

**AUDIT OF RHODE ISLAND
DISTRICT ADVISORY COUNCIL**

AUDIT REPORT NUMBER 0-28

SEPTEMBER 29, 2000

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.



**U.S. Small Business Administration
Office of Inspector General
Washington, DC 20416**

AUDIT REPORT
Issue Date: September 29, 2000
Number: 0-28

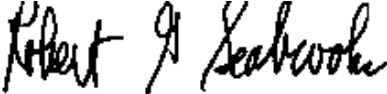
TO: Aida Alvarez, Administrator

Robert J. Baskin, Associate Administrator for Field Operations

Charles W. Payne, General Counsel

Kristine Marcy, Chief Operating Officer

Mark S. Hayward, District Director, Rhode Island District Office



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

SUBJECT: Audit of Rhode Island District Advisory Council

Attached is a copy of the subject audit report. The report contains two findings with one recommendation to the SBA Administrator, three recommendations to the Associate Administrator for Field Operations, two recommendations to the General Counsel, one recommendation to the Chief Operating Officer, and one recommendation to the Rhode Island District Office Director.

The findings in this report are the conclusions of the Office of Inspector General's Auditing Division based on a review of the Rhode Island District Advisory Council's records; pertinent laws, regulations, and policies; and interviews with SBA and General Services Administration (GSA) officials. The findings and recommendations are subject to review and implementation of corrective action 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 on the attached SBA Forms 1824, Recommendation Action Sheet.

Any questions or discussion of the issues contained in the report should be directed to Robert Hultberg, Director, Business Development Programs Group, at (202) 205-7204.

Attachment

Audit of Rhode Island District Advisory Council

TABLE OF CONTENTS

	Page
SUMMARY	i
INTRODUCTION	
A. Background	1
B. Audit Objective and Scope	2
RESULTS OF AUDIT	
A. Rhode Island District Advisory Council (RI Council) Engaged in Non-Advisory Activities	3
B. Improvements Needed in SBA Management and Oversight of District Advisory Councils	7
APPENDICES	
A: SBA Management’s Response	
B: Report Distribution	

SUMMARY

The purpose of this audit was to determine whether the Rhode Island District Advisory Council (the RI Council) operated in accordance with governing laws, regulations, and policies. We found that various RI Council activities and SBA actions to oversee the RI Council were not in accordance with the Federal Advisory Committee Act, Public Law 92-463 (FACA); Code of Federal Regulations (CFR); and SBA's standard operating procedures for Advisory Councils (the SOP). The SOP, however, contradicts SBA's District Advisory Council charter and possibly FACA regarding what Advisory Councils can and cannot do in many instances. This and other evidence lead to the additional conclusion that improvements are needed in SBA's management and oversight of District Advisory Councils.

Though under the current charter SBA's District Advisory Councils are only allowed to advise, the RI Council engaged in the following SBA or SBA related activities for non-advisory purposes:

- Soliciting funds and charging fees;
- Maintaining a private checking account;
- Paying expenses for and managing SBA events, e.g. Small Business Week;
- Developing and giving training seminars;
- Developing and maintaining a website; and
- Entering into Memoranda of Understanding (MOUs) and co-sponsorship agreements with SBA and other organizations.

A former Rhode Island District Director stated that he followed the example of other SBA District Offices when he encouraged and allowed the RI Council to engage in non-advisory activities. He believed that the SOP permitted Advisory Councils to engage in such activities. The present District Director and District Counsel stated that they followed the SOP, which cites non-advisory activities. The SOP does cite non-advisory activities, contradicting the charter and possibly FACA in those areas. FACA and the charter, however, take precedence over the SOP. The present District Director stated that the RI District Office was never sent a copy of the charter and, therefore, was unaware that the Council was restricted to only providing advice.

SBA needs to improve its management and oversight of its District Advisory Councils. Though required by FACA, SBA had no Committee Management Officer (CMO) to manage and oversee the operations of the District Advisory Councils and SBA's reporting requirements under FACA.

