



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

RURAL DEVELOPMENT  
FISCAL YEAR 2001  
FINANCIAL STATEMENTS  
CALIFORNIA STATE OFFICE



Report No.  
85401-1-SF  
February 2002



UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Western Region – Audit

75 Hawthorne Street, Suite 200

San Francisco, CA 94105

TEL: 415-744-2851 FAX: 415-744-2871



DATE: February 28, 2002

REPLY TO

ATTN OF: 85401-1-SF

SUBJECT: Rural Development - FY 2001 Financial Statements  
California State Office

TO: Paul Venosdel  
State Director  
California State Office  
Rural Development

This report presents the results of our audit of Rural Development's fiscal year 2001 Financial Statements in the State of California. Your written response to the draft report is included as exhibit C to the report.

We have accepted your management decision on all recommendations in the report. The Office of the Chief Financial Officer (OCFO), U.S. Department of Agriculture, has responsibility for monitoring and tracking final action on the findings and recommendations. Please note that final action on the findings and recommendations should be completed within 1 year to preclude listing in the Semiannual Report to Congress. Follow your agency's internal procedures for forwarding final action correspondence to OCFO.

We appreciate the cooperation and assistance provided by your staff during the audit.

/s/

SAM W. CURRIE

Regional Inspector General  
for Audit

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**EXECUTIVE SUMMARY**

**RURAL DEVELOPMENT  
FISCAL YEAR 2001  
FINANCIAL STATEMENTS  
CALIFORNIA STATE OFFICE**

**AUDIT NO. 85401-1-SF**

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**RESULTS IN BRIEF**

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This report presents the results of our fiscal year (FY) 2001 audit of Rural Development's financial statements at the California State office. This audit was performed as part of our nationwide audit of Rural Development's FY 2001 Financial Statements. The objectives of our audit were to determine if Rural Development's system of internal control provides reasonable assurance that control objectives were met, and whether Rural Development has complied with laws and regulations for transactions and events that may have a material effect on its financial statements. We concluded that Rural Development's system of internal control generally provided reasonable assurance that control objectives were met, and that Rural Development had generally complied with laws and regulations for transactions and events that may have a material effect on its financial statements. However, we noted the following exceptions.

We found that the State office had made a community facility loan to an ineligible applicant. The applicant, a town government, was ineligible for the loan because the town's population exceeded allowable limits.

We also found that the four area offices we reviewed had not taken all required steps to facilitate the refinancing of single-family housing loans. Rural Development procedures require borrowers whose circumstances allow them to refinance their loans to do so. To accomplish this, area offices are required to determine if certain borrowers are able to refinance their loans. One of the four area offices had not initiated this process. At the other three area offices, we selected a total of nine borrowers and found that the offices had not timely carried out all required actions for seven of the nine borrowers.

One area office did not maintain an adequate separation of duties relating to collection of single-family housing loan payments. Regulations require

that collection duties (controlling the data and controlling the payment) be handled by separate employees.

The Local Agency Program Coordinator had not validated purchase card transactions selected by the Purchase Card Management System for validation, as required by Rural Development procedures.

For two of the five community facility loans we reviewed, Rural Development did not document that the borrower was unable to obtain financing elsewhere, as required by agency procedures.

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## **KEY RECOMMENDATIONS**

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We are recommending that the California State office

- Collect or otherwise service the unauthorized community facility loan provided to the ineligible applicant in accordance with applicable procedures,
- Ensure that area offices comply with requirements relating to the refinancing of single-family housing loans and separation of collection duties,
- Require the Local Agency Program Coordinator to validate purchase card transactions identified by the Purchase Card Management System, and
- Ensure that determinations regarding community facility borrowers' ability to obtain other financing are documented as required.

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## **AGENCY RESPONSE**

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In its February 15, 2002, written response, Rural Development concurred with the report's recommendations. The response is included in its entirety as exhibit C to this report.

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## **OIG POSITION**

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Based on its response, we have accepted Rural Development's management decision on all recommendations.

