



U.S. Department of Agriculture  
Office of Inspector General  
Southwest Region  
Audit Report

RURAL DEVELOPMENT  
RURAL BUSINESS-COOPERATIVE  
SERVICE  
LENDER SERVICING OF BUSINESS  
AND INDUSTRY GUARANTEED LOANS  
COLUMBIA, SOUTH CAROLINA



Report No.  
34601-8-Te  
FEBRUARY 2002



UNITED STATES DEPARTMENT OF AGRICULTURE  
OFFICE OF INSPECTOR GENERAL  
Southwest Region  
101 South Main  
Temple, Texas 76501



DATE: February 19, 2002

REPLY TO  
ATTN OF: 34601-8-Te

SUBJECT: RBS B&I Guaranteed Loans – Rural Development State Office,  
Columbia, South Carolina

TO: Charles D. Sparks  
State Director  
Rural Development  
1835 Assembly Street, Room 1007  
Columbia, SC 29201

This report presents the results of our audit of lender servicing in the Rural Development Business and Industry (B&I) guaranteed loan program in South Carolina. The South Carolina Rural Development State Office's response to the draft report, dated December 31, 2001, is included in exhibit B with excerpts and the Office of Inspector General's (OIG) position incorporated into the relevant sections of the report.

Management decision has been reached for Recommendations Nos. 1 and 3. Follow your internal agency procedures in forwarding final action correspondence to the Office of the Chief Financial Officer/Planning and Accountability Division.

To reach management decision for Recommendation Nos. 2, 4, and 5, we need additional information as set forth in the Recommendation section of Finding Nos. 2, 3, and 4 in the report. Please furnish the information needed to reach agreement on the management decision for these recommendations within 60 days. Please note that Departmental Regulation 1720-1 requires a management decision for all recommendations within a maximum of 6 months from the date of report issuance, and final action to be taken within 1 year of each management decision.

We appreciate the courtesies and cooperation extended to us by members of your staff during the audit.

/s/ R. E. Gray  
ROBERT E. GRAY  
Regional Inspector General  
for Audit

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# EXECUTIVE SUMMARY

## RURAL DEVELOPMENT RURAL BUSINESS-COOPERATIVE SERVICE LENDER SERVICING OF BUSINESS AND INDUSTRY GUARANTEED LOANS COLUMBIA, SOUTH CAROLINA

AUDIT REPORT NO. 34601-8-Te

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### RESULTS IN BRIEF

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We performed a review in South Carolina as part of our nationwide audit of lender servicing of Business and Industry (B&I) guaranteed loans. The results of this audit may be included in a report to the Rural Business-Cooperative Service (RBS) National Office. Our objective was to determine if lenders were properly servicing B&I guaranteed loans.

The purpose of the B&I guaranteed loan program is to improve, develop, or finance business, industry, and employment and improve the economic climate in rural communities. B&I loans achieve this purpose by bolstering the existing private credit structure through the guarantee of quality loans. Loans are guaranteed through private lenders that are responsible for taking servicing actions that a prudent lender would perform in servicing its own portfolio of loans that are not guaranteed.

Of the six loans reviewed, we found that four lenders did not adequately service their B&I guaranteed loans to borrowers A, B, C, and D. For example, lenders did not: (1) follow the requirements listed in the conditional commitment for use of loan funds and for obtaining collateral appraisals, (2) comply with the Office of Management and Budget (OMB) Circular A-129 by processing and closing a loan when the borrower had delinquent Federal debt, and (3) obtain agency approval before making additional non-guaranteed loans to the borrower. In our opinion, this occurs in the B&I loan program because lenders are delegated complete responsibility for servicing actions with little or no oversight provided by the RBS State Office (SO). We found that the SO was unaware that these conditions had occurred.

Inadequate servicing by lenders increases the likelihood of a loss if the businesses of the borrowers are liquidated. One loan has been liquidated and three loans are in foreclosure, pending liquidation. The agency's risk of loss on the guarantees is over \$7.3 million on the four loans.

It should be noted that when we brought the delinquent Federal debt issue to the attention of the SO, the processing of another guaranteed loan for \$3.5 million was stopped because the applicant owed delinquent Federal employment taxes.

We did not find any material reportable conditions in our review of borrowers E and F.

