

**PROCESSING OF INSURANCE
RECOVERY CHECKS AT THE DISASTER
LOAN SERVICING CENTERS**

Report Number: 11-07

Date Issued: February 10, 2011

**Prepared by the
Office of Inspector General
U.S. Small Business Administration**



U.S. Small Business Administration
Office Inspector General

Memorandum

To: John A. Miller
Director, Office of Financial Program Operations

From: /s/ Original Signed
Peter L. McClintock
Deputy Inspector General

Subject: Report on the Processing of Insurance Recovery Checks at the
Disaster Loan Servicing Centers, Report No. 11-07

Date: February 10, 2011

This report summarizes our audit of the Small Business Administration's (SBA) processing of insurance recovery checks at the Disaster Loan Servicing Centers. The audit objective was to determine whether the servicing centers have adequate and effective systems for processing insurance checks and recovering duplicate benefits.

The servicing centers receive and process a variety of checks including loan payoff checks, borrower monthly payments, and insurance checks. To evaluate the insurance recovery check processing systems, we obtained a universe of 21,568 checks processed by the Birmingham servicing center and 9,990 checks processed by the El Paso servicing center for FY 2008 and FY 2009. Because the universe of checks did not identify which were for insurance recovery, we extracted a sample of 1,500 checks from the Birmingham universe and 800 checks from the El Paso universe to identify those checks that were for insurance. From these samples, we identified 133 insurance checks processed by the Birmingham servicing center and 211 checks processed by the El Paso servicing center that were specifically for insurance. We determined that 77 of the 133 insurance checks received by the Birmingham servicing center and 97 of the 211 insurance checks received by the El Paso servicing center were for the same disaster as the SBA loan and, therefore, should have been evaluated for potential duplication of benefits.

We interviewed the staff at the Birmingham and El Paso servicing centers responsible for performing duplication of benefits analysis and observed staff as they analyzed sample insurance checks for potential duplication of benefits (DOBs). To test whether the servicing centers accurately identified DOBs, we

reviewed Disaster Credit Management System (DCMS), Centralized Loan Chronology System (CLCS), and Field Cashiering System (FCS) entries related to the loan for each check in our sample. We also contacted the insurance companies to obtain a complete, up-to-date record of all insurance claim payments for each sample item. Our audit scope and methodology is further detailed in Appendix I, and our sampling methodology is provided in Appendix II.

We conducted the audit between March 2010 and October 2010 in accordance with *Government Auditing Standards* prescribed by the Comptroller General of the United States.

RESULTS IN BRIEF

The servicing centers did not have adequate, effective procedures and systems for processing insurance recovery checks. As a result, significant errors in the DOB determination were made by each of the servicing centers. Approximately 47 percent of the DOB determinations made by the Birmingham servicing center and 23 percent of the DOB determinations made by the El Paso servicing center were inaccurate. Consequently, \$625,884 was improperly returned to borrowers and another \$123,992 was improperly applied to outstanding loan balances. Also, for one of the loans in our sample, we identified an additional \$529,444¹ in duplicate benefits that was undetected by the servicing center.

Projecting our sample results to the universe of 21,568 checks processed by the Birmingham servicing center during FY 2008 and FY 2009, we estimate that at least 340 checks totaling nearly \$3.5 million in duplicate benefits were returned to borrowers in error. Likewise, based upon the universe of 9,990 checks processed by the El Paso servicing center, we estimate that at least 159 insurance checks processed during the same period resulted in \$667,362 in duplicate benefits being returned erroneously.

These errors occurred because: (1) SBA did not have adequate procedures to evaluate insurance checks for duplicate benefits; (2) some employees lacked the expertise and tools to calculate remaining loan eligibility needed for duplicate benefit determination; and (3) the centers did not adequately document information to support the DOB determination so that it would be available if a check for the same borrower was subsequently received.

We recommend that the Office of Financial Program Operations improve the system for processing insurance recovery checks by revising SOP 50 50 and 50 52 to incorporate detailed instructions for processing insurance recovery checks,

¹ This amount was not projected to the universe because it was not included in our sample.

which include effective practices that will correct the deficiencies identified in this report. We further recommend that the servicing centers assign the insurance recovery check processing to selected individuals and fully document the justification for the decision to return or retain each check. We also recommend that the Agency recover duplicate benefits identified in this audit. In response to the draft report, Agency management generally concurred with our recommendations. (See Appendix V).