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## INTRODUCTION

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### BACKGROUND

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The mission of Rural Development is to help rural Americans improve the quality of their lives. To do this, Rural Development provides loans and grants and extends loan guarantees for housing, community development, and electric and telecommunication programs. The Rural Development mission area consists of three program agencies, the Rural Housing Service, the Rural Utilities Service, and the Rural Business-Cooperative Service.

The loan programs are delivered through each agency's national office and Rural Development State and field offices. In California, the programs are administered through the State office and 25 area offices. Rural Development State offices provide guidance and oversight of field office activities and administer program activities.

The management of the three Rural Development agencies is responsible for establishing internal controls and for ensuring compliance with laws and regulations applicable to its programs. During the course of our review, we tested compliance with a number of these laws and regulations.

Nationwide, Rural Development has an outstanding loan portfolio of \$82.4 billion. In California, Rural Development's loan portfolio consisted of 23,322 single-family housing borrowers with outstanding balances of over \$967 million; 500 multi-family housing borrowers with outstanding balances of over \$661 million; 2,023 single-family housing borrowers with loan guarantees of over \$264 million; 147 guaranteed business and industry loan borrowers with balances of over \$222 million; 76 community facilities borrowers with balances of over \$52 million; and 238 water and waste loan borrowers with balances of over \$244 million.

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### OBJECTIVES

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Our overall audit objectives were to determine if Rural Development's system of internal controls provided reasonable assurance that control objectives were met, and that it complied with laws and regulations for transactions and events that might have a material effect on its financial statements.

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## SCOPE

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We performed audit work at the California State office and at the Bakersfield, Merced, Oroville, and Visalia area offices. At each area office, we reviewed controls over borrower eligibility determinations and loan approval functions for the direct single-family housing, community programs, water and waste, business and industry, and multi-family housing loan programs. At the State office, we reviewed similar controls over the guaranteed single-family housing loan program. Our universe consisted of loans closed in fiscal year 2001 at the offices visited. Not all offices had closed all types of loans during the year; see exhibit B for details of the number and types of loans reviewed at each office visited.

At the four area offices visited, we reviewed the following loans closed in FY 2001;

- 20 of 71 direct single-family housing loans (totaling \$1,490,646 of \$4,653,063),
- all six guaranteed business and industry loans (totaling \$13,394,800),
- all three direct multi-family housing loans (totaling \$780,000),
- all six water and waste loans (totaling \$4,660,705), and
- all five community facility loans (totaling \$2,911,020).

At the State office, we reviewed 5 of 37 guaranteed single-family housing loans closed in FY 2001 (totaling \$754,150 of \$3,917,383).

We selected additional transactions for review (loans, grants, collections, and purchases) to evaluate Rural Development's internal controls over the use of government purchase cards, refinancing of direct single-family borrowers with outside credit, collection of loan payments and fees, and disbursements of grant funds. We also reviewed internal controls over accounting for personal property and computer security. We performed fieldwork in July and August 2001.

We conducted this audit in accordance with generally accepted government auditing standards.



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To accomplish the audit objectives we:

## **METHODOLOGY**

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- Reviewed applicable regulations;
- Examined case files and case file documents;
- Reviewed online history screens from Rural Development's accounting systems;
- Conducted interviews with applicable Rural Development personnel at the offices visited;
- Confirmed disbursements with grant recipients; and
- Performed a physical inventory of accountable property at the offices visited.

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## FINDINGS AND RECOMMENDATIONS

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<b>CHAPTER 1</b>	<b>CALIFORNIA STATE OFFICE MADE LOAN TO INELIGIBLE APPLICANT</b>
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### FINDING NO. 1

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The California State office provided a community facility (CF) loan to a recipient that was not eligible to receive the loan. According to State office officials, the error occurred because they inadvertently did not consider all the eligibility requirements. As a result, funds were unavailable to fund other projects which may have been proposed by eligible applicants.

Under its CF loan program, Rural Development provides loans to governmental entities and nonprofit organizations to develop community facilities essential to the quality of life in rural areas. Community facilities typically include amenities such as schools, health care clinics, and fire stations, but can also include fire and rescue vehicles.

