




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

**ADVISORY MEMORANDUM**

**Issue Date: April 29, 1999**

**Number: 99-01**

**TO:** Aida Alvarez, Administrator

**FROM:**   
Victor R. Ruiz, Acting Assistant Inspector  
General for Auditing

**SUBJECT:** Budget Execution Process

**INTRODUCTION**

As you requested, we initiated a review of SBA's FY 1999 budget execution process as it concerned the "Reserve Account." The objectives of our review were to determine whether: (1) the policies and procedures for estimating expenses and managing the reserve were adequate, and (2) current estimates for the reserve were reasonable. The review focused on the FY 1999 "Reserve Account" from November 4, 1998 (the date it was established) to April 1, 1999.

We interviewed the Acting Chief Financial Officer; Deputy Chief Financial Officer; the former SBA Budget Officer; Acting Budget Officer; Assistant Administrator for Administration; Chief Information Officer; consultants from SOZA and Co., Ltd. (SOZA); and various other SBA employees. We also evaluated SBA policies and procedures for budget execution, and available documentation for charges to the "Reserve Account."

**BACKGROUND**

On February 19, 1999, SBA issued Procedural Notice No. 0000-1392, Hiring and Other Funding Restrictions, to address the Agency's concern on the funding status for the remainder of FY 1999. The Notice required that new hiring and competitive promotions be approved by the Chief Operating Officer (COO). Also, the Agency hired an independent contractor (SOZA), and tasked them with providing budgetary, accounting, and general financial management advice and assistance. SOZA reviewed SBA's budgeting, accounting, and personnel systems. In our review, we relied on SOZA's estimates for compensation and benefits (C&B).

## **RESULTS**

There were flaws in SBA's FY 1999 budget execution process relating to the reserve account. Policies and procedures for estimating expenses and managing the reserve were not adequate because (1) the initial reserve balance was overstated as it was based on reduced allocations to other accounts that did not materialize, and (2) procedures to document expenditures were not always followed.

As of April 1, 1999, the Office of the Chief Financial Officer (OCFO) showed a balance of \$2,311,000. Using the most recent estimates prepared by SOZA for C&B, we estimate the balance of the reserve account on April 1, 1999 to be \$3,790,000. Our estimate is based on several adjustments (described below) and an assumption that there would be no hiring after May 1999. It does not consider a projected rent shortfall of \$2,891,000. It also does not take into account any other cost reduction efforts occurring in the Agency. These issues are discussed in detail below.

### **Estimating Expenses**

OCFO, in a document entitled "Budget Process Vision," stated in its first principle that "There must be an adequate level of discretionary funds at the beginning of the year and at all times during the year, for the Administrator's new and existing initiatives." To achieve the first principle of the "Budget Process Vision," and create a \$17,289,000 reserve account, OCFO made three main downward adjustments to non-reserve accounts. These adjustments included C&B reductions of \$1.7 million for outstanding recruitments (the number of recruits stayed constant) and \$2.0 million for recruitments to be announced. In addition to the C&B adjustments, the OCFO reduced the operating budgets of all program offices by 10 percent (\$6.6 million) and the estimated expenses for rent by \$2.9 million. The reserve was overstated, however, because actions were not taken to implement the budget reductions. For instance, the FY 1999 estimate for rent was \$31.8 million based on prior GSA billings plus a 2 percent increase. The \$2.9 million reduction resulted in only \$28.9 million available for rent. The Assistant Administrator for Administration stated such savings on the rent could not be realized in FY 1999.

Some of the Agency officials interviewed stated that the former CFO, in his efforts to make the "Reserve Account" as large as possible, did not use a realistic approach in the initial budget allotments to the Agency program offices. The C&B adjustment was based on the CFO's position that recruitment actions would not attain fruition at all. This position, however, was not formally communicated to the program offices performing the hiring, and in fact, the offices hired at an accelerated pace. The reduction in the operating budgets of the program offices was made without any specific plans to achieve these reductions. Also, the former Budget Officer stated that the original estimate for the rent budget was reasonable and appropriate. The unreasonable adjustments were rectified on November 9, 1998, when the reserve

account was charged \$6.6 million for the operating budgets of the program offices and on January 20, 1999, when the reserve account was charged \$5.4 million for C&B. These two charges, totaling \$12.0 million, reduced the reserve account by nearly 70 percent within two months of its establishment and supports the conclusion that the initial balance in the reserve account was overstated.

### Management of the Reserve Account

To determine the effectiveness of the reserve account management, we reviewed the establishment and use of the reserve account. We found that the established process for using the reserve account was not followed.

#### Establishment of the "Reserve Account"

The "Reserve Account" is a term used to describe SBA's unallocated funds that are available for discretionary use and unanticipated needs. The available balance at any given point in time is determined by subtracting the total funds allocated from the total sources of funds. The following chart is an illustration of how the available balance is determined.

