress in addressing the Act's requirements and implementing our 2009

¹SBA's use of "disaster recovery plan" differs from the general use of the term to refer to an information technology-focused plan designed to restore operability of a system, application, or computer facility following an emergency.

²Pub. L. No. 110-246, Title XII, subtitle B, 122 Stat. 2168 (2008).

recommendations.³ Specifically, this statement focuses on SBA's progress in addressing certain requirements of the Act and recommendations in our 2009 report to improve the Disaster Loan Program.

For our 2009 report, we identified and analyzed the Act's requirements and related statutory deadlines; obtained information about SBA's reform efforts; reviewed documents and progress reports to determine if requirements had been addressed and deadlines met; interviewed officials and obtained information on what, if any, challenges existed that might affect SBA's ability to meet certain requirements and about next steps and resources the agency identified as needed to address any remaining requirements. We visited Iowa and Texas, and obtained information on SBA's performance after the 2008 Midwest floods and Hurricane Ike. We interviewed SBA and Small Business Development Center (SBDC) officials, state and local officials, and representatives of local Chambers of Commerce, economic development organizations, and affected small business owners about what worked well and what improvements to SBA's disaster loan processes they would suggest. Finally, we reviewed results from a survey of SBA loan applicants on their satisfaction with the Disaster Loan Program in 2008. To update information for this statement, in November 2011 we interviewed SBA officials and reviewed documents related to the disaster reform provisions and actions taken to implement our recommendations. Additional information on our scope and methodology is provided in our 2009 report.

This statement summarizes our July 2009 report and May 2010 testimony that were based on work conducted between October 2008 and July 2009 and between March and May, 2010, respectively. We updated our work in November 2011. All of these performance audits were conducted 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.

³See GAO, *Small Business Administration: Continued Attention Needed to Address Reforms to the Disaster Loan Program*, [GAO-10-735T](#) (Washington, D.C.: May 19, 2010) and *Small Business Administration: Additional Steps Should Be Taken to Address Reforms to the Disaster Loan Program and Improve the Application Process for Future Disasters*, [GAO-09-755](#) (Washington, D.C.: Jul. 29, 2009).

Background

SBA's Office of Disaster Assistance (ODA) responds to disasters and administers the Disaster Loan Program. A Presidential disaster declaration puts into motion long-term federal recovery programs, such as the Disaster Loan Program, but SBA is not a "first responder." Rather, local government emergency services assume that role with help from state and volunteer agencies. For catastrophic disasters, and if a governor requests it, the Federal Emergency Management Agency (FEMA) can mobilize federal resources. SBA typically responds to a disaster within 3 days by sending ODA field staff to the affected area to begin providing public information about SBA's services.

Once a disaster is declared, SBA can make physical disaster loans and economic injury disaster loans. Physical disaster loans are for the permanent rebuilding and replacement of uninsured or underinsured disaster-damaged property, including personal residences and businesses of any size. That is, SBA provides loans to cover repair costs that FEMA or other insurance has not already fully compensated or covered.⁴ Economic injury disaster loans provide small businesses, including agricultural cooperatives and private nonprofits, with necessary working capital until normal operations can resume.

The Act comprises 26 provisions with substantive requirements for SBA; some with specific deadlines and some needing appropriations, and includes requirements that SBA must meet for disaster planning and response, lending, and reporting.⁵ For instance, the Act includes provisions to improve SBA's coordination with FEMA, require that the agency conduct biennial

⁴SBA can lend individuals up to \$200,000 for their primary residence and \$40,000 for household goods and personal effects and can lend businesses up to an aggregated \$2 million for physical and economic injury disaster loans, before the individuals receive their insurance recovery. In these cases, the loan recipient must use the insurance recovery funds to reduce the balance of the SBA disaster loan. Even individuals or business owners who believe they have full insurance coverage are encouraged to apply for an SBA loan because their insurance recovery may turn out to be only partial, or their damage may exceed insurance policy limits.

