

SBA'S USE OF VENDORS WITHOUT A CONTRACT

REPORT NUMBER 21-08 | February 3, 2021





Office of Inspector General
U.S. Small Business Administration

MEMORANDUM

DATE: February 3, 2021
TO: Tami Perriello
Acting Administrator and Chief Financial Officer
FROM: Hannibal "Mike" Ware /S/
Inspector General
SUBJECT: SBA's Use of Vendors Without Contracts

The Office of Inspector General (OIG) is issuing this Management Advisory to notify management of a significant matter we identified during our audit of Small Business Administration's (SBA's) management of foreclosed properties, project number 20810. We discovered that SBA had been using three vendors without a contract since fiscal year 2012. As of February 18, 2020, SBA had paid these vendors an estimated combined total of more than \$10.8 million in unauthorized commitments.

We considered management's comments on the draft of this report when preparing the final report. Management agreed with recommendations 1 and 2 and disagreed with recommendation 3.

We appreciate the cooperation that we received during this review. If you have any questions, please contact me or Andrea Deadwyler, Assistant Inspector General for Audits, at (202) 205-6586.

cc: Steve Kong, Acting Chief of Staff
Arthur Plews, Deputy Chief of Staff
Nina Levine, Acting General Counsel
John Miller, Deputy Associate Administrator, Office of Capital Access
Michael Simmons, Attorney Advisor, Office of General Counsel
Martin Conrey, Attorney Advisor
Rafaela Monchek, Director, Office of Continuous Operations and Risk Management
Tonia Butler, Director, Office of Internal Controls

Background

SBA's National Disaster Loan Resolution Center was established to consolidate and streamline SBA's delinquent disaster loan portfolio. The resolution center's mission is to resolve delinquent disaster loans using all available collection tools, including foreclosure on real estate collateral, and to maximize amounts of money recovered.

If a debtor is more than 60 days past due on disaster loan payments, the loan is delinquent. Once the resolution center receives the delinquent loan, SBA employees have 30 calendar days to prepare a liquidation plan. A liquidation plan is a written plan outlining the actions the agency intends to take to ensure the highest possible recovery on a loan.

SBA's Disaster Loan Servicing and Liquidation Standard Operating Procedures state any collateral associated with the loan with recoverable value should be liquidated. But foreclosure on real estate collateral is used as a last resort.

During the foreclosure process, SBA either receives proceeds when another party buys the property, or it becomes the owner of the property and must maintain the property and make limited repairs, when necessary, until the property is sold. Since 2012, SBA has begun or completed foreclosure proceedings on 3,489 properties. As of February 2020, the completed foreclosures recovered \$62,345,789 from a total delinquent loan balance of \$369,365,614.

We initiated our ongoing audit of SBA's management of foreclosed properties after discovering that SBA has owned two foreclosed properties for nearly 30 years. The two properties had been foreclosed by district offices before the resolution center was established, and the property records were never transferred.

SBA managers were not aware the agency owned the two properties. SBA managers only became aware of these properties in 2019, after a local municipality issued a fine to the agency for failing to maintain one property and a buyer offered to purchase the other.

SBA Used Vendor Services Without a Contract

During our audit work, we learned SBA used three vendors without a contract to handle foreclosures and sales of properties. These vendors were primarily responsible for identifying subcontractors for appraisals, repairs, maintenance, listings, sale of properties, and legal services.

The three vendors billed the resolution center for the foreclosure and sale services and administrative fees for commissioning the sales. Since 2012, SBA has made 34,030 payments for unauthorized commitments totaling over \$10.8 million to these vendors as follows:

1. Vendor 1—22,384 payments totaling more than \$8.1million
2. Vendor 2—9,325 payments totaling more than \$2.4 million
3. Vendor 3—2,321 payments totaling more than \$336,800

Agencies are required to use the U.S. government's System for Award Management

(SAM) as the primary source of vendor information. None of the three vendors were registered in the SAM, as required, and SBA did not purchase their services following federal procurement policy. We questioned these unauthorized payments, totaling more than \$10.8 million, because SBA did not comply with regulations (see Appendix I).

Federal Acquisition Regulation (FAR) Part 1.102 requires “promotion of competition, maximizing the use of commercial products and services, and conducting business with integrity, fairness, and openness.” FAR Part 13 Subpart 104 Promoting Competition states a contracting officer must “promote competition to the maximum extent practicable to obtain supplies and services from the source whose offer is the most advantageous to the Government.”

The regulatory provision defined in the FAR states that any agreement made by a government employee who lacked the authority to enter into such agreement with a vendor is considered an unauthorized commitment. Title 5 of the Code of Federal Regulations (CFR) Part 2635.101 Standards of Ethical Conduct for Employees of the Executive Branch states employees shall not knowingly make unauthorized commitments or promises of any kind that bind the government.

