



**U.S. SMALL BUSINESS ADMINISTRATION**  
**OFFICE OF INSPECTOR GENERAL**  
Washington, DC 20416

<b>AUDIT REPORT</b>
<b>Issue Date: June 29, 2004</b>
<b>Number: 4-27</b>

**TO:** Mike Pappas  
Associate Administrator for Field Operations

/s/ original signed [FOIA Ex. 6]

**FROM:** Robert G. Seabrooks  
Assistant Inspector General for Auditing

**SUBJECT:** Audit of San Francisco District Office Administrative Activities Related  
to the Silicon Valley Small Business Development Center

Attached is a copy of the subject report. The report contains one finding and two recommendations to the Associate Administrator for Field Operations.

The finding in this report is the conclusion of the Office of Inspector General's Auditing Division. The recommendations in this report are subject to review and implementation of corrective action by your office in accordance with existing Agency procedures for audit follow-up and resolution. Please provide your management decision for each recommendation made to you within 30 days from the date of this report using the attached SBA Forms 1824, Recommendation Action Sheet.

If you have any questions about the issues contained in the report, please contact Garry Duncan, Director, Credit Programs Group, at (202) 205-[FOIA Ex. 2].

Attachments

**Audit of San Francisco District Office Administrative Activities  
Related to the Silicon Valley Small Business  
Development Center  
San Francisco, CA  
Report No. 4-27**

**The finding in this report is the conclusion of the OIG's Auditing Division based on testing of SBA operations. The finding and recommendations are subject to review, management decision, and corrective action in accordance with existing Agency procedures for follow-up and resolution. This report may contain proprietary information subject to the provisions of 18 USC 1905 and must not be released to the public or another agency without permission of the Office of Inspector General.**

**Audit of San Francisco District Office Administrative Activities  
Related to the Silicon Valley Small Business  
Development Center**

**Table of Contents**

	<u>Page</u>
<b>SUMMARY</b> .....	i
<b>INTRODUCTION</b>	
A. Background .....	1
B. Objective and Scope .....	2
 <b>RESULTS OF AUDIT</b>	
<b>Finding and Recommendations</b>	
Improvements are Needed in the Operation of the Silicon Valley Small Business Development Center .....	3
 <b>APPENDICES</b>	
A – Management Response	
B – Report Distribution	

## SUMMARY

The Office of Small Business Development Centers' draft examination reported program income generated by the Silicon Valley Small Business Development Center (SVSBDC) was not properly managed. Concerned that improper activities by SBA personnel may have occurred, the Small Business Administration (SBA) Administrator requested the Office of Inspector General (OIG) to conduct an audit.

The audit objective was to determine whether program income was properly managed and whether selected activities were conducted in compliance with applicable regulations. The audit concluded that \$57,645 of program income for the SVSBDC was inappropriately collected, commingled with unrelated funds, and disbursed by the San Jose Service Core of Retired Executives (SCORE) office. In addition, \$225,000 was paid for contractor services that were not acquired in accordance with established guidelines.

These conditions occurred because [FOIA Ex. 6] (i) improperly implemented procedures which resulted in SVSBDC funds being handled contrary to SBDC Cooperative and Cosponsorship Agreements, and (ii) influenced the sole-source selection of the SBDC-Technical Assistance Program Director in possible violation of ethics and employee standards of conduct rules.

We recommend the Associate Administrator, Office of Field Operations:

- Determine what, if any, disciplinary or other administrative actions should be taken against [FOIA Ex. 6] for developing a Cosponsorship policy memorandum that overrode the SBDC cooperative agreement.
- Direct [FOIA Ex. 6] to instruct the San Jose SCORE Chapter to return all SVSBDC program income that was generated at the E-Center and is being held in the E-Center Special Account to West Valley Community College.

The Associate Administrator has initiated a thorough review of the issues raised by the audit and will provide a comprehensive response to Recommendation 1 within 30 days. In response to recommendation 2, program income has been returned to the SVSBDC.

## **A. Background**

Section 21(a)(1)(a) of the Small Business Act (Act) gives SBA the authority to provide qualified applicants with grants to help establish small business development centers. The centers provide a broad-based system of assistance for the small business community. SBA executes this authority through the SBDC Program. SBDCs link Federal, state, and local government resources with those of the educational community and the private sector. SBDCs provide Small businesses with access to counseling services, management and technical assistance, information, research, and access to business analysts.

In California, SBA had awarded a Cooperative Agreement (CA) to the California Technology, Trade and Commerce Agency (CTTCA) to run a statewide SBDC program. CTTCA, in turn, subcontracted with West Valley-Mission Community College District (West Valley) to establish and host an SBDC Center in San Jose. The name of the center opened by West Valley was Silicon-Valley SBDC. The subcontract, among other things, required that West Valley monitor and be responsible for program income and expenditures made as a result of the CA. The subcontract also stated that West Valley must “keep all books, records, accounts, and documents pertaining to this agreement separate from other activities unrelated to the agreement.” SBA Standard Operating Procedure (SOP) 60 16 reiterates West Valley’s obligation to comply with the terms of the CA.