BACKGROUND

The SBA provides direct disaster loans to homeowners, renters, businesses and nonprofit organizations to help them return to pre-disaster condition. Section 312 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act (42 U.S.C. 5155), amended in June 2007, requires the Federal Government to ensure that no person or entity be provided disaster assistance if he or she has received financial assistance under any other program or from insurance or any other source. The Act further provides that Federal agencies may provide disaster assistance to a person who is or may be entitled to receive benefits for the same purpose from another source if the person has not received these benefits by the time of application for Federal assistance and if the recipient agrees to repay all duplicative assistance to the agency providing the Federal assistance. Finally, the Act specifies that persons who receive Federal assistance for a major disaster or emergency shall be liable to the United States to the extent that the assistance duplicates benefits awarded to the person for the same purpose. According to 44 CFR 206.919(b)(1), Federal agencies shall establish appropriate agency policies and procedures to prevent duplication of benefits.

To comply with the Act, Standard Operating Procedure (SOP) 50 30 requires ODA to determine the borrower's uncompensated loss, which is the difference between the total loss determined by SBA and any deductions (insurance or other recoveries) for duplication of benefits. All insurance payments for the same purpose as the disaster loan are considered a duplicate benefit.

An Assignment of Insurance Proceeds (AIP), executed by the borrower prior to final loan disbursement, instructs the insurance company to send applicable insurance proceeds to SBA. The servicing centers routinely receive all assigned insurance checks and are responsible for evaluating whether the checks might be a duplication of benefits.

The *Disaster Loan Servicing* SOP 50 52 provides basic criteria for when it is permissible to release insurance proceeds to borrowers that have disaster home loans. The SOP specifies that an insurance check may be endorsed and released to

the borrower if the loan is current and the check is not a duplication of benefits. However, the SOP is silent regarding how to identify duplication of benefits when an insurance check is received, what to do once a duplication has been identified, what information should be retained to support the accuracy of the determination, and what action should be taken to ensure that DOBs identified are successfully collected. Additionally, SOP 50 50, which provides criteria for servicing business loans, does not provide any guidance for processing insurance checks for potential duplication of benefits.

The first step necessary to evaluate an insurance check for potential DOBs is to compute remaining borrower eligibility; however, SOP 50 52 does not specify how to perform the computation. There are a number of components to the eligibility computation, including verified loss, total project cost, FEMA grant awards, initial insurance recoveries, and other grant awards. Additionally, OMB Circular A-123, *Management Accountability and Control*, requires that agencies' management have well-defined documentation processes for internal controls that contain an audit trail, verifiable results, and specify document retention periods.

RESULTS

Disaster Loan Servicing Centers Did Not Accurately Process Insurance Recovery Checks

The Disaster Loan Servicing Centers made inaccurate DOB determinations and inappropriately returned or retained some insurance checks. Specifically, 36 of 77, or 47 percent, of the checks from our sample that were processed by the Birmingham servicing center had an inaccurate DOB determination. Of the 36 inaccurate determinations made by the Birmingham servicing center, 32 checks totaling \$477,102 were returned to borrowers in error, and 4 checks totaling \$108,956 were erroneously applied to outstanding loan balances. Additionally, 22 of 97, or 23 percent, of the checks from our sample that were processed by the El Paso servicing center also had an inaccurate DOB determination. The El Paso servicing center improperly returned 19 checks totaling \$148,778 and improperly applied 3 checks totaling \$15,036. Projecting these sample results to the universe of 21,568 checks processed by Birmingham servicing center during FY 2008 and FY 2009, at least \$3,498,799 in duplicate benefits were returned to borrowers in error. Similarly, we projected that at least \$667,362 in duplicate benefits was returned in error by the El Paso servicing center from a universe of 9,990 checks. We also identified an additional \$529,444 in insurance checks that resulted in duplicate benefits that were undetected by the Birmingham servicing center, which were outside of the sampled universe.

The incorrect DOB determinations and disposition of insurance recovery checks occurred because: (1) SBA did not have adequate procedures to evaluate insurance checks for duplicate benefits, (2) some employees lacked the expertise and tools to calculate remaining loan eligibility needed for the duplicate benefit determination; and (3) the centers did not adequately document information to support the DOB determination so that it would be available if a check for the same borrower was subsequently received .

Inadequate Procedures Contributed to Processing Deficiencies

Practices at both servicing centers led to inaccurate DOB determinations. For example, when an insurance check was received, the servicing centers did not routinely contact the insurance company that issued the check to obtain a list of all payments previously made to the borrower. All previous insurance payments must be included in order to accurately determine whether a duplication of benefits has occurred. Unless the servicing center has a record of all insurance payments, the DOB evaluation cannot be performed accurately. In one case, the El Paso servicing center was unaware of \$52,061 in prior insurance payments and as a result, returned a \$50,000 check to the borrower that should have been applied to the loan balance. Had it contacted the insurance company, the \$50,000 DOB would have been identified.