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## **KEY RECOMMENDATIONS**

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In consultation with the Office of the General Counsel (OGC), we recommend reducing the loss claim of lender A, and rescinding the loan note guarantee to lenders B, C, and D. Recommendations to improve the oversight by all agency SOs of lenders' servicing actions will be made to RBS in a nationwide audit report.

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## **AGENCY RESPONSE**

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In a letter dated December 31, 2001, the SO informed us that the agency terminated lender A's loan note guarantee on November 2, 2001, and did not pay the report of loss. The agency plans to seek OGC's advice about rescinding the loan note guarantees to lenders B, C, and D. (See exhibit B.)

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## **OIG POSITION**

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We agree with the management decision for the recommendation regarding lender A. To reach management decision on the recommendations for lenders B, C, and D, we need documentation showing that the agency has submitted the facts for lenders B, C, and D to OGC to obtain advice on rescinding the loan note guarantees.

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# INTRODUCTION

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## BACKGROUND

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The RBS is an agency of the U.S. Department of Agriculture's Rural Development mission area. The mission of RBS is to enhance the quality of life for all rural residents by assisting new and existing businesses and cooperatives through partnerships with rural communities. RBS accomplishes this, in part, through the B&I guaranteed loan program administered by the SOs.

The purpose of the B&I guaranteed loan program is to improve, develop, or finance business, industry, and employment and improve the economic and environmental climate in rural communities with a population of less than 50,000. B&I guaranteed loans achieve this purpose by bolstering the existing private credit structure through the guarantee of quality loans, which provide lasting community benefits. It is not intended to use the guarantee authority for marginal or substandard loans or for the relief of lenders having such loans.

Generally, the total amount of agency loans to one borrower cannot exceed \$10 million. This limit includes the guaranteed and unguaranteed portions, the outstanding principal, and the interest balance for any new loan requests. The Administrator, with the concurrence of the Under Secretary for Rural Development, may grant an exception to the \$10 million limit under certain circumstances. Total guaranteed loans to one borrower may not exceed \$25 million under any circumstances. Generally, the maximum guaranteed percentages are 80 percent for loans of \$5 million or less, 70 percent for loans between \$5 million and \$10 million, and 60 percent for loans exceeding \$10 million.

The lender is responsible for servicing the entire loan and for taking all servicing actions that a prudent lender would perform in servicing its own portfolio of loans that are not guaranteed. The loan note guarantee is unenforceable by the lender to the extent any loss is occasioned by violation of usury laws, use of loan funds for unauthorized purposes, negligent servicing, or failure to obtain the required security interest regardless of the time at which the agency acquires knowledge of the foregoing. This responsibility includes, but is not limited to, the collection of payments, obtaining compliance with the covenants and provisions in the loan agreement, obtaining and analyzing financial statements, checking on payments of taxes and insurance premiums, and maintaining liens on collateral.

As of December 31, 2000, South Carolina had 74 borrowers with 91 loans totaling \$108.5 million, including 11 borrowers with 17 loans totaling \$20.1 million classified as delinquent. Of these 11 borrowers, 7 were more than 30 days delinquent and 4 were in liquidation.

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**OBJECTIVE**

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The audit objective was to determine whether lenders were properly servicing B&I guaranteed loans.

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**SCOPE**

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We performed this audit as part of a nationwide review of the B&I guaranteed loan program. South Carolina was selected based on the number of loans outstanding and the total dollar value of those loans, the total delinquent amount, and total loss payments made by the agency to honor its guarantees. We conducted the fieldwork from January to June 2001 at the SO in Columbia, South Carolina. We conducted interviews, reviewed loan files, and conducted collateral inspections in Elloree, Spartanburg, Rock Hill, and Columbia, South Carolina. Coverage included B&I guaranteed loan activity during fiscal years 1998, 1999, and 2000.

Since January 1, 1990, the SO has issued 96 loan note guarantees with lending institutions totaling over \$125 million, a segment of the 3,150 loans totaling over \$4.1 billion made nationally by the agency. As of October 17, 2000, the South Carolina B&I guaranteed loan portfolio had 60 loans totaling \$87.9 million on loans made since January 1, 1990, a segment of the 2,420 loans totaling over \$3.2 billion nationally. From this universe, we judgmentally selected for review six loans that totaled \$1 million or more with emphasis on delinquent loans. These loans totaled \$14.9 million.