The CTTCA/West Valley subcontract also required that West Valley host a technology advisory program in the San Francisco Bay area. The mission of the program was to improve business operations by providing technology consulting services to small businesses. To this end, the SBDC Technology Assistance Program (SBDC-TAP) was created. The SBDC-TAP Director was “hired” through a contractual agreement with West Valley.

In April 2000, the San Jose Entrepreneur Center (E-Center) was opened under the authorization of SBA Cosponsorship Agreement #00-0912-16. The cosponsorship agreement documented the relationship established whereby SBA, in conjunction with other entities, would provide training and counseling programs to assist small businesses. The major signers of the Cosponsorship Agreement included SBA, the City of San Jose, the San Jose State University Foundation, the San Jose Service Core of Retired Executives (SJSCORE) Chapter, and the SVSBDC. The E-Center offered small businesses and entrepreneurs one facility where they could obtain assistance with their business needs. The SVSBDC and SJSCORE Chapter were two of the organizations that operated within the E-Center. The Cosponsorship Agreement identified the San Jose State University Foundation as the fiscal agent that would provide fiduciary responsibility for the accounting of all revenues and expenses of the E-Center.

**B. Objective and Scope**

The audit objective was to determine whether program income was properly managed by West Valley and the SVSBDC and if selected activities were conducted in compliance with applicable regulations. We reviewed income generated by training activities from January 2000 through August 2003. SBA and SVSBDC officials were interviewed and procurement procedures and activities related to filling of the program director's position were reviewed. The audit was conducted in San Francisco and San Jose, California in accordance with generally accepted Government Auditing Standards.

## RESULTS OF AUDIT

### **Finding Improvements are Needed in the Operation of the Silicon Valley Small Business Development Center**

Program income for SVSBDC was inappropriately collected, commingled with unrelated funds, and disbursed by the SJSCORE office. In addition, the services of the Director of the SBDC-TAP were not acquired in accordance with guidelines. These conditions occurred because [FOIA Ex. 6] (i) improperly implemented procedures for handling funds of the E-Center and its cosponsors which were contrary to the SBDC Cooperative and Cosponsorship Agreements; and (ii) influenced the sole source selection of the SBDC-TAP Director in possible violation of ethics and employee standards of conduct rules. As a result, the SBDC was unable to collect and use \$57,645 in program income and authorized \$225,000 for contracted services, which did not comply with the competitive procurement requirements of the CA.

### **West Valley Mission Community College District did not control program income**

Contrary to the cooperative and cosponsorship agreements, the SJSCORE Chapter collected, commingled, and disbursed up to \$57,645 of program income from the SVSBDC training activities that were conducted at the E-Center. This occurred because [FOIA Ex. 6] issued a “cosponsorship policy memorandum” dated August 5, 2003, that had the effect of circumventing the requirements of the West Valley/CTTCA cooperative agreement. The memorandum from the [FOIA Ex. 6] required the SJSCORE Chapter to receive and manage funds generated by training events held by the SVSBDC. According to the memorandum:

- the SJSCORE Chapter designation as fiscal agent was justified because services would be efficient and ensure timely responses to SVSBDC training class needs,
- the SJSCORE Chapter services would remove any inconveniences caused by the historical problems with West Valley’s management of training revenues, and
- procedures that generate the best service to the small business program should supersede established regulations and guidance.

[FOIA Ex. 6] responsibilities for the SBDC program are outlined in SOP 60 16. Specifically, [FOIA Ex. 6] are responsible for (i) monitoring the cooperative agreement and the operations of the SBDC, and (ii) facilitating SBDC cooperation with SBA resources, performing SBDC programmatic and budget reviews, and referring clients for services. The SOP, however, does not permit [FOIA Ex. 6] to establish alternative procedures which cause SBDCs to be out of compliance with a cooperative agreement. Furthermore, [FOIA Ex. 6] have no authority to create cosponsorship policy memorandums that supersede the contractual requirements of SBA cooperative

agreements or amend the cosponsorship agreement without following established procedures found in SOP 90 75 2.

As a result of the [FOIA Ex. 6] actions, West Valley was unable to meet the cooperative agreement's requirement to exercise its fiduciary responsibility. Specifically, (i) program income generated by training activities was not managed by West Valley, (ii) income was not separated from other unrelated activities, and (iii) financial records were not maintained, as required.

