

By Electronic Mail and First-Class Mail
February 23, 2007

Senator John F. Kerry
Chairman
U.S. Senate Committee on Small Business and Entrepreneurship
304 Russell Senate Office Building
Washington, D.C. 20510

Senator Olympia J. Snowe
Ranking Member
U.S. Senate Committee on Small Business and Entrepreneurship
154 Russell Senate Office Building
Washington, D.C. 20510

Re: Gross Mismanagement at U.S. Small Business Administration
Disaster Assistance Program

Dear Senator Kerry and Senator Snowe:

We are writing to you about the whistleblower disclosures of Caroline Pankove, a former attorney at the U.S. Small Business Administration's (SBA) Disaster Assistance Processing and Disbursement Center (PDC) in Fort Worth, Texas. In October 2006, Ms. Pankove made disclosures regarding significant issues of waste, fraud, and abuse to the SBA Inspector General's Office (OIG), SBA Administrator Steven Preston, and others. The majority of the issues stem from widespread disbursement of SBA loans to Gulf Coast states hit by Hurricanes Katrina, Wilma, and Rita despite the fact that documents required by law and SBA policy are routinely missing or legally insufficient, due to pressure applied to employees by managers, group directors, and Center Counsel to reach daily disbursement quotas.

Over the past few months, the SBA OIG has launched an investigation and large scale audit into this issue, and the SBA Inspector General, Eric Thorson, has personally expressed his "respect and gratitude for Ms. Pankove's courage in coming forward with the very serious allegations that she has made about the alleged abuses in the SBA disaster loan program." As the Senate committee with oversight of the SBA, we believe that the Committee on Small Business and Entrepreneurship can play a crucial role in ensuring that the SBA appropriately addresses these and other serious problems in its Disaster Assistance Program.

This problem springs primarily from the SBA's continued practice of valuing "production" over accuracy. While the SBA's goal to disburse loans as quickly as possible is laudable, its actual processing of these loans without regard to legal requirements or customer

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needs is not. The metric used to measure success is not whether SBA employees provide accurate, timely, and courteous service to their customers, but whether loans are churned out quickly, often with legally required documentation missing. PDC routinely holds awards ceremonies, in which cash awards are distributed to employees who complete the highest number of loan disbursements or loan modifications, creating an unfortunate incentive for SBA employees to process loans as quickly as possible, without regard to legal or policy requirements. Team supervisors routinely pass on information from their meetings with group managers and directors that employment longevity of PDC employees is tied directly to disbursement numbers. Employees who have achieved high raw disbursement numbers have been retained, while employees who have process their loans correctly, with committed customer service, and in accordance with the law have been targeted for layoffs. As a result of such hasty processing of loan disbursements, millions of dollars have been disbursed to people that might not have been legally eligible for such loans.

SBA's procedures also result in numerous loan recipients receiving extremely slow service. As Ms. Pankove further disclosed in a letter to Mr. Preston on December 19, 2006, literally thousands of SBA mortgage documents containing major typing errors are sent out from PDC *directly by the typists*, without having been first reviewed by SBA disaster attorneys. As a result, thousands of borrowers in the Gulf Coast states, many of them impoverished, spend significant sums of their own money to execute documents before a notary and record these mortgages. Often they must take as much as a full day off of work to complete execution and recording of the SBA required documents, only to be later informed that the documents contained errors and will have to be re-typed by SBA and then re-recorded by the borrower, thus doubling the delay and their expense. This problem could easily be corrected with no or minimal additional resources, simply by designating one SBA disaster attorney on each team to review these documents for accuracy *before* they are sent out to the borrower. SBA has to date declined to take this step.