⁵In June 2008, as part of the Food, Conservation, and Energy Act (also commonly known as the Farm Bill), Pub. L. No. 110-246, 122 Stat. 1651, Congress passed the Small Business Disaster Response and Loan Improvements Act of 2008. This law repealed and replaced a duplicative enactment of May 22, 2008. However, the Farm Bill contains a provision that generally preserved the prior act's date of enactment if it would provide an earlier effective date than that in the Farm Bill. Although the Act became law on June 18, 2008, the enactment date for purposes of determining the effective date is May 22, 2008. We calculated all statutory deadlines in our July 2009 report from May 22, 2008.

disaster simulations, create a comprehensive disaster response plan, and improve communication with the public when disaster assistance is made available. It includes requirements to improve ODA's infrastructure, appoint an official to oversee the disaster planning and responsibilities of the agency, and establish reporting requirements for various reports to Congress. The Act also creates new programs, such as the Immediate Disaster Assistance Program that would provide small-dollar loans immediately following a disaster and the Expedited Disaster Assistance Loan Program that would provide expedited disaster assistance to businesses.

SBA Continues to Improve Its Disaster Loan Program

As of November 2011, SBA has continued to make progress addressing requirements of the Act (see fig. 1). In addition, SBA provided us with evidence in November 2011 that the agency has taken steps to implement three of the five recommendations from our 2009 report. As of November 2011, SBA met requirements for 16 of 26 provisions of the Act and partially addressed 6. Four provisions do not require any action at this time. As we recommended and the Act requires, SBA has updated its DRP annually—most recently in June 2011 (section 12075). The current plan is more complete than the previous plan, providing updated information on actions SBA has taken on disaster recovery planning.⁶ As we reported in May 2010, SBA also issued regulations on coordinating with FEMA to better ensure that disaster assistance applications are submitted in a timely manner (section 12062). In addition, SBA must revise the regulations annually and report on the revisions when submitting its annual report to Congress. More recently, in January 2011, SBA issued final rules to implement the authority provided by the Act for issuing surety bond guarantees for contracts and orders related to a major disaster (section 12079).

⁶Small Business Administration, *Disaster Recovery Plan*, June 2011.

Figure 1: SBA's Status in Addressing Requirements of the 2008 Small Business Disaster Response and Loan Improvements Act, as of November 2011

