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

AUDIT REPORT
ISSUE DATE: September 29, 2003
REPORT NUMBER: 3-41

To: James E. Rivera, Associate Administrator
Office of Financial Assistance

From: Robert G. Seabrooks, Assistant Inspector General
For Auditing

Subject: Audit of a SBA Guaranteed Loan to Concrete Transport, Inc.

Attached is a copy of the subject audit report. The report contains one finding and recommendation addressed to your office. Your comments have been synopsized in the report and included in their entirety at Appendix A.

The recommendation in this report is subject to review and implementation of corrective action by your office in accordance with the existing Agency procedures for audit follow-up. Please provide your management decision for the recommendation to our office within 30 days of the date of this report using the attached SBA Form 1812, Recommendation and Action Sheet.

Any questions or discussion of the finding and recommendation contained in the report should be directed to Garry Duncan, Director, Credit Programs Group, at 202-205-7732.

Attachment

AUDIT OF SBA GUARANTIED LOAN TO
CONCRETE TRANSPORT, INC.
BALTIMORE, MARYLAND

AUDIT REPORT NO. 3-41

SEPTEMBER 29, 2003

AUDIT OF SBA GUARANTIED LOAN TO
CONCRETE TRANSPORT, INC.
BALTIMORE, MARYLAND

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BACKGROUND

The Small Business Administration (SBA) is authorized under Section 7(a) of the Small Business Act to provide financial assistance to small businesses in the form of government-guarantied loans. SBA loans are made by participating lenders under an agreement (SBA Form 750) to originate, service, and liquidate loans in accordance with SBA regulations, policies, and procedures. SBA is released from liability on a loan guaranty, in whole or in part, within SBA's exclusive discretion, if a lender failed to comply materially with SBA regulations, the Loan Agreement, or did not make, close, service, or liquidate a loan in a prudent manner.

During the audit of SBA's Guaranty Purchase Process (Report No. 3-15, issued March 17, 2003), the OIG identified several problematic loans that were subject to further examination. One of the loans was made by General Electric Capital Corporation (lender) to Concrete Transport, Inc. (borrower) and is the subject of this report. The loan was processed under the Preferred Lenders Program (PLP) which permits lenders to process, close, service, and liquidate loans with reduced requirements for documentation or prior approval by SBA.

The lender approved this loan (number 153-313-4007) on September 11, 1997, for $1,000,000. The purpose of the loan was to purchase a concrete business. The loan was disbursed in December 1997 and the borrower defaulted in February 10, 1999, 14 months after disbursement. SBA purchased the guaranty for $640,325 in June 2000.

AUDIT OBJECTIVE AND SCOPE

The objective of the audit was to determine if the lender originated, disbursed, and liquidated the loan in accordance with SBA rules and regulations. The loan was reviewed for compliance with requirements found in SBA rules and regulations and the SBA lender guaranty agreements. During the audit, we examined the loan files maintained by SBA and the lender. We also interviewed SBA officials in the Office of Financial Assistance (OFA). The audit was conducted during May 2002 in accordance with Government Auditing Standards.

RESULTS OF AUDIT

Finding 1 - The Lender did not Properly Protect and Secure Loan Collateral

The lender waited six months to inventory the collateral and assess its condition after discovering that the prior owner (seller) had removed a portion of the collateral from the small business concern. At liquidation, several pieces of collateral were missing. As a result, the loss to SBA was increased by $273,675 when the guaranty was improperly paid in full.

The lender was required by the Authorization & Loan Agreement to obtain a first security interest on all machinery and equipment, including automotive equipment. The appraisal of all available business assets was based on a list provided by the seller, who also accompanied the appraiser during the inspection of the collateral. Prior to loan

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closing, the seller claimed that the collateral list mistakenly included an automobile that was his personal property. The seller did not claim ownership of the other business assets at that time. The liquidation value of the collateral was appraised at $964,400 and the appraisal report was attached to the financing statements filed to record the liens on the equipment.

Fifteen months after loan disbursement and one month after the borrower had defaulted, the lender met with the borrower to discuss a deferment request. During the visit, the lender learned that:

➢ A portion of the collateral had been removed by the seller who claimed it belonged to another business. According to the lender's report, the collateral removed included "...a front-end loader and a couple of industrial concrete saws that have some substantial value." Based on the origination appraisal, the items removed had a liquidation value of $65,000.

➢ The facility was operating at about 20 percent of capacity and needed $100,000 in repairs, but the borrower had no means to finance the repairs.

Based on these factors, the lender concluded that the business was beyond repair and that a deferment would only forestall the inevitable.

According to SOP 50 51 2, Chapter 8, paragraph (8)(b)(1), a lender must perform an inventory of collateral and determine its condition within 15 days of an adverse event, such as collateral being lost or its value diminished, which would cause a loan to go into liquidation. The lender, however, did not perform the requisite inventory until six months after learning that collateral was missing and the business was failing.

A comparison of the origination and liquidation appraisals showed that 17 pieces of collateral with a liquidation value of $364,900 were missing at liquidation. Among the missing collateral were a central mixer and a batch plant, both essential to the operation of the business. Although three of the items were noted as missing by the lender during the previous site visit, there was no evidence that the lender made any attempt to recover the equipment. The remaining 14 items were not identified as missing during the liquidation process.

The lender's six month delay in performing a required site visit to assess and secure collateral, and its lack of effort to recover improperly removed collateral, increased SBA's loss by $273,675 ($364,900 X 75%).

RECOMMENDATION

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

1. Require the lender to repay SBA $273,675 for loan number 1533134007.

Management Comment

[FOIA Ex. 5   ]

OIG Evaluation of Management Comment

Management's comment is responsive to the recommendation. [FOIA Ex.5]
[FOIA Ex.5   ]

From:	Intlekofer, Walter C.
Sent:	Tuesday, September 23, 2003 9:20 AM
To:	Seabrooks, Robert G.
Cc:	Harris, Larry G.; Seifert, Stephen; Miller, John A.
Subject:	Concrete Transport, Inc.

[

FOIA Ex. 5

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AUDIT REPORT DISTRIBUTION

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