Additionally, the Birmingham servicing center did not evaluate insurance checks listing a senior lien holder as a co-payee for potential DOB. SBA is often not the primary lien holder of the damaged property; therefore, many insurance checks it receives are also co-payable to the first, or senior, lien holder. The servicing center generally assumed that senior-lien-holders would always exercise the right to keep the insurance funds, without verifying that the senior lien-holder required the funds. As a result of not evaluating checks with a senior lien holder listed as a co-payee, the Birmingham servicing center did not identify or collect \$59,423 dollars in duplicate benefits arising from 10 checks.

The Birmingham servicing center also returned insurance checks resulting from re-evaluation settlements to borrowers without analyzing them for duplication of benefits. Re-evaluation settlement checks are insurance payments resulting from borrowers appealing the initial insurance settlement amount received for their damaged property. The servicing center personnel mistakenly believed that all such checks were for debris removal and other property clean up. We determined that this assumption was erroneous, and had they contacted the insurance company, the servicing center personnel would have identified the purpose of the re-evaluation settlement check. Since the settlement checks in question were for real estate and personal property, not debris removal, the checks should have been evaluated for potential DOBs and applied to the loan balance. A total of \$44,292 in insurance recoveries that created duplicate benefits were returned to borrowers

as a result of the faulty assumption that the eight checks were for debris removal and property clean up.

Also, a practice at both servicing centers was to return insurance checks, issued for increased cost of compliance (ICC), to borrowers without evaluating the checks for duplication of benefits. ICC checks are generally for hazard mitigation or increasing property elevation to bring the property into compliance with local codes. The servicing centers presumed that the disaster loans did not include funds for mitigation or elevation, and thus the checks could not be a duplication of benefits. However, mitigation and elevation are an allowable use of proceeds for disaster loans. Although we did not identify any insurance checks for ICC that created duplicate benefits, there is a risk that this could occur.

The purpose of an SBA disaster loan is to repair or replace a disaster victim's real property, or his or her personal property, which was damaged or destroyed as a result of a natural disaster. Another deficient practice of the servicing centers was to only evaluate, for potential DOBs, checks with the same purpose as the loan. For example, one check for \$16,342 was for personal property, whereas the SBA loan was for real estate only. The servicing center did not evaluate the loan for potential DOBs and returned the check to the borrower. However, there was an existing unidentified duplicate benefit for real estate due to a previous failure of internal controls. Therefore, the entire \$16,342 should have been applied to the loan balance since SBA had previously duplicated benefits the borrower had received from insurance and, therefore, had loaned the borrower more than he was eligible to receive. When SBA inadvertently loans a borrower an amount exceeding loan eligibility, the loan balance is referred to as "over-disbursed." We found eight instances in which the loans were already over-disbursed when the insurance checks were received by the servicing centers, but the checks were returned to the borrowers without a DOB evaluation.

One of the reasons the deficiencies in the process for evaluating insurance recovery checks occurred is because the Agency did not have adequate, effective written policies and procedures for the servicing centers to address duplicate benefits from insurance checks. Although SOP 50 52 states that an insurance recovery check must not be returned to the borrower if it is a duplication of benefits, the SOP does not explain: (1) which checks to evaluate; (2) how to evaluate an insurance recovery check for potential DOB; (3) what information to use in performing the loan eligibility computation; and (4) where to find the information needed to perform the calculation. This lack of adequate written guidance contributed to the inaccurate DOB evaluations and inconsistencies in the DOB evaluation practices at the servicing centers.

To effectively resolve these deficiencies, SBA should revise SOP 50 50 and SOP 50 52 to establish policies and procedures that address deficiencies identified in this audit.

Some Employees Lacked Expertise and the Tools Necessary to Calculate Remaining Loan Eligibility

A disaster victim does not always borrow the total amount which he or she is eligible to borrow from SBA. When a disaster victim accepts a loan for less than he or she is eligible to receive from SBA, that borrower will have remaining loan eligibility. The remaining borrower eligibility, not the amount borrowed, dictates whether or not an insurance check creates a duplicate benefit. Provided that a borrower has remaining SBA loan eligibility, an insurance check will not create a duplication of benefits.