The audit was conducted in accordance with Generally Accepted Government Auditing Standards.

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## **METHODOLOGY**

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To accomplish the objective of the audit, we performed the following procedures:

At the SO, we: (1) interviewed State office personnel to determine the policies and procedures for approving and servicing B&I guaranteed loans, (2) obtained and reviewed borrower loan files, and (3) selected the lenders and borrowers to be reviewed for this audit.

At the lenders' offices, we: (1) interviewed lender personnel to determine their understanding of the loan program and their responsibilities for servicing their B&I loans, (2) reviewed the lending policy as it relates to collateral and use of loan proceeds, and (3) reviewed the borrowers' loan files to ensure compliance with guaranteed conditions.

We visited sites in Ellore and Rock Hill, South Carolina and interviewed the borrowers to verify the existence of collateral pledged to secure the loan and to determine if the borrower had any concerns regarding the servicing of the loan.



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## FINDINGS AND RECOMMENDATIONS

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|                  |   |
|------------------|---|
| <b>CHAPTER 1</b> | <b>LENDERS DID NOT COMPLY WITH RURAL DEVELOPMENT INSTRUCTIONS FOR MAKING AND SERVICING B&amp;I GUARANTEED LOANS</b> |
|------------------|---|

Of the six loans reviewed, we found that four lenders did not adequately service their B&I guaranteed loans to borrowers A, B, C, and D. This occurred because lenders did not: (1) follow the requirements listed in Rural Development Form 4279-3 (Conditional Commitment) for use of loan funds and obtaining appraisals, (2) comply with OMB Circular A-129 by processing and closing a loan when the borrower had delinquent Federal debt, and (3) obtain agency approval before making additional non-guaranteed loans to the borrower. In our opinion, this occurs in the B&I loan program because lenders are delegated complete responsibility for servicing actions with little or no oversight provided by the SO. We found that the SO was unaware that these conditions had occurred.

Inadequate servicing by lenders increases the likelihood of a loss if the businesses of the borrowers are liquidated. One loan has been liquidated and two loans are in foreclosure, pending liquidation. Of the loans reviewed, one lender has filed a report of loss to the agency, three loans are in default, and the agency's risk of loss on the guarantees is over \$7.3 million on four loans.

It should be noted that when we brought the delinquent Federal debt issue to the attention of the SO, the processing of another guaranteed loan for \$3.5 million was stopped because the applicant owed delinquent Federal employment taxes.

Rural Development instructions state that the lender is responsible for servicing the entire loan and for taking all servicing actions that a prudent lender would perform in servicing its own portfolio of loans that are not guaranteed.<sup>1</sup> Additionally, the instructions state that it is the responsibility of the lender to ascertain that all requirements for making, securing, servicing, and collecting the loan are complied with.<sup>2</sup>

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<sup>1</sup> Rural Development Instruction 4287, subpart B, §4287.107, dated December 23, 1996.

<sup>2</sup> Rural Development Instruction 4279, subpart A, §4279.1(b), dated December 23, 1996.

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**FINDING NO. 1 – LOAN FUNDS  
DISBURSED FOR  
UNAUTHORIZED PURPOSES**

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Lender A did not adequately service its B&I guaranteed loan to borrower A because the lender disbursed loan proceeds for unauthorized purposes. In the B&I guaranteed loan program, conditions like these occur because guaranteed lenders are

delegated complete responsibility for servicing actions with little or no oversight provided by RBS. The SO was unaware of this deficiency. As a result, the agency is at risk for a loss on the loan. Subsequently, lender A liquidated the loan and submitted a report of loss to the agency for \$233,018. The agency has requested that OGC review the report of loss.

Rural Development instruction states that the lender must certify that the loan proceeds have been or will be disbursed for purposes and in amounts consistent with the conditional commitment.<sup>3</sup> The lender certified on April 15, 1998, that all conditions and requirements as outlined in the conditional commitment had been complied with.