Another significant problem at the PDC is the lack of one single comprehensive Memorandum from Center Counsel to reiterate current law, SOP, policy, rules and guidance for the employees in the legal department. Despite several requests, PDC Counsel, Burton Warner, has consistently failed to issue a memorandum addressing many urgent issues such as collateral deficiencies, insurance deficiencies, injection, and real estate requirements. A uniform training guide, a written response to questions posed, or any other written uniform legal guidance for SBA disaster attorneys is still unavailable. As a result, attorneys receive conflicting oral guidance from their direct supervisors (team leads, managers, and group directors), often directing them to disregard portions of the SOP that could impede disbursements. Additionally, different team leaders at the PDC issue guidance to the attorneys under their supervision in ways

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that are entirely inconsistent from one another. This lack of consistent guidance dramatically reduces the efficiency of SBA's disaster attorneys, who must independently evaluate numerous policy and legal decisions from scratch, and results in borrowers facing identical situations being treated in an inconsistent manner. While Ms. Pankove requested that such guidance be given to the PDC's disaster attorneys in an October 27, 2006, email to Mr. Burton and in the December 19, 2006, letter to Mr. Preston, and despite Mr. Thorson's assurance on December 7, 2006, that he had "urged [Mr. Warner] that immediate answers [to the questions raised in Ms. Pankove's email] be provided," the SBA has never provided such guidance. Because of the ongoing failure to address these issues, employees at the PDC continue to disburse loans with inadequate documentation and based on grossly inconsistent standards applied from team to team.

Another major loan disbursement issue at the PDC is insurance injection. Current SBA policy provides that borrowers must provide evidence that they have applied their own real estate insurance proceeds to the repair of their property before receiving a loan disbursement for real estate repair funds from the SBA. From the beginning of the campaign, attorneys received oral directives to "relax" or "disregard" this requirement in order to meet SBA disbursement goals. Despite numerous requests for written guidance from PDC disaster attorneys to directors and Center Counsel, no official written revision of this policy has been issued. Therefore, disaster staff continues to operate under various inconsistent oral directives of their GS-9 and GS-11 supervisors. Specifically, PDC has applied its insurance injection policies inconsistently, with some attorneys adhering to SBA's written policies requiring proof of injection, while other attorneys have completely ignored the injection requirement. Moreover, SBA policy or training does not mandate that SBA loan officers explain the issue of insurance injection to borrowers before receipt of their loans. This results in many borrowers' inadvertent violation of SBA loan requirements that otherwise would be easily followed. This problem could be addressed through training and policy guidance that stresses one consistent rule for loan officers and attorneys about insurance injection and the potential adverse impact on the borrowers' loans. This should be communicated at the beginning of the loan application process and reinforced by case managers and attorneys.

Finally, with respect to the OIG's investigation, Ms. Pankove's disclosures regarding the manner in which SBA has disbursed relief funds in the wake of Hurricanes Katrina, Wilma, and Rita is fundamentally a legal matter, as those funds have been disbursed with intentional disregard for legal prerequisites. The OIG's analysis of SBA loan files to see whether those legal prerequisites were met thus requires a thorough understanding of the numerous legal issues particular to each of the Gulf Coast states as related to disaster relief funds disbursement. While the auditors have worked with Ms. Pankove to try to apply appropriate legal principles to OIG's review of disbursement files, it is simply not possible for a non-attorney, or even an attorney

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without training in the SBA disaster relief disbursement process, to fully understand these complex legal issues. Although the OIG seems committed to a thorough investigation of Ms. Pankove's disclosures, we question whether it will be able to adequately perform such an investigation unless the SBA commits to temporarily assigning disaster attorneys to assist the OIG. SBA has several disaster attorneys it could temporarily assign to assist the investigation, but has thus far refused to do so.

As you and the Senate Committee on Small Business and Entrepreneurship have previously recognized, the SBA Disaster Assistance Program currently faces significant issues, and we believe that resolution of the issues outlined above are among the most crucial for the future success of the program. These issues undermine not only the ability of thousands of hard-working SBA employees to perform their jobs as effectively as possible, but the ability of thousands of SBA borrowers dependent on SBA's Disaster Assistance Program, many of them living in desperate circumstances, to be effectively served by the SBA.

We urge your offices and the Senate Committee on Small Business and Entrepreneurship to look into these issues, and to complement the SBA OIG's ongoing investigation. Should you or a member of your staff desire more information about this matter, feel free to contact us. Thank you in advance for your attention to this matter.

Sincerely,


Debra S. Katz


Avi Kumin
Attorneys for Caroline Pankove

cc: Senator Mary L. Landrieu
Senator Ted Stevens
Congresswoman Nydia M. Velázquez
Congressman Steve Chabot
Mr. Steven Preston
Ms. Caroline Pankove