Additionally, Title 48 of the Code of Federal Regulations Part 1.602-3 Ratification of Unauthorized Commitments states ratification of an unauthorized commitment may only be performed by a contracting officer or an official with the authority to do so as designated by the head of the contracting office.

The CFR defines an unauthorized payment as any action or agreement which is not binding solely because the representative who made it lacked the proper authority to enter into this action or agreement on behalf of the government. Agencies should take positive action to preclude, to the maximum extent possible, the need for ratification actions.

SBA had not entered into a government contract and was using vendors that were not recorded in SAM. The agency paid more than \$10.8 million in unauthorized commitments that should be ratified under 48 C.F.R. § 1.602-3. Additionally, the agency did not conduct these contracting actions with integrity and openness in a fair and equitable manner, as required by the FAR.

An SBA official told us the vendors were first engaged for small services for what was perceived to be of minimal value. Use of the vendors continued over time and became part of the resolution center’s normal process. The practice of using these vendors without a contract was not intentional but rather an oversight.

The official further explained that the FAR applies to the acquisition of supplies and services with appropriated funds. The nature of the services does not require the use of federally appropriated funds. The fees associated with each service are the borrower’s financial obligation and are charged back to the borrower by way of a care and preservation of collateral fee.

It is important to note that the disaster loans are in default, and the sale of the real estate collateral is being used as a last resort to recover a portion of the delinquent debt. Any fees charged by the vendors are added to the delinquent loan balance. Any portion of the delinquent debt not recovered through foreclosure is charged off, so the

federal government ultimately pays for these services.

In addition, SBA pays the vendors as services are rendered, which is before any of the debt is recovered through foreclosure. Federal funds are expended to pay these vendors until the collateral is sold.

During our review, SBA officials acknowledged that a contract was required and said the agency has instructed SBA's acquisitions division to put a contract in place for these services.

Use of Computer-Processed Data

We relied on computer-generated data from SBA's Foreclosure and Real Estate Database and Capital Access Financial System. We conducted limited testing by comparing the data in each system. We found one property reported in the Capital Access Financial System as owned by SBA from FYs 2012 through 2019. However, the property was sold in 2003.

Capital Access Financial System is audited annually, so we do not think this one error causes the data we used to be unreliable for our testing. Consequently, we believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our objectives.

We performed this inspection in accordance with the Council on Inspectors General on Integrity and Efficiency's Quality Standards for Inspection and Evaluation. Those standards require that we plan and perform the inspection to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions and observations based on our objective. We believe the evidence obtained provides a reasonable basis for our conclusions and observations based on our objectives.

Recommendations

We recommend the Administrator to direct the Associate Administrator for the Office of Capital Access to:

1. Require responsible personnel to execute a contract for foreclosure and real estate services to ensure the procurement of services are obtained and authorized in accordance with the Federal Acquisition Regulation requirements.
2. Ensure that vendors used to provide foreclosure and real estate services are registered in SAM, as required.
3. Ratify the over \$10.8 million in payments in accordance with the FAR and 48 C.F.R. § 1.602-3.

Analysis of Agency Response

Management provided formal comments that are included in their entirety in Appendix II. They agreed with recommendations 1 and 2 and disagreed with recommendation 3. Management also provided recommendation action sheets for each recommendation that indicated the implementation date. Management's proposed actions for recommendations 1 and 2 satisfy the intent of the recommendations. However,

recommendation 3 is unresolved.

Summary of Actions Necessary to Close the Report

The following provides the status of the recommendations and necessary actions to close them.

1. **Resolved.** Management agreed with our recommendation, stating SBA's Office of Financial Program Operations (OFPO) recognized OIG's view that a contract is needed for a vendor to provide such services. SBA's OFPO has identified responsible personnel to execute contracts for foreclosure and real estate services to ensure the procurement of services are obtained and authorized in accordance with the FAR. SBA stated it initiated this corrective action in July 2020 and the final implementation date is July 19, 2021.

Management proposed actions satisfy the intent of the recommendation. This recommendation can be closed when management provides evidence that they have appointed responsible personnel to ensure the procurement services are obtained and authorized in accordance with the FAR and that contracts have been executed to obtain applicable foreclosure and real estate services.

2. **Resolved.** Management agreed with our recommendation, stating they will ensure vendors used to provide foreclosure and real estate services are registered in SAM, as required. The final implementation date is July 19, 2021.

Management proposed actions satisfy the intent of the recommendation. Management should take immediate action to ensure vendors used for these services are registered in SAM. This recommendation can be closed when management provides evidence that vendors used for foreclosure and real estate services are registered in SAM.