Rural Development instruction states that the loan note guarantee is unenforceable by the lender to the extent any loss is occasioned by violation of usury laws, use of loan funds for unauthorized purposes \* \* \* <sup>4</sup>

Borrower A received a B&I guarantee for a \$2,076,000 loan on April 14, 1998. The agency guaranteed 80 percent of the loan, or \$1,660,800. The borrower projected that the business would create 45 new jobs. However, the project was never constructed due to delays in obtaining the right-of-way from the Department of Transportation and subsequent financial problems. The lender disbursed only \$1,015,288 of the total loan amount to the borrower.

On April 15, 1998, the lender disbursed part of the loan funds (\$468,950) to pay off an existing unguaranteed debt of the borrower with the lender. Rural Development's conditional commitment for this loan did not allow for the loan funds to be used for debt refinancing. The conditional commitment required that the loan funds would be used for: (1) \$228,000 for business working capital, (2) \$1,350,000 to purchase real estate, and (3) \$498,000 to purchase machinery and equipment. The State office was unaware of this deficiency.

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<sup>3</sup> Rural Development Instruction 4279, subpart B, § 4279.181(l), dated December 23, 1996.

<sup>4</sup> Rural Development Instruction 4287, subpart B, § 4287.107, dated December 23, 1996.

The lender requested that the agency approve a report of loss even though the lender did not comply with the conditional commitment. The agency has requested that the OGC review the report of loss and issue an opinion.

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**RECOMMENDATION NO. 1**

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In consultation with OGC, take action to not allow the loss claim of \$233,018.17.

**Rural Development Response**

In a letter dated December 31, 2001, the SO informed us that OGC concurred with the agency's recommendation not to pay the report of loss and terminate the loan note guarantee. The report of loss was not paid and lender A was notified on November 2, 2001, that the loan note guarantee was terminated.

**OIG Position**

We agree with the management decision.

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**FINDING NO. 2 – LOAN  
APPROVED WHEN  
BORROWER HAD  
DELINQUENT FEDERAL DEBT**

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On March 1, 1999, RBS guaranteed a \$2.8 million loan from lender B to borrower B even though the borrower had an outstanding Federal debt of \$334,592 owed to the Internal Revenue Service (IRS) for delinquent employment taxes. This occurred because the lender was apparently unaware of the

requirement that loans are not to be granted under these circumstances and the Rural Development SO was unaware of the outstanding Federal debt. Additionally, the lender closed the loan knowing that the borrower had these serious financial problems.

OMB Circular A-129 states that processing of applications should be suspended when applicants are delinquent on Federal tax or non-tax debts. Processing may continue only when the debtor satisfactorily resolves the debt (e.g., pays in full or negotiates a new repayment plan).<sup>5</sup> The borrower was delinquent for 6 quarters when the loan closed, indicating that the borrower had serious cash flow problems and was unable to pay its taxes.

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<sup>5</sup> OMB Circular No. A-129, III. A. 1.b., dated January 11, 1993.

Rural Development instruction states that the lender must analyze all credit factors associated with each proposed loan and apply its professional judgment to determine that the credit facts, considered in combination, ensure loan repayment.<sup>6</sup>

Borrower B received a \$2.8 million B&I guaranteed loan on March 1, 1999, for debt restructure and working capital to enable the company to increase its production to support its debt service. The agency guaranteed 80 percent of the loan, or \$2,240,000.

The borrower projected that the business would save 55 jobs. The company currently has less than five employees. The borrower is delinquent on the guaranteed loan and the lender is foreclosing. The borrower defaulted on the loan 7 months after loan closing.

Prior to loan closing, lender B was aware that the borrower owed over \$334,000 to the IRS for delinquent employment taxes. The lender noted on the loan closing statement that the loan proceeds could not be used to pay the delinquent debt to the IRS. Additionally, the lender noted that a repayment schedule would be obtained from the IRS.

| <b>Delinquent Employment Taxes<br/>Owed to the IRS</b> |                               |                              |
|--|-------------------------------|------------------------------|
| <b>IRS Form</b>  | <b>Tax Period<sup>7</sup></b> | <b>Unpaid Balance of Tax</b> |
| 941  | 09-30-97                      | \$33,216.32                  |
| 941  | 12-31-97                      | 59,732.70                    |
| 941  | 03-31-98                      | 54,448.12                    |
| 941  | 06-30-98                      | 60,061.94                    |
| 941  | 09-30-98                      | 76,105.57                    |
| 941  | 12-31-98                      | 46,832.21                    |
| 940  | 12-31-98                      | 4,196.02                     |
| <b>Total</b>   |                               | <b>\$334,592.88</b>          |

When the Federal debt issue was brought to the attention of the SO, the SO stopped the processing of another guaranteed loan for \$3.5 million after learning that the applicant owed the IRS delinquent Federal employment taxes. After notifying the lender of the OMB Circular A-129 rule, the lender withdrew its application in September 2001, stopping the loan process.