Discussions held with the former Acting Associate Administrator for the Office of Small Business Development Centers (OSBDC) and the [FOIA Ex. 6] during our review resulted in a change of policy regarding SVSBDC generated program income. The OSBDC discussed the issue with the [FOIA Ex. 6]. The [FOIA Ex. 6] then issued a memorandum to restore management of SVSBDC program income to West Valley. From that point forward, the SVSBDC should have been collecting training income generated through SVSBDC training classes and paid at the door. On-line registration payments were to be forwarded to the SVSBDC when received by the San Jose SCORE Chapter. The SVSBDC Interim Director was to forward all collections to West Valley upon receipt. By January 2004, approximately \$20,000 in SVSBDC program income held by the SJSCORE was to be transferred to the SVSBDC for management as required by the CA. As of March 15, 2004, the Interim SVSBDC Director had been unsuccessful in accessing SVSBDC funds held by the SJSCORE in the E-Center's account.

### **The program director position was improperly filled**

In Fiscal Years 2001, 2002, and 2003, the SBDC Technology Assistance Program (TAP) Director was "hired" using sole-source selection procedures which were contrary to the West Valley cooperative agreement. West Valley did not solicit competitive bids for the position because [FOIA Ex. 6] suggestion for the director position was hired.

The [FOIA Ex. 6] issued a memo detailing the proposed implementation of a stand-alone Technical SBDC that would focus on the technological development of small businesses. The Technical SBDC would be contracted through the existing host organization-West Valley College. According to the memo, the process for selecting SBDC Directors in Community Colleges hosting SBDCs was time consuming and subject to complex hiring policies. To avoid delays, the District "approached West Valley College about an alternative hiring approach for this position." The Technical SBDC Director contract was estimated at \$75,000 - \$85,000, annually. The [FOIA Ex. 6] acknowledged "this is typically more than the college can contract without advertising for bids," but went on to say "there appears to be the means to make this arrangement possible."

Discussions with the previous SBDC Director, the Interim SBDC Director, key West Valley and SCORE personnel revealed an atmosphere where the parties were reluctant to rebuff the [FOIA Ex. 6] requests. West Valley personnel indicated [FOIA Ex. 6] was hands-on at every level. The interviews also reflected a concern that the



[FOIA Ex. 6] had significant influence over whether a college was reinstated as an SBDC. [FOIA Ex. 6] maintains that his suggestions were just that and it is incumbent upon program officials to follow their established policies and procedures when agreeing to implement suggested ideas or policies.

Employees are required to act impartially and not give preferential treatment to any private organization or individual per 5 CFR 2635.101(a) (8). Also, 13 CFR 105.206 requires every employee to follow all agency rules, regulations, operating instructions and other directives in the performance of their official duties. [FOIA Ex. 6] did not comply with these requirements.

Exhibit D 3, Purchase Orders & Subcontracting Provisions, of the CA requires West Valley to obtain three competitive bids on each contracting action greater than \$2,500 or justify why the bids could not be obtained. SOP 60 16, SBDC Program Policy Guidelines state the SBDC State Director is responsible for program implementation and limits the degree of involvement from the [FOIA Ex. 6] to oversight, advocacy, and referral services. [FOIA Ex. 6] acted beyond his scope of authority thereby influencing the SVSBDC's hiring process. As a result of the [FOIA Ex. 6] influence, procurement of services totaling \$225,000<sup>1</sup> for the TAP Director position did not comply with competitive contracting requirements and may not have been obtained from the most cost effective source.

## **Recommendations**

We recommend that the Associate Administrator for Field Operations take the following actions:

- 1 A. Determine what, if any, disciplinary or other administrative actions should be taken against [FOIA Ex. 6] for developing a Cosponsorship policy memorandum that overrode the SBDC cooperative agreement.
- 1 B. Direct [FOIA Ex. 6] to instruct the SJSCORE Chapter to return all SVSBDC program income that was generated at the E-Center and is being held in the E-Center Special Account to West Valley Community College.

## **Management Comments**

The Associate Administrator has initiated a thorough review of the issues raised by the audit and will provide a comprehensive response to Recommendation 1 within 30 days. In response to recommendation 2, program income has been returned to the SVSBDC.

---

<sup>1</sup> The TAP director received \$75,000 in fiscal year (FY) 2001, \$100,000 in FY2002, and \$50,000 for the first 6 months of FY2003.

## **OIG Evaluation of Office of Field Operations Comments**

The comments were responsive to the recommendations. Final resolution to recommendation 1 will be accomplished through the audit follow up process.

## Report Distribution

<u>Recipient</u>	<u>No. of Copies</u>
Associate Deputy Administrator for Management and Administration .....	1
Associate Administrator for the Office of Small Business Development Centers .....	1
Associate Administrator for the Office of Business Initiatives .....	1
General Counsel.....	3
Office of Chief Financial Officer Attention: Jeffrey Brown .....	1
General Accounting Office .....	1