3. **Unresolved.** Management disagreed with our recommendation to ratify the over \$10.8 million in payments in accordance with the FAR and 48 C.F.R 1.602-3. Management stated the vast majority of the purchases were not required to be performed by a contracting officer. SBA further referenced FAR 13.2 *Actions at or Below the Micro-Purchase Threshold*, which sets forth expedited purchase procedures for acquisitions valued at or below the Micro-Purchase threshold. Management stated the FAR establishes the micro-purchase threshold for acquisition of supplies and services using simplified acquisition procedures at \$10,000. For acquisitions of supplies and services to support a response to an emergency or disaster, the micro-purchase threshold is \$20,000 for purchases made inside the United States. Management further stated approximately 99.98 percent of the services provided, including all three vendors, were for less than \$10,000. Management stated the FAR was not applicable to these transactions because the services were not purchased with appropriated funds.

Additionally, SBA stated the administrative action of merely charging a loan off does not relieve the borrower of their financial obligation nor does it transfer this obligation to the federal government. The SBA has recourse options to continue efforts on a loan after charge-off, including the obligation to refer all legally

collectible borrowers and/or guarantors to Treasury's Debt Management Services for collection, including, but not limited to, administrative wage garnishment and offset.

SBA's response to recommendation 3 is unfounded and contradictory to its acknowledgement and agreement to the report finding that it inappropriately used vendors without establishing contracts and its agreement with recommendations 1 and 2. Specifically, SBA agreed that contracts were required for the identified foreclosure and real estate services. In fact, in its response SBA stated they initiated corrective actions regarding this matter in July 2020. SBA also agreed that the vendors used to provide these services were required to be registered in SAM and stated it would ensure this moving forward.

SBA's disagreement to ratify these same services that they agreed were unauthorized commitments and provided by vendors not registered in SAM, as required is confounding. As noted in the report, SBA paid more than \$10.8 million in unauthorized commitments that should be ratified under 48 C.F.R. § 1.602-3. Specifically, SBA did not have the designated officials in place appointed in writing prior to these reimbursements. These actions between SBA and the vendors were not binding because the government official who made these commitments lacked the authority to do so. The FAR defines this as an unauthorized commitment. Ratification of the \$10.8 million should be performed by a contracting officer or an official with the authority to do so as designated by the head of the contracting office.

SBA's assertion that these were expedited purchases made during a disaster, thereby deemed as micro-purchases is also unfounded. Our review found that these purchases were for foreclosure and real estate services (maintenance, legal fees, and etc.). The purchases were made beginning FY 2012 through February 18, 2020 many years after the original disasters. These are not expedited purchases during a disaster or random non-reoccurring purchases. Thus, the micro-purchase clause is not applicable.

Lastly, SBA's assertion that the cost of these vendor services are added to the loans, therefore not purchased with appropriated funds, is also unfounded. We recognize and agree that the charged-off defaulted loans could be collected through Treasury's Debt Management Services. However, this does not diminish the fact that SBA made the payment to these vendors with appropriated funds.

This recommendation can be closed when management provides evidence that the \$10.8 million in unauthorized commitments have been approved by an official with the authority to do so through ratification or provide an alternate solution to satisfy the intent of this recommendation.

Appendix I: Questioned Costs

Questioned costs are costs not supported by adequate documentation at the time of the audit or that otherwise do not comply with legal, regulatory, or contractual requirements, according to 2 CFR § 29003.

Table 1. Payments to Three Uncontracted Vendors

Vendor	Number of Payments Made Without a Contract	Total Payment Amount (\$)
1	22,384	8,111,656
2	9,325	2,352,020
3	2,321	336,800
Total Unauthorized Payments	34,030	\$10,800,476

Source: SBA

Appendix II: Agency Response

U.S. SMALL BUSINESS ADMINISTRATION

WASHINGTON, D.C. 20416



TO: Hannibal M. Ware
Inspector General, Office of Inspector General

FROM: Jihoon Kim
Director, Office of Financial Program Operations

THRU: John A. Miller
Deputy Associate Administrator, Office of Capital Access

SUBJECT: Response to Draft Management Advisory: SBA's Use of Vendors Without Contracts

DATE: January 15, 2021

We appreciate the role the Office of Inspector General (OIG) plays in working with management in ensuring that our programs are effectively managed, and for the feedback provided in this draft management advisory.

The draft management advisory discusses the OIG's identification of the three vendors providing property management services on a population of disaster loans without a contract in place. The draft advisory asserts that since 2012, SBA made a total of 34,030 payments¹, between the three vendors, for services provided further stating that none of the three vendors were registered in the US government's System for Awards Management (SAM), a requirement of all federal agencies. The management advisory ultimately asserts that because SBA had not entered into a government contract and was using these three vendors

¹Any fees incurred during the servicing or liquidation process of a loan are the responsibility of the borrower. The payment is paid to the vendor through a Care and Preservation of Collateral billing. The billing is reflected on the borrower's transcript of account and is the borrower's financial obligation. Federally appropriated funds are not used to pay vendors for these services.

not recorded in SAM, the agency paid more than \$10.8 million in unauthorized commitments that should be ratified under 48 C.F.R. § 1.602-3².