When a loan is transferred to servicing, there is no data element in DCMS of the borrower's remaining eligibility, or audit trail for easily identifying which figures the Processing and Disbursement Center (PDC) used to compute eligibility. The servicing centers rely upon eligibility information generated by the PDC during loan origination; therefore, the PDC shares the responsibility for accurate insurance check processing. DCMS stores the components of eligibility in various places, but the information is not consolidated and doesn't identify which figures were used to determine eligibility. Lacking this information, the servicing centers must re-compute borrower eligibility from the point the loan was originated to evaluate each check for DOBs. Given the complexity of the calculation, there is a risk that the resulting computation could be inaccurate. Also, the practice of computing borrower eligibility each time an insurance check is received is inefficient.

OFA will need to coordinate with ODA to develop a process for conveying remaining borrower eligibility when the loan is transferred to servicing.

Additionally, to compute eligibility when a loan involves relocation, verified loss information in the Home Financial Analysis Tool (HFAT), a component of DCMS, must be used to obtain the correct loss amount. The servicing centers were not aware of this fact and also lacked access to HFAT; therefore, they were not always able to make the correct DOB determination. For example, one check in the amount of \$89,930 involving borrower relocation was returned in error, because the servicing center used the verified loss from the DCMS property screen, instead of the correct verified loss amount found in HFAT.

The servicing center personnel are not proficient in locating the components of eligibility and performing the calculations. The El Paso servicing center made 13 inaccurate determinations, totaling \$59,609 to retain or return insurance checks because they were unable to correctly calculate borrower eligibility. The servicing

center did not have sufficient expertise to consistently locate all of the components of eligibility in DCMS and perform the eligibility calculation correctly, as evidenced by the 13 inaccurate determinations, including 11 checks that were returned to borrowers in error, and two checks that were retained in error due to mistakes made in the eligibility calculation. We were unable to evaluate the accuracy of the eligibility determinations made by the Birmingham servicing center because there was no evidence that calculations were performed.

In order to correctly evaluate insurance checks for DOBs, the servicing centers should establish and train a dedicated team of employees to specialize in processing insurance checks for DOBs. In our discussions with the agency, they agreed with this recommendation and have taken steps to implement it.

All Information Supporting the DOB Determination for Each Check Was Not Recorded

The two servicing centers did not routinely retain information needed to evaluate an insurance check for DOBs, such as: (1) the amount of the check; (2) the date of loss associated with the check; (3) whether the check was compensation for real estate or personal property; (4) the computation used to determine whether the check was a duplication of benefits; and (5) the remaining borrower eligibility. Lacking this information, when the servicing centers received a subsequent insurance check, they had to extract all of the components of eligibility from DCMS and perform the computation again. This occurred because the servicing centers did not have a centralized location for recording and storing information specific to each loan. Since the servicing centers did not retain pertinent details about prior insurance checks, there is a high risk that an error could occur in the calculation.

To prevent errors in the DOB determination, the servicing centers should document all of the information related to the check disposition decision.

RECOMMENDATIONS

We recommend that the Director of the Office of Financial Program Operations:

1. Recover \$625,880 of DOBs identified in this audit that were improperly returned to borrowers and \$529,444 of DOBs identified in this audit that were outside of the scope of the sample.
2. Identify and recover other DOBs improperly returned during FY 2008, FY 2009, and FY 2010.

3. Revise SOP 50 50 and SOP 50 52 to incorporate detailed instructions for processing insurance recovery checks that explain which checks to evaluate for DOB, how to evaluate them, what information to use in performing the loan eligibility computation, and where to find the information needed to perform the computation.
4. Assign the processing of insurance recovery checks to selected individual(s) at each center and provide them training to allow them to become proficient in calculating duplication of benefits.
5. Ensure the servicing centers document all of the information related to the decision to return or retain each check for future reference.

AGENCY COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE

On December 23, 2010, we provided the Office of Financial Program Operations (OFPO) with the draft report for comment. On January 31, 2011, OFPO submitted its formal response which is contained in Appendix V. Management agreed with our findings and concurred with our recommendations. Management has already initiated action to address Recommendations 4 and 5. A summary of management's comments and our response is as follows.