We recommend that SBA:

- Ensure that District Advisory Councils do not engage in any non-advisory activities unless and until the charter is amended;
- Determine whether impermissible augmentation of SBA's appropriation has occurred and, if so, take appropriate corrective actions;
- Properly dispose of all funds which District Advisory Councils should not possess;

- Ensure that the SOP provides for full compliance with governing laws, District Advisory Council charters, and regulations; and
- Appoint a Committee Management Officer (CMO) to control and supervise the establishment, procedures and accomplishments of Advisory Councils.

SBA management responded that they intend to provide a response to all recommendations made in the final audit report. The response also indicated they have been in the process of improving the district advisory council program and eliminating the deficiencies found by the audit. The response in its entirety is included as Appendix A.

INTRODUCTION

A. BACKGROUND

SBA District Advisory Councils are advisory committees established according to the Small Business Act and an approved charter filed with GSA, the Library of Congress and the Small Business Committees of Congress. The RI Council is one such advisory committee, established at the discretion of the SBA Administrator pursuant to the provisions of FACA and the Small Business Act. The term "advisory committee" means any committee, board, commission, council, conference, panel, task force, or other similar group, or any subcommittee or other subgroup.

Congress recognized the importance of interacting with the nation's private citizens and having them contribute to the government's overall efforts. Furthermore, Congress found that advisory committees are a useful and beneficial means of furnishing expert advice, ideas, and diverse opinions to the Federal government. Congress, however, also found that the need for many existing advisory committees has not been adequately reviewed. In 1972, Congress enacted FACA to ensure advisory committees:

- provide relevant and objective advice;
- are open to the public;
- act promptly to accomplish their work; and
- comply with reasonable cost controls and record keeping requirements.

Government-wide, approximately 1,000 advisory committees provide advice to the President and Federal agencies. With issuance of Executive Order #12024, the General Services Administration's Committee Management Secretariat became responsible for oversight of these Federal advisory committees. Title 41 CFR, Part 101-6, contains guidance regarding FACA implementation. Though called the Rhode Island District Advisory Council within SBA, GSA knows the RI Council as the Providence District Advisory Council.

The Small Business Act of 1953 Section 8(b)(13), as amended, empowers SBA "to establish such advisory boards and committees as may be necessary to achieve the purpose of this Act..." Along with other types of advisory committees, SBA established District Advisory Councils. The District Advisory Councils are chartered for two-year terms. SBA has one master charter for all of its District Advisory Councils. According to SBA's 1999 District Advisory Council charter:

The Councils will provide advice and opinions regarding the effectiveness of and need for SBA programs, particularly within the local districts which members represent The Councils will provide advice and recommendations only.

B. AUDIT OBJECTIVE AND SCOPE

The audit objective was to determine whether the RI Council was operating in accordance with governing laws, regulations, and policies. We reviewed a judgmental sample of the RI Council's records (financial, meeting minutes, correspondence, etc.) for the period 1992 through 1999, and interviewed officials in the following offices: General Counsel (OGC); Chief Financial Officer (OCFO); the Boston Regional Office; the Rhode Island District Office; and GSA's Committee Management Secretariat. We requested and received an OGC legal opinion concerning whether SBA District Advisory Councils can engage in non-advisory activities. According to this opinion, under the present charter, the Council's sole function is to provide SBA advice and recommendations, and non-advisory activities or activities for purposes other than advice are not allowed.

The fieldwork was conducted from December 20, 1999 to February 28, 2000. The audit was conducted in accordance with Government Auditing Standards.

RESULTS OF AUDIT

Finding A: Rhode Island District Advisory Council (RI Council) Engaged in Non-Advisory Activities.

Although SBA District Advisory Councils are only allowed to advise, the RI Council engaged in numerous activities that were non-advisory. A former Rhode Island District Director stated that he followed the example of other SBA District Offices when he encouraged the RI Council to engage in these non-advisory activities. He believed that the RI Council could do so based on the language of the SOP, which cites various non-advisory activities. By engaging in non-advisory activities, the RI Council violated its charter and possibly FACA, and possibly augmented SBA appropriations.