Section	Description of requirement	Status (Nov. '11)	Deadline
12061	SBA permitted to make economic injury disaster loans to nonprofits.	●	
12062 ^a	SBA must ensure its disaster assistance programs are coordinated to the maximum extent practicable with FEMA programs.	●	○
12063	Better public awareness of disaster declaration, application periods, and creation of a marketing and outreach plan.	◐	○
12064	SBA must conduct a study looking at the consistency between standard operating procedures and regulations of the Disaster Loan Program.	●	○
12065	SBA increased loan amounts from \$10,000 to \$14,000 without requiring collateral.	●	
12066	SBA authorizes private contractors to process disaster loans and coordinate efforts with Internal Revenue Service to expedite loan processing.	◐	
12067	SBA must develop, implement, or maintain a centralized information system to track and follow up with disaster loan applicants.	●	
12068	SBA is authorized to increase the deferment period of loans, but the deferment may not exceed 4 years.	N/A	
12069	SBA must put in a place a secondary facility for processing disaster loans in case the primary facility is unavailable.	●	
12070	SBA can not require the borrower to pay any non-amortized amount for the first 5 years after repayment begins.	●	
12071	SBA is authorized to make economic injury disaster loans in cases of ice storms and blizzards.	●	
12072	SBA must develop and implement a major disaster response plan and conduct a disaster simulation exercise at least once every 2 years.	●	●
12073	SBA must assign an individual the disaster planning responsibilities and report to Congress.	●	●
12074	SBA should ensure that the number of full-time equivalent ODA employees is not fewer than 800 and in the disaster cadre not fewer than 1,000.	●	
12075	SBA must develop, implement, or maintain a comprehensive written disaster response plan and update the plan annually.	●	◐ ^b
12076	SBA must develop long-term plans to secure sufficient office space to accommodate an increased workforce in times of disaster.	●	
12077	SBA may not rely solely on the loan applicant's status as a major source of employment prior to the disaster to qualify for disaster loans beyond the current statutory limit.	●	
12078	Maximum disaster loan amount increased from \$1.5 to \$2 million.	●	
12079	SBA may guarantee any surety against loss on a bid, payment, performance, or ancillary bond on any work order or contract that at the time of the bond execution does not exceed \$5 million.	●	
12081	If the President declares a major disaster, SBA may declare eligibility for additional disaster assistance.	N/A	
12082	SBA permitted to make economic injury disaster loans to eligible small business concerns located anywhere in the United States (including outside the disaster area) when the SBA declares eligibility for additional disaster assistance.	N/A	
12083 ^a	SBA must establish and implement a Private Disaster Assistance Program. SBA may guarantee timely payment of principal and interest on private disaster loans issued to eligible small businesses and homeowners within an eligible disaster area.	◐	○
12084	SBA must establish an Immediate Disaster Assistance Program to provide immediate small-dollar loans through private lenders.	◐	
12085 ^a	SBA must establish an Expedited Disaster Assistance Business Loan Program.	◐	○
12086	SBA is allowed to institute a program to refinance Gulf Coast disaster loans resulting from Hurricanes Katrina, Rita, or Wilma up to an amount no greater than the original loan.	N/A	
12091 ^c	SBA must submit reports to Congress on disaster assistance.	◐	◐

● Addressed (initial or ongoing)

◐ Partially addressed

○ Missed deadline

N/A Not applicable because no action is needed to be taken by SBA at this time, due to provisions' discretionary nature.

Source: GAO analysis of the Act and SBA documents.

^aThe Act requires SBA to issue regulations for these provisions.

^bSBA provided the first updated DRP on November 15, 2009, several months past the expected update in June 2009. Since then, SBA updated the DRP on July 31, 2010, and in June 2011.

^cSection 12091(f) includes requirements for a loan approval rate report, which is to provide a "detailing of how [SBA] can improve the processing of applications under the disaster loan program." SBA officials told us that they had covered the requirement in the 2007 DRP.

SBA has taken some steps to address the marketing and outreach provision of the Act (section 12063). SBA officials told us the agency has (1) begun an ongoing dialogue with the directors of SBDCs in the Gulf Coast about disseminating disaster planning and preparation information in the five most hurricane-prone states before the hurricane season; (2) detailed an SBA employee who works with the SBDCs to the Office of Entrepreneurial Development to help the agency develop a strategic approach for its disaster role; (3) issued some public service announcements tailored to specific regions; and (4) provided disaster preparedness presentations in conjunction with regional administrators and SBDCs. In November 2011, SBA told us that while the agency had not yet developed a written marketing plan, it had plans to do so.

According to SBA officials, as of May 2010, the agency had not yet completely addressed some provisions because to do so, SBA would have to make extensive changes to current programs or implement new programs—such as the Immediate and Expedited Disaster Assistance Programs (sections 12084 and 12085). These programs, which require participation of private lenders, would be designed to provide businesses with access to short-term loans while they were waiting for long-term assistance. As we reported in 2009, SBA plans to conduct pilots of these programs before fully implementing them. For our May 2010 testimony, SBA officials told us they had established a work group jointly chaired by officials from ODA and the Office of Capital Access to address these requirements and develop the pilots. ODA officials said they drafted regulations and received subsidy and administrative cost funding in the 2010 budget to allow them to pilot test about 600 loans under the Immediate Disaster Assistance Program (section 12084). In May 2010, SBA officials had told us that their goal was to have the pilot for the Immediate Disaster Assistance Program in place by September 2010. As of November 2011, SBA has not provided evidence indicating that the agency has made progress on this initiative.