The Office of Financial Program Operations (OFPO), within the Office of Capital Access (OCA), substantially agrees with two of the three OIG audit recommendations as presented in the draft report. OFPO would like to take this opportunity to emphasize that it takes its fiduciary duty to protect taxpayer dollars very seriously. OFPO takes exception to the OIG's assertion that working with these vendors was done so without integrity. As discussed in the management advisory, the National Disaster Loan Resolution Center (NDLRC or Center) initially engaged these vendors to perform small property management services; such services were minimal in value with an average cost of \$317.00 per transaction. The Center initially selected these vendors based upon the price and value of their services as compared to other similar vendors. Over time, the frequency of engagement increased and became a normal practice of the center. Use of these vendors without a contract was not intentional nor was it meant to circumvent federal purchasing and contracting regulations. OFPO recognized OIG's view that a contract is needed for a vendor to provide such services and engaged the SBA's Acquisitions Division in July 2020 to establish a contract vehicle for such services in compliance with federal regulations.

The draft advisory references both the Federal Acquisition Regulation (FAR) and the Code of Federal Regulations (CFR), including several citations regarding "unauthorized commitments." OFPO would like to emphasize that the foreword to the FAR states that it applies to the acquisition of supplies and services with appropriated funds. It is important to note that the nature of these services do not require the use of federally appropriated funds; rather, the fees associated with each service are charged back to the borrower by way of a Care and Preservation of Collateral (CPC) payment. The billing is reflected on the borrower's transcript of account and is the borrower's financial obligation.

The draft advisory surmises that with these disaster loans being in default, and the liquidation of collateral being a last resort to collect on the delinquent debt, any remaining balance is charged off requiring the federal government to ultimately pay for these services. SBA's Standard Operating Procedures, SOP 50 52 2, Disaster Loan Servicing and Liquidation addresses loan charge-off in Chapter 25, Section 1(A), stating the following:

"Charge-off is an SBA administrative action whereby a loan is moved from "liquidation" status to "charged-off" status. It has no impact on the Obligor's liability for the loan balance. Decisions regarding when to charge-off a loan should be consistent with federal

² Ratification is a FAR-based process stipulating the use of appropriated funds. The services provided were not purchased with appropriated funds placing them outside of the FAR.

debt management and collection guidelines.”

To this end, OFPO disagrees with the recommendation to ratify the over \$10.8 million in payments in accordance with the FAR. The administrative action of merely charging a loan off does not relieve the borrower of their financial obligation nor does it transfer this obligation to the federal government. The SBA has recourse options to continue its collection efforts on a loan after charge-off, including the obligation to refer all legally collectible borrowers and/or guarantors to Treasury’s Debt Management Services (DMS) for collection, including, but not limited to, administrative wage garnishment (AWG) and offset.

Furthermore, the vast majority of these purchases were not required to be performed by a contracting officer. FAR Subpart 13.2 sets forth expedited purchase procedures for acquisitions valued at less than the Micro-Purchase threshold. The Micro-Purchase threshold is \$20,000 for the support of response to a declared disaster, or \$10,000 for other acquisitions. Approximately 99.98% of the services provided, including all three vendors, were less than \$10,000. The OIG’s draft advisory cites the FAR confirming ratification as a FAR-based process; as these services were not purchased with appropriated funds, the FAR is not applicable to these transactions.

As previously stated, OFPO will continue its efforts with the Acquisitions Division and will establish a contract vehicle with a vendor registered in SAM, in accordance with federal procurement and contracting regulation

OIG made the following recommendations:

1. Require responsible personnel to execute a contract for foreclosure and real estate services to ensure the procurement of services are obtained and authorized in accordance with the Federal Acquisition Regulation requirements.
2. Ensure that vendors used to provide foreclosure and real estate services are registered in SAM, as required.
3. Ratify the over \$10.8 million in payments in accordance with the FAR and 48 C.F.R. § 1.602-3.

Management’s response to the recommendations in the draft report is as follows:

Management acknowledges the following recommendations listed in the report:

1. OFPO agrees with this recommendation and has identified responsible personnel to execute a contract for foreclosure and real estate services to ensure the procurement of

services are obtained and authorized in accordance with the Federal Acquisition Regulation requirements.

2. OFPO agrees with this recommendation and will ensure that vendors used to provide foreclosures and real estate services are registered in SAM, as required.

Management ***does not agree*** with the following recommendation listed in the report:

3. OFPO will complete the corrective actions required under Recommendation 1 and 2 of this Management Advisory but does not agree that over \$10.8 million must be ratified in accordance with the FAR and 48 C.F.R. § 1.602-3.