On February 15, 2001, the State office closed a \$264,000 CF loan to the Town of Paradise, California, to purchase a fire truck. The loan had been obligated on April 4, 2000. According to the town's loan application, the fire truck was to be used in rural areas surrounding the town, which the town was responsible for serving through mutual aid agreements.

Regulations require that facilities funded under the CF loan program be located in and primarily serve rural areas.<sup>1</sup> Rural Development obtained information to establish that the outlying areas to be served by the fire truck met the definition of rural area and, based on this information, determined the requirement to have been satisfied.

However, regulations also require that

Loans for essential community facilities will not be made to a city or town with a population in excess of 20,000 inhabitants, according to the latest decennial Census of the United States.<sup>2</sup>

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<sup>1</sup> RD Instruction 1942.17, paragraphs (b)(2)(i) and (ii), dated February 6, 1985.

<sup>2</sup> RD Instruction 1942-A, paragraph 1942.17 (b)(1)(i)(B), dated February 6, 1985.

This requirement was not satisfied because the town's population of 25,524 (per the 1990 census) exceeded 20,000.

Rural Development officials at both the State and National offices agreed that the Town of Paradise was an ineligible applicant. The State office's Business and Cooperative Program Director (who oversaw CF loans at the time this loan was processed) concurred that the town was not eligible, and attributed the error to oversight. He stated he was unaware of the town having a population over 20,000, and also stated that he and his staff had been more focused on the fact that the facility was serving a rural population.

By regulation, a loan to an ineligible recipient is considered unauthorized assistance. RD Instruction 1951-O defines unauthorized assistance as

any loan ... received by a recipient ... for which the recipient was not eligible.<sup>3</sup>

The instruction further states that

When unauthorized assistance has been received, an effort must be made to collect from the recipient the sum which is determined to be unauthorized ...<sup>4</sup>

However, the instruction also includes provisions allowing continuation of the loan in lieu of collection if certain conditions are met.

Because the loan recipient was not eligible for the loan, we are recommending that the loan be collected or otherwise serviced in accordance with the regulation.

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## **RECOMMENDATION NO. 1**

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Collect or otherwise service the unauthorized loan to the Town of Paradise in accordance with the provisions of RD Instruction 1951-O.

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<sup>3</sup> RD Instruction 1951-O, paragraph 1951.702 (i), dated May 2, 1985.

<sup>4</sup> RD Instruction 1951-O, paragraph 1951.703 and 1951., paragraph dated May 2, 1985.

### **Rural Development Response**

In its written response dated February 15, 2002, Rural Development stated

We concur with the recommendation. Within 30 days Rural Development State Office staff will meet with the Town of Paradise and follow the procedures outlined in 1951-O. RD staff will review the Town's audit to determine if the Town can pay off now either with cash available or through other borrowing. If not, we will see if the Town can pay off the loan early. If they are unable to pay off either now or early, then the loan will be classified as non-program and the Town will be permitted to pay off the loan under existing regulations. Finance Office will be notified and the appropriate annual reporting requirements will be met.

### **OIG Position**

We accept Rural Development's management decision on this recommendation.

**CHAPTER 2****AREA OFFICES DID NOT TAKE APPROPRIATE ACTION TO FACILITATE REFINANCING BY SINGLE-FAMILY HOUSING BORROWERS****FINDING NO. 2**

The four area offices reviewed did not carry out all required actions to facilitate the refinancing of single-family housing loans. According to area office staff or managers, this occurred

because those responsible for carrying out the actions had not had the time to do so because of other job priorities. As a result of the actions being delayed, Rural Development may have been providing assistance to borrowers who no longer required it.

Single-family housing loans are intended to be available only to borrowers who are unable to obtain financing through conventional sources, such as banks. If during the term of the loan, the borrower's financial circumstances change so that he or she becomes able to obtain other financing, the borrower is required to refinance his or her loan at that time. Rural Development plays an active role in tracking borrowers to identify those borrowers who may become able to refinance their loans. Both Rural Development's Centralized Servicing Center (CSC) in St. Louis, Missouri and the area office staff share responsibility in this process. Rural Development's Handbook 1-3550 and its Dedicated Loan Origination and Servicing System (DLOS) Training Manual specify procedures Rural Development staff should follow to accomplish refinancing by eligible borrowers.