Recommendation 1

Management Comments

OFPO concurs with this recommendation. However, OFPO believes it is highly unlikely that the funds identified by the OIG will be returned. In all likelihood, OFPO will have to refuse further discretionary loan servicing assistance until the borrowers repay the improperly returned funds in a lump sum or through agreed upon monthly installments. OFPO and the Disaster Centers will make every effort to recover as much of the improperly returned DOBs by 12-31-2011 as follows:

- OFPO will review the loans identified in the audit to re-verify OIGs findings. If there is a discrepancy, OFPO will discuss the issue with the OIG prior to taking any action to collect.
- OFPO will develop a standardized dunning letter and workflow document to guide the loan specialists in retrieving duplication of benefits that were improperly returned.
- The letters will be mailed to all borrowers no later than April 30, 2011. The letter will include a statement that if the money is not returned to the

SBA, future discretionary SBA loan servicing assistance will not be granted as stated above. Additionally, OFPO will gather monthly data from both centers of the contacted borrowers, including responses from the borrower and the total amount recovered beginning May 1, 2011.

OIG Response

Management's comments are responsive to the recommendation.

Recommendation 2

Management Comments

OFPO concurs with this recommendation. Due to the volume of work this project would entail, it would be most beneficial to do a cost benefit analysis in July, 2011, determined by the results of trying to collect the funds as noted above in recommendation 1. If it is determined that the borrowers did not respond to the attempt to collect the DOB under Recommendation 1, OFPO reserves the opportunity to review this recommendation with the OIG. It is important to note that there is no loss to the SBA if the borrower continues to make payments until the loan is paid in full.

OIG Response

Management's comments are responsive to the recommendation.

Recommendation 3

Management Comments

OFPO concurs with this recommendation as indicated in the opening narrative. OFPO expects to place edits of the SOP 50 52 into clearance by July 2011 and will develop language to be included in the next revision of SOP 50 50 (during its annual update which is issued each September).

OIG Response

Management's comments are responsive to the recommendation. OIG requests an opportunity to review the anticipated edits to the SOPs in July 2011 and comment upon their effectiveness in addressing the concerns noted in this report.

Recommendation 4*Management Comments*

OFPO concurs with this recommendation and has addressed and or plans to address these concerns as reflected in the opening narrative.

OIG Response

Management's comments are responsive to the recommendation.

Recommendation 5*Management Comments*

OFPO concurs with this recommendation and has already taken action to capture determinations as evidenced in the opening narrative. Additionally, OFPO will work with the Denver Finance Center (DFC) to improve the process for identifying insurance checks in the field cashiering system. OFPO will recommend changes to the field cashiering system which would identify insurance checks that are received by the disaster loan servicing centers and reflect the disposition of check (i.e. returned to borrower/senior lender for endorsement, applied against loan, not related to the disaster etc.). These discussions will start no later than April 15, 2011.

OIG Response

Management's comments are responsive to the recommendation.

ACTIONS REQUIRED

Please provide your management decision for each recommendation on the attached SBA Forms 1824, Recommendation Action Sheet, within 30 days from the date of this report. Your decision should identify the specific action(s) taken or planned for each recommendation and the target date(s) for completion.

We appreciate the courtesies and cooperation of the Office of Disaster Assistance during the audit. If you have any questions regarding this report, please contact me at (202) 205-[ex. 2] or Craig Hickok, Director, Disaster Assistance Group, at (817) 684-[ex. 2]

The audit objective was to determine whether the servicing centers have adequate and effective systems for processing insurance recovery checks and recovering duplicate benefits.

To satisfy this objective, we interviewed managers at the El Paso and Birmingham servicing centers to obtain an understanding of the procedures that the centers were following. We provided examples of insurance checks to personnel at each servicing center and observed as the staff processed these example checks.

We obtained a Field Cashiering Report of all checks received by the Birmingham and El Paso servicing centers during FY 2008 and FY 2009 and tested a sample of those checks to identify whether or not the checks were insurance checks. After obtaining the universe of checks, we extracted a sample of 1,500 checks from the Birmingham universe and 800 checks from the El Paso universe to identify those checks that were for insurance. Based upon the percentage of checks received by each servicing center determined to be insurance checks, we obtained a statistical sample of 147 probable insurance checks from Birmingham and 216 probable insurance checks from El Paso servicing center for review. We reviewed the documentation provided by the Birmingham servicing center for the 147 probable insurance checks and concluded that 133 of these checks were actually for insurance and were processed by the Birmingham servicing center. We concluded that 211 of the 216 El Paso servicing center probable insurance checks were for insurance and were processed by the El Paso servicing center.

