U.S. SMALL BUSINESS ADMINISTRATION
OFFICE OF INSPECTOR GENERAL
WASHINGTON, D.C. 20416

Final Report Transmittal
Report Number: 16-04

DATE: December 11, 2015

TO: Maria Contreras-Sweet
Administrator, Small Business Administration

Douglas Kramer
Deputy Administrator, Small Business Administration

Tami Perriello
Chief Financial Officer, Small Business Administration

FROM: Troy M. Meyer /s/
Assistant Inspector General for Auditing

SUBJECT: KPMG Management Letter Communicating Matters Relative to SBA's FY 2015 Financial Statement Audit

The attached management letter identifies matters that were identified during the audit of SBA's FY 2015 financial statements. The audit was performed by an independent public accountant, KMPG LLP, under a contract with the Office of Inspector General and in accordance with *Generally Accepted Government Auditing Standards;* Office of Management and Budget's (OMB) Bulletin No. 15-02, *Audit Requirements for Federal Financial Statements*; the U.S. Government Accountability Office (GAO)/President's Council on Integrity and Efficiency *Financial Audit Manual;* and GAO's *Federal Information System Controls Audit Manual.*

The management letter addressed recommendations to the Associate Administrator for Capital Access; Chief Human Capital Officer; and Directors for the Offices of Credit Risk Management and Performance and Systems Management. We provided a draft of KPMG's findings to each of these officials or their designees, who fully or substantially concurred with the findings relative to their respective areas. The officials or designees agreed to implement the recommendations or have already taken action to address the underlying conditions. We appreciate the cooperation that we received from your staff during our audit. Please contact me if you would like to discuss this report or any related issues.

cc: Nick Maduros, Chief of Staff
Melvin F. Williams, Jr., General Counsel
Martin Conrey, Attorney Advisor, Legislation and Appropriations
LaNae Twite, Director, Office of Internal Controls

Attachment

KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

November 16, 2015

CONFIDENTIAL

Inspector General
U. S. Small Business Administration
Washington, D.C.

Ladies and Gentlemen:

In planning and performing our audit of the consolidated financial statements of the U.S. Small Business Administration (SBA), as of and for the year ended September 30, 2015 and 2014, in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget Bulletin No. 15-02, *Audit Requirements for Federal Financial Statements*, we considered SBA's internal control over financial reporting (internal control) as a basis for designing auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of SBA's internal control. Accordingly, we do not express an opinion on the effectiveness of SBA's internal control.

During our audit we noted certain matters involving internal control and other operational matters that are presented for your consideration. These comments and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve internal control or result in other operating efficiencies and are summarized in Exhibit I. We would be pleased to discuss these comments and recommendations with you at any time.

In addition, we identified a combination of certain deficiencies in internal control that we consider to be a significant deficiency, and communicated them in writing to management and those charged with governance on November 16, 2015.

Our audit procedures are designed primarily to enable us to form an opinion on the financial statements, and therefore may not bring to light all weaknesses in policies or procedures that may exist. We aim, however, to use our knowledge of the SBA's organization gained during our work to make comments and suggestions that we hope will be useful to you.

This communication is intended solely for the information and use of management, the Office of the Inspector General, others within the organization, the Government Accountability Office, and the U.S. Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

KPMG LLP

Exhibit I

U.S. SMALL BUSINESS ADMINISTRATION

Management Letter Comments

FY 2015

Deficiencies in Lender Assessment Corrective Action Follow-up

SBA performs Risk-Based Reviews (RBR) of lenders and 504 Certified Development Companies (CDCs) that issue loans under SBA's 7(a) and 504 guaranty loan programs. Corrective action items may be issued by SBA as a result of findings identified during the lender review process. Lenders that receive RBR assessments of Acceptable with Corrective Actions, Marginally Acceptable with Corrective Actions, or Less than Acceptable with Corrective Actions are required to respond to the corrective action items within 30 days of receiving the transmittal letter from SBA.

During our control testwork over corrective action follow-up, we noted 2 deficiencies in a sample of 16 lender assessments performed by the Office of Credit Risk Management (OCRM):

- OCRM did not timely review or follow up on the corrective action responses from a lender with an RBR assessment of Less than Acceptable with Corrective Actions.