The RI Council engaged in non-advisory SBA or SBA-related activities including:

- Raising approximately \$586,000 from 1993 through 1999 by soliciting funds for events such as Small Business Week and MEDWeek, and charging fees for training;
- Maintaining a private checking account (the account had a balance of \$34,176.47 at December 17, 1999) for purposes not authorized by the charter;
- Paying approximately \$530,000 of SBA and SBA related expenses;
- Managing SBA events, e.g. Small Business Week;
- Developing and maintaining a website for purposes not authorized by the charter;
- Developing and presenting training seminars including PowerUp, a 13 week training course, and various training seminars provided on the website;
- Mentoring;
- Promoting SBA programs and events;
- Making a donation to and paying expenses for a SBA Business Information Center (BIC);
- Entering into MOUs and cosponsorship agreements with SBA and other organizations; and
- Judging nominations for SBA awards.

According to SBA officials, other SBA District Advisory Councils also have engaged in non-advisory activities.

Under the current charter, SBA's District Advisory Councils are only allowed to engage in advisory functions. The 1992 and 1993 charters authorizing SBA's District Advisory Councils stated that its District Advisory Councils' duties are limited to being advisory. The 1999 charter states that "The Councils will provide advice and recommendations only." SBA had not filed the 1995 and 1997 charters with GSA and we could not locate these charters at SBA. FACA Sections 2 (b)(6) and 9(b), state "the function of advisory committees should be advisory only...and [u]nless otherwise specifically provided by statute or Presidential directive, advisory committees shall be utilized solely for advisory functions." OGC believes it is possible that Section 8(b)(13) of the Small Business Act may give SBA the authority to have District Advisory Councils engage in non-advisory functions if the charter is modified to include non-

advisory activities. This section of the Small Business Act states that the Administrator has the authority to “establish such advisory boards . . . as may be necessary to achieve the purposes of this Act.” OGC has not however, determined whether the Small Business Act actually does provide that authority.

The former Rhode Island District Director believed that the RI Council was permitted to raise funds and maintain a checking account based on the broadness of the language in the SOP. As such, he encouraged and allowed the RI Council to engage in these activities. He stated that he copied the example of other SBA District Advisory Councils that were engaging in similar activities, interpreting the SOP as permitting Advisory Councils to engage in such activities. The present District Director and District Counsel also stated that they followed the SOP, which cites non-advisory activities and did not know that the SOP was incorrect. The present District Director stated that the RI District Office was never sent a copy of the charter and therefore, was unaware that the Council was restricted to only providing advice. The “Goals” and “Functions” sections of the SOP provide for such non-advisory activities as:

- assisting the SBA in carrying out its role,
- promoting SBA programs,
- educating the public,
- speaking out for small business and SBA programs, and
- encouraging banks to participate in SBA programs and make more capital available.

Another section of the SOP is devoted to Small Business Week activities, and states “Advisory Council members shall participate in planning and executing Small Business Week activities in coordination with SBA offices.” The SOP, however, cannot override the advise only limitations imposed by the charter and possibly FACA.

The RI Council commercial checking account provided the RI District Office a source of non-appropriated funds to engage in activities that the District Office determined should be undertaken. The following chart, which was developed using the receipts and expenditures from the RI Council’s financial records maintained in “*Quicken Quick Books*,” shows the approximate amounts raised and expended by the RI Council for specific SBA events and projects.

<u>Event</u>	<u>Total Received by the Council</u>	<u>Total Paid by the Council</u>	<u>Difference</u>
Small Business Week	\$459,435	\$443,670	\$ 15,765
MED Week	\$ 57,741	\$ 30,431	\$ 27,310
Bridging the GAP	\$ 17,026	\$ 9,690	\$ 7,336
BIC Grand Opening	\$ 0	\$ 3,949	\$ (3,949)
Newport Conference	\$ 0	\$ 7,556	\$ (7,556)
Power Up	\$ 9,780	\$ 3,100	\$ 6,680
Women's Breakfast/Roundtable	\$ 0	\$ 2,084	\$ (2,084)
White House Conference	\$ 0	\$ 1,367	\$ (1,367)
Advisory Council Meetings	\$ 0	\$ 13,877	\$(13,877)
Y2K	\$ 0	\$ 868	\$ (868)
Technology (Website)	\$ 0	\$ 11,055	\$(11,055)
Totals	\$543,982	\$527,647	\$ 16,335