In April and October of each year, CSC generates a Graduation Prospect Report (report R248-1) that lists those borrowers it determines may be able to refinance based on predetermined selection criteria. The area office is responsible for reviewing the report and, based on their knowledge of each borrower's circumstances, identifying those borrowers who may be able to refinance. The area office enters a code for each borrower into FASTeller, a DLOS subsystem used by Rural Development to service loans, which causes a letter to be sent to the borrower. The letter requests the borrower to complete a financial statement and/or budget, and submit it along with supporting documentation within 30 days to the area office. Once this information is received, the area office analyzes it to assess whether the borrower is able to qualify for reasonable rates and terms offered by private lenders. Procedures detail actions to be taken at specified intervals based on the borrower's response.

At three of the four area offices reviewed (Merced, Visalia, and Bakersfield), we selected a sample of three borrowers at each site from the April 2001 R248-1 report to evaluate the office's actions to facilitate refinancing by eligible borrowers. At the fourth office (Oroville), we were unable to select a sample because the office could not generate the report (see further discussion below).

At the three offices, we found that not all required actions had been taken for seven of the nine borrowers in our sample. The required actions had been carried out for the remaining two borrowers.

In each of the nine cases, the initial step had been taken to identify potential candidates for refinancing and code the system to send the initial letter to the borrower.

Four of the seven borrowers failed to respond to the initial letter. In these cases, procedures call for the area office to request the system to send a followup letter, giving the borrower an additional 15 days to provide the requested information.

- In three cases, the area office did not request the followup letter, and no further action had been taken on the case at the time of our review, approximately 3 months after the initial letter had been requested.
- In the fourth case, the area office requested the followup letter to be sent, but the borrower also failed to respond to this letter, and the area office had taken no further action at the time of our visit, about 1 month after the followup letter had been requested. In such cases, procedures call for the area office to contact the borrower by telephone and request a final letter be sent to the borrower.

Three of the seven borrowers did respond to the initial letter and submitted financial information to the area office.

- In one case, the information submitted by the borrower was incomplete, but the area office had not taken further action to request the missing information at the time of our audit, approximately 2 months after the borrower had submitted the information.
- In two cases, the area office determined the borrower might be eligible to refinance. In these cases, the area office is responsible for coding the system to send a letter to the borrower, giving the borrower 90 days to refinance their loans. If no response has been received within 45 days, procedures call for a reminder letter to be sent. In both

cases, the area office had requested the 90-day letters to be sent, but had not requested the 45-day reminder letter to be sent, although more than 45 days had elapsed (at the time of our audit, approximately 63 and 70 days had elapsed in the two cases).

In the fourth area office reviewed (Oroville), area office staff had not taken any action relating to refinancing by single-family housing borrowers. The area office manager stated that the office had not been performing this process due to the large volume of work that needed to be completed in other areas. We were unable to obtain a copy of the April 2001 R248-1 report at this office because the manager stated that the designated printer was not functioning.

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## **RECOMMENDATION NO. 2**

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Ensure that area offices comply with the requirements relating to the refinancing of loans by single-family housing borrowers.

### **Rural Development Response**

In its written response dated February 15, 2002, Rural Development stated

We concur with the recommendation. Within 30 days Rural Development will be issuing a memo to all managers and directors in the field notifying them that the graduation process will be considered a high priority. When Graduation Prospect Reports are generated by Centralized Servicing Center in April and October, managers will be required to certify the status of graduation accounts.

### **OIG Position**

We accept Rural Development's management decision on this recommendation.