- OCRM did not maintain sufficient documentation of correspondence between SBA and the lender since the issuance of the RBR report dated 9/27/2013, where the lender received an assessment of Acceptable with Corrective Actions.

We recommend the Associate Administrator for Capital Access work with the OCRM director to:

1. Continue to develop and implement policies and procedures that ensure timely and quality follow-up on lender corrective actions, including policies for retention of lender records.

Management's Response:

SBA management concurred with the finding and recommendation.

Deficiencies in Lender Delegated Authority Renewals

SBA performs reviews of lenders whose delegated authority is set to expire within three months. SBA notifies lenders that they are conducting a review and requests specific documentation in addition to information requested from the District Offices. A financial analyst completes a risk assessment over the lender and makes a recommendation regarding whether the lender's delegated authority should be renewed and the appropriate officials perform a second sign-off on the analyst's recommendation. Based upon the results of the review, a lender may be renewed for 6 months, 1 year, or 2 years, or their authority may be revoked. A lender is notified of their results in order to continue issuing and servicing their SBA-guarantied loan portfolio.

During our control testwork over 7(a) and 504 CDC delegated authority status renewals, we noted 3 deficiencies in a sample of 45 status renewals in which the 7(a) lender's delegated authority expired before SBA's completion of the renewal process. The lapse in time between expiration date and renewal for each of these three incidents was 1, 2, and 28 days during which SBA did not grant temporary extensions.

We recommend the Associate Administrator for Capital Access work with the OCRM director to:

2. Reallocate staff to ensure timely completion of delegated authority renewals before they expire.

Management's Response:

SBA management concurred with the finding and recommendation.

Deficiencies in Disaster Loan Servicing

SBA is responsible for necessary direct loan servicing actions, including monitoring of disaster loan installment payments and reviewing delinquency reports, to ensure timely and proper referrals to Treasury and charge-offs of uncollectible balances.

During our testwork over direct loan receivables, we noted the following 2 deficiencies in a sample of 154 disaster loans:

- One loan was improperly coded as regular servicing and should have been charged off in a prior fiscal year. This resulted in the outstanding principal balance being misstated by $242,171.37.

- For another loan, SBA did not return the borrower's repayment terms from interest only to principal and interest in accordance with the Loan Authorization Agreement after the modification period ended in 2005. This did not result in a substantive error as the outstanding receivable balance was accurate based on the borrower's repayments.

We recommend that the Associate Administrator for Capital Access, in coordination with the Office of Performance and Systems Management director:

3. Remediate the 25 disaster loan control deficiencies identified.

4. Perform an analysis of all direct loans coded in the system as interest only repayments to ensure the loan terms are consistent with the underlying loan documents.

5. Implement a manual or automated control to monitor all direct loan modifications to ensure repayment terms are properly recorded and updated in the system in accordance with the underlying loan documents.

Management's Response:

SBA management concurred with the finding and recommendation.

Inadequate Review of STAR Time and Attendance Reports

SBA has controls in place to ensure timely review and approval of System for Time and Attendance Reporting (STAR) Time and Attendance (T&A) Reports as well as requests for leave or approved absence.

During our control testwork over approvals of STAR T&A Reports and related supporting documentation for amounts certified, we noted the following 4 control deficiencies in a sample of 38 reports:

- One STAR T&A Report was not signed by the timekeeper (certifier).
- Two STAR T&A Reports were not signed by the supervisor (approver).
- One STAR T&A Report was not properly dated by the employee's supervisor.

We recommend the Chief Human Capital Officer:

6. Continue to reinforce policies and procedures regarding the certification of STAR T&A Reports with supervisors and timekeepers (i.e., issuance of a memorandum, training).
7. Continue to perform periodic quality assurance reviews to ensure supervisors and timekeepers are properly certifying and dating all STAR T&A Reports.
8. Develop and implement appropriate enforcement actions against individuals and offices with multiple instances of noncompliance.

Management's Response:

SBA management concurred with the finding and recommendations.