While SBA has addressed most of the multiple new reporting requirements established in the Act, such as submitting annual reports to Congress on disaster assistance for the past 3 years, the agency has not met some statutory deadlines (section 12091). For example, as required by the Act and as we recommended in our 2009 report, the agency issued its first annual report on disaster assistance in November 2009 but

the report was due in November 2008. Specifically, the Act requires that SBA report annually on the total number of SBA disaster staff, major changes to the Disaster Loan Program (such as changes to technology or staff responsibilities), a description of the number and dollar amount of disaster loans made during the year, and SBA's plans for preparing and responding to possible future disasters.⁷ Since our May 2010 testimony, SBA provided us its fiscal year 2010 and 2011 annual reports on disaster assistance that were issued in June 2011 and November 2011, respectively.

In our 2009 report, we recommended that SBA develop an implementation plan and include milestone dates for completing implementation and any major program, resource, or other challenges the agency faces as it continues to address requirements of the Act. As of November 2011, the agency did not provide evidence it had implemented this recommendation. Not having an implementation plan in place for addressing the remaining requirements can lead to a lack of transparency about the agency's Disaster Loan Program, its capacity to reform the program and make program improvements, and its ability to adequately prepare for and respond to disasters.

In 2009, we also recommended that SBA develop and implement a process to address identified problems in the application process for disaster loans. We reported in 2009 that while SBA's initial response following the 2008 Midwest floods and Hurricane Ike aligned with major components of its DRP in terms of its use of infrastructure and staff, information technology, and communications, both the individuals we interviewed and survey results indicated the loan application process could be improved. For example, individuals we interviewed and survey responses pointed to concerns about the amount of paperwork required to complete applications and the timeliness of loan disbursements. To address these concerns, the individuals we interviewed suggested eliminating the requirement that business loan applicants provide copies of federal tax records; providing partial disbursements earlier in the

⁷The Act also states the annual report must include information on some requirements under certain provisions, such as (a) the regulations on coordination with FEMA to assure that applications for disaster assistance are submitted as quickly as practicable as required under section 12062; (b) disaster simulation exercises conducted by the agency under section 12072; (c) updates to the comprehensive DRP required under section 12075; and (d) updates to SBA's plans for securing office space to accommodate an expanded workforce required under section 12076.

process; using bridge loans to help ensure disaster victims receive timely assistance; and involving SBA, SBDCs, and state and local officials in joint pre-planning and disaster preparedness efforts.

More recently, SBA reported they have been improving the application process. For example, SBA's 2011 annual report on disaster assistance states the loan process has been streamlined and that the agency continues to enhance the electronic loan application so it has greater functionality with the Disaster Credit Management System. While SBA officials told us that they listened to customer feedback and results from the customer satisfaction survey related to the application process have improved, SBA has not provided information on how it would implement a formal process to address identified problem areas in the disaster loan application process, as we recommended in 2009. By establishing such a process, SBA could better demonstrate its commitment to improving the Disaster Loan Program and the application process for future applicants.

In conclusion, SBA has taken important steps to address three of our five recommendations. These include progress made in improving marketing and outreach to various regional entities, submitting its annual reports to Congress, and updating its DRP annually.

Chairman Graves, Ranking Member Velazquez, and Members of the Committee, this concludes my prepared statement. I would be pleased to respond to any questions that you may have at this time.

GAO Contacts and Acknowledgments

For further information on this testimony, please contact William B. Shear at (202) 512-8678 or shearw@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Individuals making key contributions to this testimony include Marshall Hamlett, Assistant Director; Anna Carbino, William Chatlos, Beth Faraguna, John Forrester, John McGrail, Marc Molino, and Barbara Roesmann.

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