**CHAPTER 3****AREA OFFICE DID NOT MAINTAIN AN ADEQUATE SEPARATION OF COLLECTION DUTIES FOR SINGLE-FAMILY HOUSING PAYMENTS****FINDING NO. 3**

The Visalia area office did not maintain a separation of duties in the collection of payments received from single-family housing borrowers.<sup>5</sup> According to Rural Development staff, this occurred because they believed it was no longer required to separate collection duties since single-family housing payment processing procedures were simplified in 1997. Consequently, the potential for the misuse of funds was increased.

Rural Development procedures<sup>6</sup> require that

Offices with three or more individuals<sup>7</sup> will ensure that at least two individuals are involved in collecting borrower payments — one to control the payments and one to control the data. These duties should be rotated semiannually.

According to area office staff, the office has not maintained a separation of duties for collections since the State converted to CSC in 1997. Prior to 1997, single-family housing borrowers would submit their payments directly to their local office. The collection process required more extensive documentation and duties were separated. Under the new procedures, borrowers submit their payments directly to CSC, although certain Rural Development offices, including the Visalia area office, still accept payments directly from borrowers.

At the time of our audit, the Visalia area office was receiving only a limited number of payments. Between October 4, 2000, and July 9, 2001, the office took in 37 collections totaling \$51,896 from single-family housing borrowers. According to area office staff, when a borrower brought in a payment, any one of the available Rural Development technicians would handle the entire collection process. The process consisted of recording the collection on the office's collection log, completing a payment coupon (if the borrower did not have one), making a copy of the check or money

<sup>5</sup> Of the four area offices we visited, the Visalia area office was the only one that accepted payments.

<sup>6</sup> RD Instruction 1951-B, paragraph 1951.55 (j)(2), dated June 19, 1991.

<sup>7</sup> These requirements are applicable to the Visalia area office because it has a staff of more than three.



order and payment coupon, and mailing the payment and coupon to CSC for processing.

By not separating the duties of collecting and forwarding payments, the potential for misuse of funds was increased.

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### **RECOMMENDATION NO. 3**

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Ensure that area offices processing collections comply with requirements that collection duties be separated.

#### **Rural Development Response**

In its written response dated February 15, 2002, Rural Development stated

We concur with the recommendation. Rural Development at the National Level has been in the process of revising RD Instruction 1951-B, revised June 19, 1991. In an unnumbered letter dated, September 15, 1999, Rural Development National Office issued interim procedures for handling and safeguarding collections in field offices. California AN No. 1004 (1951-B) was issued on July 2, 2001, to relay the new procedures relating to management control requirements in the handling and safeguarding of collections in field offices. The checklist specifically addresses the separation of duties. A teleconference was also held on November 13, 2001, with all field office managers and directors to review the guidelines and answer any questions. A copy of the AN was provided during the exit conference.

#### **OIG Position**

We accept Rural Development's management decision on this recommendation.

**CHAPTER 4****LOCAL AGENCY PROGRAM COORDINATOR DID NOT VALIDATE TRANSACTIONS IDENTIFIED BY THE PURCHASE CARD MANAGEMENT SYSTEM****FINDING NO. 4**

The Local Agency Program Coordinator (LAPC) did not validate cardholder transactions selected by the Purchase Card Management System (PCMS) for review. According to the

LAPC, this occurred because she did not schedule this task as a priority. As a result, there is not adequate assurance that cardholders were using purchase cards in accordance with program requirements.

The purchase card program is intended to reduce administrative costs by streamlining the process for making smaller purchases of goods and services. Cardholders can expend up to \$2,500 per transaction.<sup>8</sup> Purchase cards are not to be used for personal purchases under any circumstances.

The LAPC for California was issued a purchase card, and authorized the issuance of purchase cards to 10 other State and area office personnel. During fiscal year 2001 (through May 31, 2001), a total of \$184,145 was charged to the 11 purchase cards.

The LAPC is responsible for validating transactions selected by PCMS (an automated system designed to manage the purchase card program) for validation.<sup>9</sup> PCMS statistically selects the transactions, and sends a message electronically to the LAPC requiring that specified data relating to the transaction be validated.

The LAPC stated that she had not performed the validations due to other responsibilities, and had not considered them a high priority. However, the LAPC concurred that the validations should have been conducted.