<sup>6</sup> Rural Development Instruction 4279, subpart A, section 4279.30(b), dated December 23, 1996.

<sup>7</sup> Returns are due by the last day of the month following the end of quarter. 26 CFR, Part 31, section 31.6071(a)-1.

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**RECOMMENDATION NO. 2**

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Consult with OGC to determine if this \$2.24 million loan note guarantee should be rescinded because an ineligible borrower was granted a B&I guaranteed loan.

**Rural Development Response**

In a letter dated December 31, 2001, the SO informed us that lender B was notified on November 21, 2001, that the loan note guarantee might be terminated. Additionally, the agency will seek OGC's advice by January 25, 2002, about rescinding the loan note guarantee to lender B.

**OIG Position**

To reach management decision, we need documentation showing that the agency has submitted the facts for lender B to obtain OGC's advice on rescinding the loan note guarantee.

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**RECOMMENDATION NO. 3**

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Provide documentation that the agency did not guarantee a loan to applicant A.

**Rural Development Response**

In a letter dated December 31, 2001, the SO informed us that the agency could not determine eligibility of the lender's request until numerous issues were addressed, including delinquent Federal debt. The lender did not respond and the agency considered the request withdrawn.

**OIG Position**

We agree with the management decision.

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**FINDING NO. 3 – APPRAISAL  
ON COLLATERAL NOT  
OBTAINED**

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Lender C did not adequately service the RBS guaranteed loan to borrower C because it did not obtain an appraisal of the inventory and equipment as required by Rural Development's conditional commitment for guarantee. Instead, the lender used compiled

financial statements to evaluate the inventory and a "desktop" survey<sup>8</sup> to evaluate the equipment. In our opinion conditions like these occur

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<sup>8</sup> A Desktop Opinion of Value (Desktop Survey) is not an appraisal. It is the appraiser's best estimate based on materials or information supplied and evaluated, without benefit of an actual on-site observation, according to the appraiser's letter to lender C dated March 12, 1999.

because lenders are delegated all servicing responsibilities with little or no oversight provided by the SOs. The SO was unaware of this deficiency. As a result, without a proper appraisal of the collateral securing the B&I loan, the agency's risk of loss is increased should liquidation of the loan occur.

Rural Development Instruction 4279, subpart B, section 4279.173(a),(b), dated December 23, 1996, states that, upon approval of a loan guarantee, the agency will issue a conditional commitment to the lender containing conditions under which a loan note guarantee will be issued.

On April 29, 1999, Rural Development issued the Conditional Commitment for Guarantee, Form 4279-3, to lender C detailing the conditions for the guarantee, including the responsibility that the lender obtain an independent appraisal of the borrower's real estate, inventory, equipment, furniture, and fixtures. On November 4, 1999, lender C certified that all conditions had been met and, on the same date, the borrower received a \$1.1 million Rural Development guaranteed loan. Rural Development guaranteed 80 percent of the loan, or \$880,000.

We found that the lender obtained an appraisal on the real estate, valued at \$250,000, but not on the inventory and equipment, which had a book value of over \$1.8 million. The lender used compiled financial statements<sup>9</sup> prepared by the borrower's accountant to value the inventory and a "desktop" survey to evaluate the equipment. The lender did not propose to Rural Development any alternative conditions to the requirement of obtaining an independent appraisal of all collateral securing the B&I loan. The State office was unaware of this deficiency.

Borrower C is currently delinquent on this guaranteed B&I loan.

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**RECOMMENDATION NO. 4**

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In consultation with OGC, determine if the loan note guaranteed to lender C should be rescinded because the lender did not properly service the guaranteed loan.

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<sup>9</sup> Statement of Standards for Accounting and Review Services (SSARS) No. 1, issued in December 1978, defines a compilation of financial statements as, presenting in the form of financial statements, information that is the representation of management (owners) without undertaking to express any assurance on the statements.