We then compared the disaster date associated with each insurance check to the SBA loan disaster date. Since the servicing centers often did not have documentation providing the disaster date associated with each check, we contacted the insurance companies which provided the checks to obtain the date of loss associated with the check. From the 133 Birmingham servicing center checks, we identified a statistical sample of 77 insurance checks with the same disaster date as the SBA loan that were evaluated by the Birmingham servicing center for potential DOBs. From the 211 El Paso servicing center checks, we identified 97 checks evaluated for DOBs during FY 2008 and FY 2009 with the same disaster date as the SBA loan. We performed an independent DOB evaluation for each check in the sample and compared our DOB determinations with those made by the servicing center.

The audit was conducted between March 2010 and October 2010 in accordance with *Government Auditing Standards* as prescribed by the Comptroller General of the United States, and included such tests considered necessary to provide reasonable assurance of detecting abuse or illegal acts.

APPENDIX II. SAMPLING METHODOLOGY

We obtained a universe of 21,568 checks processed by the Birmingham servicing center during FY 2008 and FY 2009 and 9,990 checks processed by the El Paso servicing center for the same period. The Birmingham universe included not just insurance checks, but all checks received by the Birmingham servicing center during FY 2008 and FY 2009. The El Paso servicing center universe, however, was obtained by taking the list of all checks received during the period and filtering out those checks processed by the group responsible for insurance checks. After obtaining the universe of checks, we extracted a sample of 1,500 checks from the Birmingham servicing center and 800 checks from the El Paso servicing center. We reviewed the CLCS comments for each of the 1,500 Birmingham and 800 El Paso servicing center samples to identify those checks that were for insurance. From these samples, we indentified 133 checks processed by Birmingham servicing center and 211 checks processed by El Paso servicing center that were specifically for insurance.

We calculated the population point estimates and the related lower and upper limits for the selected attributes using the Windows RAT-STATS statistical software program at a 90-percent confidence level. Projecting our sample results to the universe of 21,568 checks, we estimate that at least 340 Birmingham servicing center processed checks contained duplication of benefits not identified or recovered. Projecting our sample results to the universe of 9,990 checks, we estimate that at least 159 El Paso servicing center processed checks also contained duplication of benefits not identified or recovered.

OIG Estimate of <u>Birmingham</u> DLSC Processed Checks Containing Duplicated Benefits That Were <i>Returned to Borrowers in Error</i>				
	Occurrence in Sample of 147 Checks	Population Point Estimate	90 Percent Confidence	
			Lower Limit	Upper Limit
Number of Checks	32	318	340	610
Outstanding Dollar Value	\$477,102	\$6,860,092	\$3,498,799	\$10,221,386

APPENDIX II. SAMPLING METHODOLOGY

OIG Estimate of <u>EI Paso</u> DLSC Processed Checks Containing Duplicated Benefits That Were <i>Returned</i> to Borrowers in Error				
	Occurrence in Sample of 216 Checks	Population Point Estimate	90 Percent Confidence	
			Lower Limit	Upper Limit
Number of Checks	19	184	159	341
Outstanding Dollar Value	\$147,370	\$1,840,289	\$667,362	\$3,013,215

APPENDIX III. BIRMINGHAM DLSC LOANS WITH CHECK DISPOSITION ERRORS

	Sample	Loan Number	Check Amount Returned in Error by Birmingham DLSC	Sample	Loan Number	Check Amount Retained in Error by Birmingham DLSC
1	001	8699684010	\$55,555.46	021	7921114000	\$8,508.72
2	002	2230346000	16,342.64	046	1661466009	89,930.00
3	018	3611946001	4,300.00	097	3194886005	3,141.71
4	020	1235276008	19,966.66	104	9501204006	7,375.59
5	024	9556474003	4,623.22			
6	028	1306076005	9,527.40			
7	040	1911196004	1,193.69			
8	041	1864486004	1,048.78			
9	042	9338434004	3,087.50			
10	049	8699684010	58,296.28			
11	052	1211806007	7,500.00			
12	065	9257764007	1,357.15			
13	066	9338914006	10,000.00			
14	067	9887614002	2,334.63			
15	068	1913086010	9,700.00			
16	072	9558744005	12,986.00			
17	074	1239066001	13,098.00			
18	077	3363306008	10,200.00			
19	092	1918006007	404.11			
20	093	4709304008	474.50			
21	095	9486584005	9,000.00			
22	105	9664564003	89,580.40			
23	108	9729094006	2,081.66			
24	109	9375224010	5,800.00			
25	112	9747774002	2,147.03			
26	115	1944466009	40,000.00			
27	118	2422036006	1,055.00			
28	121	9368864005	9,100.00			
29	123	9370994008	8,000.00			
30	133	1788166010	2,810.30			
31	138	2252236003	3,000.00			
32	141	8699684010	62,531.72			
		TOTALS	\$477,102.13			\$108,956.02