**RECOMMENDATION NO. 4**

<sup>8</sup> LAPC's have higher limits.

<sup>9</sup> APC/LAPC Purchase Card Program Guide, Section II, Dated September 2000; APC/LAPC PCMS Users Guide, Section III, dated August 2000.

Require the LAPC to validate purchase card transactions selected by PCMS for validation, in accordance with Rural Development procedures.

**Rural Development Response**

In its written response dated February 15, 2002, Rural Development stated

We concur in both the findings and recommendation of this recommendation. A memo will be issued to each cardholder reminding them of the regulations. The LAPC will monitor the accounts in accordance with Rural Development regulations. Scheduled completion date is within 30 days.

**OIG Position**

We accept Rural Development's management decision on this recommendation.

**CHAPTER 5****RURAL DEVELOPMENT DID NOT ALWAYS DOCUMENT COMMUNITY FACILITY BORROWERS' INABILITY TO OBTAIN CREDIT ELSEWHERE****FINDING NO. 5**

Rural Development did not document the borrower's inability to obtain credit elsewhere for two of the five CF loans we reviewed. According to a State office official, this occurred due to oversight. As a result, there was not adequate assurance that this program requirement had been met by the borrowers.

Regulations<sup>10</sup> require Rural Development to

determine and document that the applicant is unable to finance the proposed project from their own resources or through commercial credit at reasonable rates and terms.

Procedures require that Rural Development's determination that the applicant is unable to obtain other financing be documented on the project summary (form RD 1942-43). The instructions for the form<sup>11</sup> require that section S of the form (District Director's Recommendations) "... include documentation on the availability of other credit ..."

We found that the project summaries for four of the five projects reviewed did not include the required documentation on the project summary; however, for two of the four projects, Rural Development managers did document the determination elsewhere.

- In one case (Kern River Valley Youth Center, Inc.), the determination was documented in a letter to the State office.
- In another case (Castle Challenger Learning Center Foundation), the conclusion was documented on a preapplication review document.

In the remaining two cases (Town of Paradise and City of Biggs), we could not locate any documentation of Rural Development's determination.

In each case, Rural Development officials told us that they had considered

<sup>10</sup> RD Instruction 1942.17 (b)(3), dated February 6, 1985.

<sup>11</sup> Forms Manual Insert, Form RD 1942-43, dated September 30, 1998.

this requirement and concluded that other financing was not available to the applicants, and we did not find any evidence suggesting that the applicants could have obtained financing elsewhere. However, Rural Development procedures require that the determination be documented in the project summary, and we concluded that complying with this procedure would provide greater assurance that loan recipients have met all eligibility requirements.

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## **RECOMMENDATION NO. 5**

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Ensure that the project summaries document Rural Development's determinations regarding borrowers' ability to obtain other financing.

### **Rural Development Response**

In its written response dated February 15, 2002, Rural Development stated

We concur in the finding and recommendation. Within the next 30 days, a memo will be issued to the field emphasizing this requirement. Additionally, when the State Office reviews loans for approval they will ensure that project summaries are documented.

### **OIG Position**

We accept Rural Development's management decision on this recommendation.

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**EXHIBIT A – SUMMARY OF MONETARY RESULTS**

<b>FINDING NO.</b>	<b>DESCRIPTION</b>	<b>AMOUNT</b>	<b>CATEGORY</b>
1	Community facilities loan made to ineligible applicant	\$264,000	Questioned Loan, Recovery Recommended

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**EXHIBIT B – LOAN ACTIVITY AT OFFICES VISITED**

<b>OFFICES VISITED</b>	<b>NUMBER AND TYPES OF LOANS REVIEWED</b>					
	<b>SFH Guaranteed Loans</b>	<b>B &amp; I Loans</b>	<b>Water &amp; Waste Loans</b>	<b>Community Program Loans</b>	<b>MFH Direct Loans</b>	<b>SFH Direct Loans</b>
Bakersfield AO			1	1	3	5
Merced AO			1	1		5
Oroville AO		4	1	3		5
Visalia AO		2	3			5
State Office	5					
<b>TOTAL</b>	<b>5</b>	<b>6</b>	<b>6</b>	<b>5</b>	<b>3</b>	<b>20</b>