According to an official with GSA's Committee Management Secretariat, advisory councils' expenses should be paid out of the sponsoring agency's appropriations. Consequently, some or all of the RI Council's expenditures might have augmented SBA's budget. For example, the RI Council paid the expenses associated with its meetings rather than SBA. Since SBA has gift acceptance authority under the Small Business Act, the funds raised and expensed by the RI Council for SBA events and projects could be construed as gifts to SBA. Therefore, we recommend that the OGC determine whether the use of funds raised by SBA District Advisory Councils constitutes augmentation of SBA's appropriations, and, if augmentation has occurred, determine what corrective actions need to be taken.

Recommendations

We recommend that:

- A01: The Rhode Island District Director take necessary action to ensure that the RI Council ceases all non-advisory activities, unless and until the master charter is amended to allow such activities;
- A02: The Associate Administrator for Field Operations (AAFO) issue a Procedural Notice to all District Offices with District Advisory Councils explaining what activities these Councils can partake in and notifying them that these Councils must immediately cease all non-advisory activities unless and until the master charter is amended to allow these activities;
- A03: The General Counsel determine whether the use of funds raised by the Rhode Island Advisory Council and any other Advisory Councils identified by the AAFO constitutes impermissible augmentation of SBA's appropriations, and if impermissible augmentation has occurred, determine what corrective actions need to be taken;

- A04: The General Counsel determine the proper disposition of the funds remaining in the Rhode Island Advisory Council's checking accounts and of any such funds for other SBA Advisory Councils identified by the AAFO;
- A05: If impermissible augmentation has occurred, the Associate Administrator for Field Operations, in consultation with the Chief Financial Officer, ensure that appropriate corrective action is taken;
- A06: The Associate Administrator for Field Operations, in consultation with the Chief Financial Officer, ensure that the funds remaining in all District Advisory Council checking accounts be properly disposed of according to the General Counsel's determination;
- A07: The Chief Operating Officer issue a revised SOP for SBA Advisory Councils, which provides guidance to ensure compliance with FACA, SBA's District Advisory Council charter and 41 CFR Part 101-6.

SBA Management's Response

In its response, SBA management indicated that it issued an Information Notice informing all district offices and their advisory councils to cease and desist from all such non-advisory activity. Management also indicated that it is in the process of drafting a procedural notice and new Standard Operating Procedures that will address recommendations A02 and A07. Management did not specifically address the other recommendations in its response and intends to do so in its response to the final report.

In its response, SBA management also made the following observation:

not one small business was hurt by the actions of the RI Council, but in fact many small businesses across the Nation were assisted. Clearly the RI Council conducted itself consistently and honorably within what it believed were the dictates of the SOP . . .

Finding B: Improvements Needed in SBA Management and Oversight of District Advisory Councils.

SBA needs to improve its management and oversight of its District Advisory Councils. SBA currently does not have a CMO, the official responsible for controlling and supervising the establishment, procedures, and accomplishments of SBA's District Advisory Councils, though FACA Sec. 8(b) requires it. SBA did not:

- Question reported closed and partially closed meetings though such meetings cannot be held without obtaining the authorization from the Administrator;
- Ensure there were the required detailed minutes of advisory council meetings or certifications that the minutes of the meetings were correct;
- Post required notices of Council meetings in the Federal Register;
- Ensure maintenance of a required system of records covering past, present, and proposed members of SBA Advisory Councils;
- Ensure that required reports of Advisory Council recommendations and resolutions were prepared and distributed;
- Ensure that submitted annual reports on Council operations contained complete and correct information;
- Ensure that Council members did not exceed their limit of three two-year terms (total of 6 years) of service; and
- Send GSA required copies of the charters for years 1995 through 1998.

Better oversight of SBA Advisory Councils is needed to ensure that SBA and the Councils operate in compliance with FACA, applicable Federal regulations and the SOP.