APPENDIX IV. EL PASO DLSC LOANS WITH CHECK DISPOSITION ERRORS

	Sample	Loan Number	Check Amount Returned in Error by El Paso DLSC	Sample	Loan Number	Check Amount Retained in Error by El Paso DLSC
1	026	1245066008	\$239.24	093	3148706007	\$6,619.82
2	033	9883414004	2,785.95	131	9879574003	7,583.00
3	041	9243424009	11,656.84	148	1313686009	833.33
4	061	3322646009	6,263.09			
5	079	9505154001	5,668.75			
6	087	1627826006	1,218.40			
7	089	3611806005	12,820.47			
8	143	1103946006	982.67			
9	144	1574076001	2,500.00			
10	153	1546916007	2,383.00			
11	162	9331294007	50,000.00			
12	168	1023986007	3,338.31			
13	183	1159166007	2,000.00			
14	187	9565974002	1,500.00			
15	194	2215246007	2175.39			
16	195	2091346010	3,324.80			
17	205	9191734005	20,495.89			
18	211	9796324003	13,429.35			
19	215	1017556000	6,000.00			
		TOTALS	\$148,782.15			\$15,036.15



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

MEMORANDUM

January 31, 2011

To: Peter L. McClintock
Deputy Inspector General

From: John A. Miller
Director, Office of Financial Program Operations

Subject: Response to Draft Report on the Processing of Insurance Recovery Checks at the Disaster Loan Servicing Centers, Project No. 10801

Thank you for the opportunity to review the draft report. We appreciate the role that the Office of Inspector General (OIG) plays in assisting management in ensuring that these programs are effectively managed. The OIG's main concerns in this audit reflected that errors occurred because (1) SBA did not have adequate procedures to evaluate insurance checks; (2) some center staff lacked the expertise or tools; and (3) the centers did not accurately document information to support determinations. The Office of Financial Program Operations (OFPO) is confident that these concerns have been or are in the process of being addressed.

Following the audit exit conference, OFPO has taken a proactive stance to address these audit concerns in collaboration with the OIG and the Office of Disaster Assistance (ODA). Immediately, OFPO engaged with ODA to facilitate a duplication of benefits training hosted at the Fort Worth Processing and Distribution Center (PDC). OFPO identified key center staff from the Birmingham Disaster Loan Servicing Center, the El Paso Disaster Loan Servicing Center, and the Santa Ana National Disaster Loan Resolution Center and provided funding to attend training at the PDC. The training focused on improving their knowledge of the Disaster Credit Management System (DCMS) and learning through the steps that the PDC takes to process duplication of benefits checks. The training introduced the center staff to the various tools used by the PDC to complete the duplication of benefits process. In addition to the greater understanding of how DCMS works, OFPO facilitated access for select center staff to the PDC's Home/Business Financial Analysis Tool and the National Emergency Management Information System which resides under FEMA.

As a further improvement to the process, OFPO is now requiring that all transactions regarding duplication of benefits must be captured in the Comments Log that resides in DCMS (this is the only component that Disaster Loan Servicing Center staff can edit

using customer service rights comment tab). By adding comments, the loan will have centralized documentation of duplication of benefits determinations. This is particularly useful if the loan moves back to the PDC for an increase in eligibility. Currently OFPO is developing a “logic tree” on duplication of benefits illustrating the typical workflow or decision making process to instruct center staff on the steps needed to arrive at a determination. The logic tree is currently being vetted through the center staff who attended the training. OFPO will update the draft and then vet the final draft with ODA and the OIG. The focus is to provide the correct tools to the subject matter experts at the centers to better standardize the process.

In conjunction with the logic tree, OFPO plans to initiate the development of standard letter and form templates for all of the centers. We are currently collecting the different templates used in the centers and will assign a focus team made up of center staff to develop one standard. OFPO has scheduled a 2 day process improvement workshop during February, 2011 to ensure that all the disaster servicing centers are processing work in the same manner (i.e. forms, letters and process). OFPO will ensure that each center will have a team of subject matter experts to process duplication of benefits. This will improve efficiency by being able to focus appropriate training and support to one team instead of to all center staff. These subject matter experts will have the expertise and knowledge to make informed determinations on any potential duplication of benefits action. Once the new procedures are in place and prove to be effective, the changes will be incorporated into the revised SOP 50 52. The OIG notes that the SOP 50 52 is silent on processing duplication of benefits; therefore, OFPO intends to incorporate the duplication of benefits procedures for inclusion in the new release of SOP 50 52 and continue the ongoing conversation with the OIG on any concerns.

