

**LACK OF DOCUMENTATION AND INCORRECT
ACCOUNTING FOR RECOVERY ACT 7(A) LOAN
GUARANTY APPROVALS**

Report Number: ROM 11-02
Date Issued: December 15, 2010

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



**U.S. Small Business Administration
Office Inspector General**

Memorandum

To: Steven Smits
Associate Administrator for Capital Access
/s/ Original Signed
From: Peter McClintock
Deputy Inspector General
Subject: Recovery Act 7(a) Loan Guaranty Approvals
ROM 11-02

Date: December 15, 2010

Attached is the Management Letter issued by KPMG LLP which identifies a matter that came to their attention during the audit of SBA's FY 2010 financial statements. The objective was to determine SBA's compliance with its guidance for approving 7(a) loan guaranties funded under the Recovery Act.

KPMG addressed recommendations to the Director for the Office of Financial Program Operations. We provided a draft of KPMG's report to this official or his designee, who concurred with the finding. The official or designee agreed to implement the recommendations or has already taken action to address the underlying conditions.

Should you or your staff have any questions, please contact Jeffrey R. Brindle, Director, Information Technology and Financial Management Group at (202) 205- [FOIA ex. 2]

Cc: Jonathan I. Carver



KPMG LLP
2001 M Street, NW
Washington, DC 20036-3389

**AMERICAN RECOVERY AND REINVESTMENT ACT
MANAGEMENT LETTER**

December 15, 2010

CONFIDENTIAL

Office of the Inspector General,
U.S. Small Business Administration, and
Administrator of the SBA:

We were engaged by the Office of Inspector General (OIG) to perform supplemental audit services for the purpose of testing certain transactions and system enhancements related to the U.S. Small Business Administration's (SBA) implementation of the American Recovery and Reinvestment Act of 2009 (ARRA). The procedures were performed as part of an expanded scope of our fiscal year 2010 audit of SBA's consolidated financial statements. In planning and performing our audit procedures related to SBA's implementation of ARRA, we considered internal control related to the implementation and operation of the ARRA programs that were in place as of September 30, 2010.

During our audit, we noted a matter involving internal control concerning a lack of documentation and incorrect accounting pertaining to ARRA 7(a) loan guaranty approvals. The comments and resulting recommendations, presented in the Exhibit, have been discussed with the appropriate members of management and are intended to improve internal control or result in other operating efficiencies.

We would be pleased to discuss these comments and resulting recommendation with you at any time.

This report is intended solely for the information and use of the OIG, SBA management, and others within the organization and is not intended to be, and should not be, used by anyone other than these specified parties.

KPMG LLP

U.S. SMALL BUSINESS ADMINISTRATION
American Recovery and Reinvestment Act
Management Letter Comments
FY 2010

LACK OF DOCUMENTATION AND INCORRECT ACCOUNTING

Conditions:

During our testwork over American Recovery and Reinvestment Act (ARRA) 7(a) loan guaranty approvals at the Sacramento Loan Guaranty Processing Center (LGPC), we noted the following:

1. Lack of Documentation

Defense Bill 7(a) loan guaranty #3827945004 was cancelled and replaced with a new loan guaranty #3805545001 due to an unknown and undocumented issue. The loan file did not contain documentation to support the loan cancellation and the subsequent approval of a non-ARRA 7(a) loan.

2. Incorrect Accounting

For Defense Bill 7(a) CAPLine loan guaranty #3841855008, the approval was authorized in error. The loan guaranty was not eligible for approval under the Defense Bill, because the term in the loan application was only one year.

Criteria:

Department of Defense Appropriations Act, 2010 P.L. 111-118, states:

“SEC. 1006. (a) There is hereby appropriated \$125,000,000, for an additional amount for ‘Small Business Administration—Business Loans Program Account’ for fee reductions and eliminations under section 501 of division A of the American Recovery and Reinvestment Act of 2009 (Public Law 111–5) and for the cost of guaranteed loans under section 502 of such division.”

Office of Management and Budget (OMB) Circular A-129 Revised, *Policies for Federal Credit Programs*, states:

“Approved loan files (or other systems of records) shall contain adequate and up-to-date information reflecting terms and conditions of the loan, payment history, including occurrences of delinquencies and defaults, and any subsequent loan actions which result in payment deferrals, refinancing, or rescheduling.”

Federal Register, Vol. 74 No. 108, *Applicability Date of Fee Relief Provisions*, states:

“Section 501 fee relief applies to 7(a) loan applications with a term greater than one year that are approved, or issued loan numbers for delegated lender loans, by SBA on or after February 17, 2009.”

Causes:

The issues identified were attributed to inadequate supervisory loan officer review over the loan guaranty approval process. According to LGPC personnel, the loan submit button was hit twice, which required the

U.S. SMALL BUSINESS ADMINISTRATION
American Recovery and Reinvestment Act
Management Letter Comments
FY 2010

cancellation of loan guaranty #3827945004. Additionally, LGPC staff inadvertently sent an authorization with Section 501 of ARRA for loan guaranty #3841855008, which should have been recorded as a non-ARRA CAPLine loan.

Effects:

Lack of documentation and incorrect accounting increases the risk of potential errors and misstatements in the financial statements and note disclosures. Specifically, the total 7(a) loan guaranty approval account (SBA's share) was overstated by \$1,499,910. KPMG notes that SBA researched all the CAPLine loans known to be erroneously charged to ARRA/ARRA-like Treasury Appropriation Fund Symbols. As a result, SBA identified 11 (out of 78) additional, incorrectly funded CAPLine loans approved as of the date of our testing. These errors resulted in a total overstatement in the 7(a) guaranty approval account (SBA's share) of \$3,440,835.

Recommendation:

We recommend the Office of Financial Program Operations Director:

1. Reinforce the importance of effective review of loan guaranty applications by a loan officer and supervisory loan officer to ensure that loan files contain proper documentation to support the approval or denial determination, that loan guaranty transactions are properly recorded in the Loan Accounting System, and that transactions are posted to the proper program and financing accounts.

Management's Response:

SBA management concurs with the findings and recommendation.