## Rural Development Response

In a letter dated December 31, 2001, the SO informed us that lender C was notified on November 21, 2001, that the loan note guarantee might be terminated. Additionally, the agency will seek OGC's advice by January 25, 2002, about rescinding the loan note guarantee to lender C.

## OIG Position

To reach management decision, we need documentation showing that the agency has submitted the facts for lender C to obtain OGC's advice on rescinding the loan note guarantee.

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### **FINDING NO. 4 – UNAUTHORIZED LOANS TO BORROWER**

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Lender D did not adequately service its guaranteed B&I loan by making unauthorized non-guaranteed loans to borrower D without first obtaining agency approval. This occurred because the B&I program delegates all servicing actions to the lenders and provides

for little or no oversight by the SO. The SO was unaware that these loans had been made. In addition, the lender did not obtain financial statements from borrower D to submit them to the SO as required by program regulations. As a result, the ability of the borrower to repay the guaranteed loan could be weakened and, in the event of a liquidation of the business, the risk of loss on the guarantee is increased.

Rural Development instructions state that the lender will not make additional loans to the borrower without first obtaining the prior written approval of the agency, even though such loans will not be guaranteed.<sup>10</sup>

The instructions state that, at a minimum, annual financial statements prepared by an accountant in accordance with the Generally Accepted Accounting Principles will be required.<sup>11</sup> Additionally, the lender must submit annual financial statements to the agency within 120 days of the end of the borrower's fiscal year.<sup>12</sup>

Borrower D received two guaranteed B&I loans on September 25, 1998, one for \$2.28 million and one for \$2.72 million. The agency guaranteed 80 percent of the loans, or \$4 million. The purpose of the loans was to start a business and create 300 jobs.

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<sup>10</sup> Rural Development Instruction 4287, subpart B, §4287.107(e), dated December 23, 1996.

<sup>11</sup> Rural Development Instruction 4279, subpart B, §4279.137(a), dated December 23, 1996.

<sup>12</sup> Rural Development Instruction 4287, subpart B, §4287.107(d), dated December 23, 1996.

Unbeknownst to the SO, on December 9, 1999, the lender made a non-guaranteed loan to the borrower for \$600,000. Again on January 31 and August 31, 2000, the lender made non-guaranteed loans totaling \$160,000 to the borrower. A representative of the lender informed us that they were unaware of this requirement, although we determined that the lender had received copies of the program instructions.

We also determined that the lender did not obtain financial statements for the borrower for 1998 and 1999 and was, therefore, unable to provide them to the agency for review as required by program regulations.

Providing additional loans to the borrower without allowing the agency to review and approve the loans, and not obtaining financial statements for the agency to review, limits even further the ability of the agency to provide oversight of the program and could increase the risk of loss on the B&I loan should liquidation of the business occur. At the time of our audit, the borrower was delinquent on its loan payments and there were less than five employees working at the business.

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**RECOMMENDATION NO. 5**

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In consultation with OGC, determine if the loan note guarantee to lender D should be rescinded because the lender did not properly service the guaranteed loan.

**Rural Development Response**

In a letter dated December 31, 2001, the SO informed us that lender D was notified on November 20, 2001, that the loan note guarantee might be terminated. Additionally, the agency will seek OGC's advice by January 25, 2002, about rescinding the loan note guarantee to lender D.

**OIG Position**

To reach management decision, we need documentation showing that the agency has submitted the facts for lender D to obtain OGC's advice on rescinding the loan note guarantee.



## EXHIBIT A – SUMMARY OF MONETARY RESULTS

| FINDING NUMBER | RECOMMENDATION NUMBER | DESCRIPTION   | AMOUNT <sup>13</sup>   | CATEGORY                                   |
|----------------|-----------------------|---|------------------------|--|
| 1              | 1                     | Lender did not comply with conditional commitment and did not account for collateral during liquidation | \$233,018.17           | Questioned<br>Loan-Recovery<br>Recommended |
| 2              | 2                     | Lender approved loan when borrower had delinquent Federal debt  | \$2,240,000.00         | Questioned<br>Loan-Recovery<br>Recommended |
| 2              | 3                     | Lender approved loan when borrower had delinquent Federal debt  | \$3,519,375.00         | FTBPTBU <u>1/</u>                          |
| 3              | 4                     | Lender did not comply with conditional commitment and obtain appraisal on collateral                    | \$ 880,000.00          | Questioned<br>Loan-Recovery<br>Recommended |
| 4              | 5                     | Lender made unauthorized loans to borrower  | \$4,000,000.00         | Questioned<br>Loan-Recovery<br>Recommended |
|                | <b>Total</b>          |   | <b>\$10,872,393.17</b> |  |

1/ Funds To Be Put To Better Use

<sup>13</sup> The amounts represent the agency's guaranteed portion.