One other audit concern of the OIG was that it appeared that the disaster servicing centers did not contact insurance companies to determine what other insurance checks may have been issued to the borrower without the knowledge of the SBA. To address this concern, OFPO incorporated contacting insurance companies after a check is received as a standard practice. The centers are engaged and cooperative in the process to address these audit concerns.

Moving forward, OFPO hopes to continue collaboration with the OIG and ODA. The office is working on the possibility of utilizing the PDC’s Home/Business Financial Analysis Tool to upload additional scanned items that address duplication of benefits actions from the servicing or liquidation centers. Currently, the Birmingham Disaster Loan Servicing Center hosts a website that uploads data from the El Paso Disaster Loan Servicing Center daily and migrates this information into one location by loan number. This interim solution will improve documentation concerns. OFPO intends to move forward to make sure all disaster centers under OFPO and ODA have access to necessary data.

Taking into account the above narrative, OFPO is providing additional information in response to the OIG recommendations as follows:

1. Recover \$625,880 of DOBs identified in this audit that were improperly returned to borrowers and \$529,444 of DOBs identified in this audit that were outside of the scope of the sample.

OFPO concurs with this recommendation. However, OFPO believes it is highly unlikely that the funds identified by the OIG will be returned. In all likelihood, we will have to refuse further discretionary loan servicing assistance until the borrowers repay the improperly returned funds in a lump sum or through agreed upon monthly installments. OFPO and the Disaster Centers will make every effort to recover as much of the improperly returned DOBs by 12-31-2011 as follows:

- OFPO will review the loans identified in the audit to re-verify OIGs findings. If there is a discrepancy, we will discuss the issue with the OIG prior to taking any action to collect.
- OFPO will develop a standardized dunning letter and workflow document to guide the loan specialists in retrieving duplication of benefits that were improperly returned.
- The letters will be mailed to all borrowers no later than April 30, 2011. The letter will include a statement that if the money is not returned to the SBA, future discretionary SBA loan servicing assistance will not be granted as stated above.
- Additionally, OFPO will gather monthly data from both centers of the contacted borrowers, including responses from the borrower and the total amount recovered beginning May 1, 2011.

2. Identify and recover other DOBs improperly returned during FY2008, FY2009, and FY2010.

OFPO concurs with this recommendation. Due to the volume of work this project would entail, it would be most beneficial to do a cost benefit analysis in July, 2011, determined by the results of trying to collect the funds as noted above in recommendation #1. If it is determined that the borrowers did not respond to the attempt to collect the DOB under Recommendation #1, we reserve the opportunity to review this recommendation with the OIG. It is important to note that there is no loss to the SBA if the borrower continues to make payments until the loan is paid in full.

3. Revise SOP 50 50 and SOP 50 52 to incorporate detailed instructions for processing insurance recovery checks that explain which checks to evaluate for DOBs, how to evaluate them, what information to use in performing the loan eligibility computation, and where to find the information needed to perform computation.

OFPO concurs with this recommendation as indicated in the opening narrative. OFPO

expects to place edits of the SOP 50 52 into clearance by July 2011 and will develop language to be included in the next revision of SOP 50 50 (during its annual update which is issued each September).

4. Assign the processing of insurance recovery checks to selected individual(s) at each center and provide them training to allow them to become proficient in calculating duplication of benefits.

OFPO concurs with this recommendation and has addressed and or plans to address these concerns as reflected in the opening narrative.

5. Ensure the servicing centers document all of the information related to the decision to return or retain each check for future reference.

OFPO concurs with this recommendation and has already taken action to capture determinations as evidenced in the opening narrative. Additionally, OFPO will work with the Denver Finance Center (DFC) to improve the process for identifying insurance checks in the field cashiering system. OFPO will recommend changes to the field cashiering system which would identify insurance checks that are received by the disaster loan servicing centers and reflect the disposition of check (i.e. returned to borrower/senior lender for endorsement, applied against loan, not related to the disaster etc.). These discussions will start no later than April 15, 2011.

Again, thank you for the opportunity to review the draft report. OFPO hopes to continue collaboration to address the OIG concerns and invites the OIG to revisit the centers 6 months after the implementation of the logic tree document. This step will track whether efficiency has improved and if the process for making duplication of benefits determinations should be revisited. Please let us know if you need additional information or have any questions regarding our response.