Recommendation

B01: We recommend that the Administrator appoint a Committee Management Officer (CMO) with responsibility for controlling and supervising the establishment, procedures, and accomplishments of SBA's Advisory Councils to ensure that they comply with governing laws, regulations, and policies.

SBA Management's Response

In its response, management indicated that it has announced a position for a Committee Management Officer.



U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, DC 20416

APPENDIX A
Page 1 of 4

OFFICE OF FIELD OPERATIONS

DATE: September 29, 2000

TO: Robert G. Seabrooks
Assistant Inspector General for Auditing

FROM: Charles W. Payne *Charles W. Payne 9-29-00*
General Counsel

Robert J. Baskin *Robert J. Baskin 9/29/00*
Associate Administrator for Field Operations

RE: Draft Audit of Rhode Island District Advisory Council.

We appreciate the opportunity to respond to your draft Audit Report (Report) of the Rhode Island District Advisory Council (RI Council). We intend to provide a response to all recommendations made in the final audit report in accordance with your auditing standards. Given the short time frame imposed by your office to respond to the draft report, the following is an immediate response. In fact, over the last year, we have been in the process of improving the district advisory council program and eliminating the deficiencies noted in your Report. For example:

- Over four months ago SBA issued Information Notice, #7000-117 (5/15/00), informing all relevant field managers and counsel that district advisory councils may not solicit or raise funds on behalf of SBA, or organize or manage SBA events. Thus, the district offices and their advisory councils have already been instructed to cease and desist from all such non-advisory activity, unless notified otherwise.
- SBA is currently in the process of drafting a procedural notice that will provide field offices additional guidance concerning the restrictions on advisory council activity under the current charter. This is consistent with your recommendation #A02.
- The Agency has already drafted new Standard Operating Procedures (SOP). Once we have determined that the current draft is totally consistent with the findings of your Report, the Chief Operating Officer will issue it. This is consistent with your recommendation #A07.
- SBA has, in the past, had its Assistant Administrator for Advisory Councils (AAAC) serve as the Committee Management Officer (CMO), but a temporary vacancy in that position currently exists. Today, SBA announced the position for a Committee

Management Officer. This relates to your recommendation #B01.

We believe it is important to note in this audit report that SBA uses district and other Advisory Councils, as provided in the Small Business Act, as an integral component of its service to the Nation's 25 million small businesses. The context for their use in the Rhode Island District Office and elsewhere at SBA has always been to enhance and support the level of service to small business and not for any other reasons. Finally, the Agency believes that it is unlikely that any augmentation occurred by agrees to consider all the circumstances with care. It is important to note that the Office of General Counsel has not officially opined to date on this issue as requested by your office's recommendation #A03.

BACKGROUND

In January of 1992 the RI Council's membership was increased so its membership's profile represented 50% small business, 30% financial institutions, and 20% from business development organizations. Since 1992, hundreds of individuals have volunteered and served as members. They have all had a very positive and valuable effect on the Rhode Island business community, and we firmly believe that these tireless volunteers should be congratulated for their efforts on behalf of the small business community of Rhode Island and out nation's entrepreneurs.

In 1991 the Rhode Island District Office has the following dubious distinctions:

- Ranked 79 of 82 district offices, branch offices and post of duty stations for loan volume.
- The number of small business receiving a SBA loan guarantee was 1 business for every 553 small business in Rhode Island.
- The loan portfolio currency rate (number of loans paying on time) was the worst in the nation.
- Small Business Week celebration had fewer than 75 people in attendance.
- The district office's annual loan production was approximately 60 loans and roughly \$10 million per year.

In addition, the New England economy was in an economic recession. New England's financial institutions were closing because of capital shortfall. In Rhode Island this capital shortfall cause over 55 financial institutions to close. Financial institution in order to conserve capital stopped making new business loans and recalled existing loans, including business loans that had never missed a loan payment. Ins short the capital crunch of the New England region cascaded into a credit crunch for Rhode Island's small business, causing the unemployment rate to be one of the worst in the country.