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## EXHIBIT B – RURAL DEVELOPMENT’S RESPONSE TO DRAFT REPORT



United States  
Department of  
Agriculture

Rural Development  
Strom Thurmond Federal Bldg.  
1835 Assembly Street, Rm 1007  
Columbia, South Carolina 29201

(803) 253-3645  
(803) 765-5910 FAX

December 31, 2001

**SUBJECT:** RBS B&I Guaranteed Loans-Rural Development State Office  
Columbia, South Carolina

**TO:** USDA Office of Inspector General  
Southwest Region

We are responding to the official draft report of subject audit. We will respond to each audit finding. Also, we will provide comments regarding the monetary amounts in Exhibit A of your report.

**Key Recommendation:** In consultation with the Office of General Counsel (OGC), we recommend reducing the loss claim of lender A; and consider rescinding the loan note guarantees to lenders B, C, and D.

Rural Development State

**Office Response:** Lender A's Loan Note Guarantee was terminated on 11-2-01 and The Report of Loss was not paid. We plan to seek OGC's advice by 1-25-02 on rescinding the Loan Note Guarantees to lenders B, C, and D.

**Recommendation No. 1:** In consultation with OGC, take action to not allow the loss claim of \$233,018.17.

Rural Development State

**Office Response:** On 10-30-01 OGC concurred with our recommendation not to pay the Report of Loss and terminate the Loan Note Guarantee. Copy of their concurrence is attached. The Report of Loss was not paid and lender A was notified on 11-2-01 that the Loan Note Guarantee was terminated. Copy of letter is attached.

**Recommendation No 2:** In consultation with OGC, consider rescinding the \$2,240,000 loan note guarantee of the lender.

USDA Rural Development is an Equal Opportunity Lender, Provider, and Employer.  
Complaints of discrimination should be sent to: USDA, Director,  
Office of Civil Rights, Washington, D.C. 20250-9410

**Rural Development State**

**Office Response:** Lender B was notified on 11-21-01 that Loan Note Guarantee may be terminated. Copy of letter to lender B is attached. OGC's advice to be requested by 1-25-02.

**Recommendation No. 3:** Provide documentation that the agency did not guarantee a loan to applicant A.

**Rural Development State**

**Office Response:** Lender was notified on 7-12-01 that we could not determine eligibility of their request until numerous issues were addressed, among them was the delinquent Federal debt. Lender has not responded and we consider the request withdrawn. Copy of letter to lender is attached.

**Recommendation No. 4:** In consultation with OGC, consider rescinding the \$880,000 loan note guarantee of the lender.

**Rural Development State**

**Office Response:** Lender C was notified on 11-21-01 that Loan Note Guarantee may be terminated. Copy of letter to lender is attached. OGC's advice to be requested by 1-25-02.

**Recommendation No 5:** In consultation with OGC, rescind the \$4,000,000 loan note guarantee.

**Rural Development State**

**Office Response:** Lender D was notified on 11-20-01 that Loan Note Guarantee may be terminated. Copy of letter to lender is attached. OGC's advice to be requested by 1-25-02.

In regards to Exhibit A-Summary of Monetary Results, our response is that the \$233,018.17 that was not paid to Lender A, even though a Report of Loss claim had been filed, is a direct savings to the Government. The guaranteed loan amounts listed are the maximum amounts of the Rural Development guarantee. It is unknown as to how much, if any, loss claims will be requested if the guarantees remain in affect. The \$3,519,375 guaranteed loan application had numerous issues, in addition to the delinquent Federal debt, to overcome before eligibility could be determined.

If you need additional information or have any questions, please contact this office.

  
**CHARLES D. SPARKS**  
State Director

**Attachments**

