



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

Alert Memorandum
Issue Date: March 29, 2002
Report Number: 2-16

TO: Arnold Rosenthal, Assistant Administrator for
Portfolio Management, Office of Financial Assistance

Robert G. Seabrooks

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

SUBJECT: [FOIA EX. 4] Review of Asset Sale [EX. 4] Due Diligence Contract

The purpose of this memorandum is to bring to your attention two issues that we identified during our on-going audit of asset sales due diligence contracts. The issues relate to work performed by [FOIA EX. 4] and involve (i) validation of the due diligence contractor's cost data and (ii) erroneous conclusions concerning over-billing issues.

Background

For each sale, SBA contracts with a transaction financial advisor and a due diligence firm to assist with the program. SBA's due diligence contractor ([FOIA EX. 4]) was awarded due diligence service contracts for asset sale [FOIA EX. 4]. This report relates to a post review performed by [FOIA EX. 4] on the due diligence contract awarded for asset sale [EX.4].

Issues discussed in this report originated from an anonymous source that alleged [FOIA EX. 4] had submitted over \$2 million in invoices (over-billing) to SBA for work it did not complete. SBA hired an independent CPA firm ([FOIA EX. 4]) to validate the magnitude of the alleged billing concerns. [FOIA EX. 4] was requested to review third party reports invoices submitted by [FOIA EX. 4] for Asset Sale [EX.4] to determine if [FOIA EX. 4] internal audit sufficiently corrected the errors reported in sale number [EX.4] and verify that the amounts owed to SBA were also correct. [FOIA EX. 4] presented a final report to SBA containing results of their review. As a part of our audit of the asset sales due diligence contracts, we reviewed [FOIA EX. 4] report, selected working paper documents, and interviewed [FOIA EX. 4] Managing Partner.

Validation of the Due Diligence Contractor’s Cost Data

[FOIA EX. 4] were engaged to perform an agreed upon procedures review in accordance with applicable AICPA standards. Accordingly, it was required to exercise due professional care in the performance of the engagement.

Auditors who use computer-generated data to support a finding should perform tests to ensure the reliability of that data. Data reliability is tested by (a) confirming computer-processed data with product users; (b) comparing computer-processed data with source documents; (c) conducting physical counts and inspections; (d) reviewing output listings for completeness, obvious errors, and reasonableness of values; (e) tracing source documents to computer output; (f) recalculating computations; and/or (g) developing additional tests deemed necessary to validate data reliability.

[FOIA EX. 4] used the due diligence contractor provided computer-generated data to support audit findings without performing tests to ensure data reliability. Specifically, they did not compare the computer-processed data with source documents. To illustrate, our review of [FOIA EX. 4] working paper documents did not disclose any support, documentary or otherwise, for Duplication of Third Party Reports (TPRs) and Loan Numbers (Attachment C) of [FOIA EX. 4] Report. Without testing of data base transactions there is no assurance that the data is correct.

The Managing Partner, [FOIA EX. 4] told us the support consisted of a very large computer database maintained at his office that nearly “crashed” the equipment. Moreover, he acknowledged that the database used to support the Report was not validated for reliability and that transaction testing was not accomplished. He stated these things were not accomplished because “they were not included in the scope of the agreed upon (agreement with SBA) procedures.” Further, he stated that to validate the database and perform transaction testing was outside the scope of his review. Particularly, he stated that SBA did not ask him to perform a comprehensive audit.

Over-Billed Amount per the Third Party Reported Rates Analysis (Attachment B) is Incorrect

We reviewed the tables presented in [FOIA EX. 4] final report and found numerous mathematical errors. Not considering the above-mentioned deficiencies, the over-billed amount of \$620,996 per Attachment B of the [FOIA EX. 4] Report was not calculated correctly as illustrated in the following table:

TPR Type	[FOIA EX. 4]	[FOIA EX. 4]	OIG	OIG	Difference
	Quantity	Amount	Quantity	Amount	Amount
Borrower Credit Report	18,129	\$18,129	18,129	\$18,129	
Broker Price Opinion	8,254	1,740,041	8,254	1,794,498	(\$54,457)
Drive By Appraisal	25	7,500	25	7,500	
Full Appraisal	1,077	2,477,100	1,077	2,477,100	
Market Survey	1,064	186,200	1,064	185,240	960
Phase 1 Environmental	129	251,550	129	251,550	
Title Searches	9,989	2,591,980	9,989	3,037,525	(445,545)
Transaction Screen	166	141,100	166	141,100	
UCC Searches	6,119	689,839	6,119	740,399	(50,560)
Borrower Asset Search	968	117,128	968	117,128	
Borrower Bankruptcy Report	48,574	109,833	48,574	228,750	(118,917)
Guarantor Asset Search	841	101,761	841	101,761	
Regulatory Environmental	142	63,900	142	63,900	
Totals/	95,477	\$8,496,061	95,477	\$9,164,580	

1/ Reported amount billed to SBA assumed accurate for purposes of this illustration.