Sources of Funds (Direct Appropriations, Transfers from Disaster or Other Agencies, Carryovers, Estimated Fee Income, etc)	XXX	-
Less: Allocation of Funds (Compensation & Benefits, Non-Credit Programs (SBDC, USEAC, etc), Special Initiatives (i.e., Special Appropriations), Operating Expenses, etc)	XXX	
= Reserve Account	XXX	

The reserve account is not an account in the Agency's official Federal Financial System (FFS). Instead, it is an off-line account maintained by the OCFO on an Excel spreadsheet that is updated as transactions are approved and entered into the FFS. As stated above, the reserve balance was largely created by cutting budgets for hiring new employees, rent, and other expenses without assuring that these cuts could be sustained. As a result, the initial balance of funds available for discretionary use and unanticipated needs was overstated.

#### Use of the "Reserve Account"

We checked the process to request and approve the use of funds from the reserve account and tested for the proper usage of the funds. The process was outlined in the OCFO's "Budget Process Vision" first issued in May 1998. The process was then formalized in SBA Procedural Notice No. 2000-489, dated January 8, 1999. The process required an e-mail request through an Associate Deputy Administrator or comparable executive to the Budget Officer, with a copy

to the CFO and DCFO. In addition, the requestor was to complete SBA Form 2097, Funding Request. Agency officials informed us that the CFO could approve individual requests that did not exceed \$25,000. All other requests required the formal approval of the Administrator or Deputy Administrator.

As of February 1999, when our review was initiated, 26 of the 38 transactions that affected the "Reserve Account" were for amounts that exceeded \$25,000. Generally, the process for the request and approval of the reserve account was not followed. Only 1 request was accompanied by SBA Form 2097; 25 requests did not have the form. Also, we were unable to locate documents to indicate formal approval by the Administrator or Deputy Administrator. The only approval documents were e-mail message, in which the CFO or DCFO informed an OCFO employee to allocate funds and enter the data into FFS.

To ensure the proper usage of the funds, we analyzed the 38 transactions and confirmed that funds were properly allotted in the FFS. At random, we selected three transactions for an in-depth review. We traced the funds to the program office account and determined if the funds were used for the intended purpose. Also, we tested to see if any of the requested funds were unspent. We concluded that the funds were used for their intended purpose and all requested funds were obligated or spent.

#### **Reasonableness of Current Estimate**

As of April 1, 1999, the estimate of the reserve account was \$3,790,000 based on data provided to us. We derived the estimate by using the \$2,311,000 shown as the operating budget reserve in OCFO's records and making adjustments to reflect the latest estimate for C&B made by SOZA as of March 26, 1999. SOZA estimated that SBA would spend \$3,953,000 more for C&B than the original C&B estimate (when the reserve account was established). However, the reserve account had been charged \$5,432,000 for C&B on January 20, 1999. Therefore, the reserve account had been overcharged by \$1,479,000 (\$5,432,000 - \$3,953,000) due to the excessive January 20th C&B estimate.

The COO informed us that other adjustments have been made to the "Reserve Account" estimate subsequent to April 1, 1999. These adjustments would need to be reconciled to the following data to determine the estimated balance of the "Reserve Account" after April 1.

<b>Reserve Account (In thousands)</b>		
Beginning Balance (November 4, 1998)		\$17,289
Less: Charges (thru April 1, 1999)		<u>14,978</u>
Balance (April 1, 1999)		\$2,311
<b>Adjustments to Balance</b>		
SOZA estimate for C&B (March 26, 1999)	\$213,376	
Adjusted estimate for C&B (October 4, 1998)	<u>209,423</u>	
Less: Charges to Reserve Account		(\$3,953)
CFO's estimate for C&B (January 20, 1999)	\$214,855	
Adjusted estimate for C&B (October 4, 1998)	<u>209,423</u>	
Add: Charges to Reserve Account Prior to SOZA estimate		<u>5,432</u>
Increase in Reserve Account		<u>1,479</u>
Ending Balance (April 1, 1999)		<u>\$3,790</u>

### **CONCLUSION**

On March 26, 1999, SOZA issued its report entitled SBA Budgeting Analysis. Their report contains numerous recommendations to improve SBA's budget execution process. We have reviewed SOZA's work and believe if their recommendations are implemented, SBA will have better control over the budget execution process. We met with the Acting CFO and the COO, both of whom advised us that SOZA's recommendations were being implemented. The Acting CFO showed us the system he is using to track implementation. This system will help ensure that SOZA's recommendations will be implemented. If you have any questions regarding this matter, please call me at 205-7204.

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Chief of Staff ..... 1

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