In January of 1992, the newly appointed district director responded to the poor performance of the economy and the district office by developing a strategic plan which included using the RI Council as a center point for the economic recovery of Rhode Island's small business. The theme of the district director and the restructured Council was *"as long as Rhode Island small businesses were standing in line for access to credit, hardworking men and women of Rhode Island will be standing in line for jobs."*

The RI Council was an integral part of the “turn around” of the Rhode Island small business economy and the prosperity the state enjoys today. These volunteers gave of themselves to help their fellow small business owners grow and develop. In the context of this report we do not want their efforts on behalf of small business to become mired in the technical issues of the Agency’s Standard Operating Procedures.

We believe that it is clear that the RI Council acted and operated in good faith. In addition, the district office acted in good faith by providing advice on what was believed to be an accurate Standard Operating Procedures for a district advisory council. We are pleased that the report acknowledges in the summary *(i) “The SOP, however, contradicts SBA’s District Advisory Council Charter and possibly FACA regarding what Advisory Council can and cannot do in many instances.”* As stated by the former district director, he believed that he followed the SOP as it related to the RI Council and its activities.

We appreciate the reference in the report that the existing SOP states *“The Goals and Function section of the SOP provide for such non-advisory activities as”*

- 1.) *assisting the SBA in carrying out its role*
- 2.) *promoting SBA programs*
- 3.) *educating the public*
- 4.) *speaking out for small business and SBA programs, and*
- 5.) *encouraging banks to participate in SBA programs and make more capital available*

Another section of the SOP is devoted to Small Business Week activities and states “Advisory Council members shall participate in planning and executing Small Business Week activities in coordination with the SBA offices.” (Italic print direct from the report.)

With the combined efforts of the RI Council and the SBA District Office the following outcomes were achieved:

- SBA loans to small business are one SBA loan for every eight small businesses in Rhode Island, a market penetration that is one of the best in the Nation.
- SBA’s loan production is consistently over 500 loans per year and in excess of \$100 million annually.
- The currency rate for SBA’s portfolio in Rhode Island is 93%.
- Rhode Island Small Business Week’s celebrations have consistently been in excess of a 1000 people celebrating the achievements of small business and their contribution to the Rhode Island economy.
- The RI Council and the SBA district office advocated for a state tax credit for the SBA guarantee fee. The state law, which was enacted in 1994 and duplicated by other states, reduces the cost to small business for receiving a SBA guarantee loan.
- The RI Council support, consistent with the SOP, assisted the SBA district office in reaching out to the minority community, women, and new markets throughout the State of Rhode Island.

- The SBA district office is the only district office to reach and exceed the district goals every year since their establishment by the Agency in 1994.

It must be emphasized that not one small business was hurt by the actions of the RI Council, but in fact many small businesses across the Nation were assisted. Clearly the RI Council conducted itself consistently and honorably within what it believed were the dictates of the SOP, as acknowledged by the report. They did so in furtherance of the programs of SBA and in the best interest of the Rhode Island small business community. We firmly believe that the men and women who have served on the RI Council have done so with distinction and in so doing, unleashed the productive powers of small business in Rhode Island.

In order for the Agency to succeed in its efforts of reaching out to assist our vast and diverse small business constituency, we need individuals and organizations to provide leadership and assistance. Hopefully, the recommendations of this report and our responses will help to support the positive change in existing and future methodologies, in order that SBA is able to continue to lead and continue the growth and development of small business and the Nation's economy. We believe the Advisory Council provides a pivotal role in this effort, and the good work demonstrated in Rhode Island, as reflected above, is duplicated time and again across the country through other SBA offices.

Thank you for the opportunity to provide these important comments and we ask that this entire response be included in your final report.

AUDIT REPORT DISTRIBUTION

<u>Recipient</u>	<u>Number of Copies</u>
Deputy Administrator	1
Region I Administrator	1
Rhode Island District Advisory Council	1
Chief Financial Officer	1
(Attn.: Jeff Brown)	
General Counsel	2
General Accounting Office	2
Director of Committee Management Secretariat (GSA)	1