We found the differences noted above occurred because of tiers of volume (payment scale) errors, and/or computation errors. For example, in calculating the amount due [FOIA EX. 4] for Title Searches, we found the correct amount totaled \$3,037,525, not \$2,591,980, a difference of \$445,545. Specifically, [FOIA EX. 4] erred because the number of loans listed did not match the contracted payment scale for quantity discounts. **(See attached [FOIA EX. 4] Table A-1 and OIG Table A-2).**

The payment scale reduced the payment rate as the volume increased. For example, [FOIA EX. 4] was supposed to be paid \$310 per title search for the first 1,000 searches, \$305 per search for the next 1,500 searches, \$300 for the next 2,500 searches and so forth. Contrasting these tables illustrates that [FOIA EX. 4] noted loan tiers in Table A-1, Column B (Disaster Business category) did not match the payment scale shown in Table A-1, Column A. For instance, while [FOIA EX. 4] correctly calculated the payment using 1,000 title searches at the correct \$300 level, they incorrectly calculated each succeeding tier by using 1,000 title searches in each tier rather than the amount identified in the payment scale. We also noted a similar deficiency for Disaster Home, Column E. Consequently, rate extension totals were incorrect.

Furthermore, [FOIA EX. 4] addition of the extended totals was also incorrect because only the first "4 of the 6 cells" listed (Table A-1, Column. D.), were picked-up equaling \$1,210,000 apparently due to an error in the spreadsheet formula. With the changes needed to scale, rate extensions, and additions, we concluded the correct total for Column D should have been \$1,649,365.

We brought this matter to the attention of the Managing Partner of [FOIA EX. 4] who tentatively concurred with the results of our review. We also briefed the SBA Director of the Asset Sales on the results of our review.

As a result of [FOIA EX. 4] failure to validate information in the database combined with the above mentioned errors, we question the reliability of the [FOIA EX. 4] report.

Recommendation

We recommend that the Associate Administrator, Office of Financial Assistance take the following action:

- 1A. [FOIA EX. 4] database be validated and transaction testing be accomplished to ensure data accuracy and reliability prior to reaching a negotiated settlement with [FOIA EX. 4] on Asset Sale [EX. 4].

Please provide your management response to the recommendations within 30 days from the date of this report on the attached Recommendation Action Sheets (SBA Form 1824). Any questions you may have regarding this report may be directed to Garry Duncan, Director, Credit Programs Group, at 202-205-7732.

TABLE A-1

Third Party Report Types - Review of [*] Support for Overbilling of \$620,996

Title Searches

[FOIA Ex. 4] A

Scale	Disaster Business			Disaster Home			CDC Loans			Section 7a Loans		
	Number	Rate	Total	Number	Rate	Total	Numb	Rate	Total	Numb	Rate	Total
1 to 1000	1,000	310.00	310000	1,000	310.00	310000	66	310.00	20460	740	310.00	229400
1001 to 2500	1,000	305.00	305000	1,000	305.00	305000		305.00			305.00	0
2501 to 5000	1,000	300.00	300000	1,000	300.00	300000		300.00			300.00	
5001 to 10000	1,000	295.00	295000	736	295.00	217120		295.00			295.00	
10001 to 20000	1,000	290.00	290000		290.00	0		290.00			290.00	
Over 20000	447	290.00	129630		290.00			290.00			290.00	
Total	5,447		\$1,210,000	3,736		\$1,132,120	66		\$20,460	740		\$229,400

[*] Total No. 9,989
 [*] Total \$\$ \$2,591,980

TABLE A-2

Title Searches

OIG

Scale	Disaster Business			Disaster Home			CDC Loans			Section 7a Loans		
	Number	Rate	Total	Number	Rate	Total	Numb	Rate	Total	Numb	Rate	Total
1 to 1000	1,000	310.00	310000	1,000	310.00	310000	66	310.00	20460	740	310.00	229400
1001 to 2500	1,500	305.00	457500	1,500	305.00	457500		305.00			305.00	0
2501 to 5000	2,500	300.00	750000	1,236	300.00	370800		300.00			300.00	
5001 to 10000	447	295.00	131865		295.00	0		295.00			295.00	
10001 to 20000		290.00			290.00	0		290.00			290.00	
Over 20000		290.00			290.00			290.00			290.00	
Total	5,447		\$1,649,365	3,736		\$1,138,300	66		\$20,460	740		\$229,400

OIG Total No. 9,989
 OIG Total \$\$ \$3,037,525 Difference: \$445,545 (\$3,037,525 - \$2,591,980)

* FOIA EX. 4