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**EXHIBIT C – RURAL DEVELOPMENT'S WRITTEN RESPONSE TO THE  
DRAFT REPORT**




**Rural  
Development**  
Business . Housing . Utilities

430 "G" Street, Agency 4169  
Davis, CA 95616-4169  
Phone: (530) 792-5833  
Fax: (530) 792-5842  
TDD: (530) 792-5848  
[www.rurdev.usda.gov/ca](http://www.rurdev.usda.gov/ca)

February 15, 2002

**TO:** Sam W. Currie, Regional Inspector General  
Office of Inspector General  
Western Regional Office  
75 Hawthorne St., #200  
San Francisco, CA 94105

**FR:** Paul Venosdel, State Director   
Davis, California

**RE:** Rural Development – FY 2001 Financial Statements  
California State Office

This will provide our response to the five recommendations in the official draft report dated December 13, 2001.

**Finding No. 1**

**Recommendation No. 1 – Collect or otherwise service the unauthorized loan to the Town of Paradise in accordance with the provisions of RD Instruction 1951-O.**

We concur with the recommendation. Within 30 days Rural Development State Office staff will meet with the Town of Paradise and follow the procedures outlined in 1951-O. RD staff will review the Town's audit to determine if the Town can pay off now either with cash available or through other borrowing. If not, we will see if the Town can pay off the loan early. If they are unable to pay off either now or early, then the loan will be classified as non-program and the Town will be permitted to pay off the loan under existing regulations. Finance Office will be notified and the appropriate annual reporting requirements will be met.



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## EXHIBIT C – RURAL DEVELOPMENT'S WRITTEN RESPONSE TO THE DRAFT REPORT

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### **Finding No. 2**

**Recommendation No. 2 – Ensure that area offices comply with the requirements relating to the refinancing of loans by single-family housing borrowers.**

We concur with the recommendation. Within 30 days Rural Development will be issuing a memo to all managers and directors in the field notifying them that the graduation process will be considered a high priority. When Graduation Prospect Reports are generated by Centralized Servicing Center in April and October, managers will be required to certify the status of graduation accounts.

### **Finding No. 3**

**Recommendation No. 3 – Ensure that area offices processing collections comply with requirements that collection duties be separated.**

We concur with the recommendation. Rural Development at the National Level has been in the process of revising RD Instruction 1951-B, revised June 19, 1991. In an unnumbered letter dated, September 15, 1999, Rural Development National Office issued interim procedures for handling and safeguarding collections in field offices. California AN No. 1004 (1951-B) was issued on July 2, 2001, to relay the new procedures relating to management control requirements in the handling and safeguarding of collections in field offices. The checklist specifically addresses the separation of duties. A teleconference was also held on November 13, 2001, with all field office managers and directors to review the guidelines and answer any questions. A copy of the AN was provided during the exit conference.

### **Finding No. 4**

**Recommendation No. 4 – Require the LAPC to validate purchase card transactions selected by PCMS for validation, in accordance with Rural Development procedures.**

We concur in both the findings and recommendation of this recommendation. A memo will be issued to each cardholder reminding them of the regulations. The LAPC will monitor the accounts in accordance with Rural Development regulations. Scheduled completion date is within 30 days.

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## EXHIBIT C – RURAL DEVELOPMENT'S WRITTEN RESPONSE TO THE DRAFT REPORT

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**Finding No. 5**

**Recommendation No. 5 – Ensure that the project summaries document Rural Development's determinations regarding borrowers' ability to obtain other financing.**

We concur in the finding and recommendation. Within the next 30 days, a memo will be issued to the field emphasizing this requirement. Additionally, when the State Office reviews loans for approval they will ensure that project summaries are documented.

If you have any questions regarding the above information please contact Rita Medina, on (530) 792-5833.

cc: Sherrie Hinton-Henry, FMD, Rural Development, Washington, DC