



OFFICE OF
INSPECTOR GENERAL
U.S. DEPARTMENT OF THE INTERIOR

RECOVERY

RECOVERY OVERSIGHT ADVISORY

Indian Loan Guaranty Program



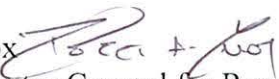
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APR 17 2012

Memorandum

To: Rhea S. Suh
Assistant Secretary, Policy, Management and Budget

Through: Mary Pletcher
Department Recovery Act Coordinator

From: Robert A. Knox 
Assistant Inspector General for Recovery Oversight

Subject: Recovery Oversight Advisory – Indian Loan Guaranty Program
Report No. RO-C-BIA-066-2011

This advisory regarding the Indian Loan Guaranty Program is part of our ongoing effort to oversee and ensure the accountability of funding appropriated to the U.S. Department of the Interior (DOI) in the American Recovery and Reinvestment Act of 2009 (Recovery Act).

Background

The Indian Loan Guaranty Program (Program) is executed by the Office of Indian Energy and Economic Development (OIEED), which reports to the Assistant Secretary – Indian Affairs (Indian Affairs). The Program helps eligible borrowers develop Indian businesses by securing conventional lender financing while helping lenders reduce their risk on the loans they make to finance these businesses.

In order to reduce the lender's risk, the Program can guarantee up to 90 percent of the unpaid principal and accrued interest due on a loan; the lender assumes the remaining 10 percent. The Program charges the lender a 2 percent premium of the original loan principal to guarantee the loan. The lender can pass the premium on to the borrower in the form of a one-time payment or by adding 2 percent to the borrower's loan.

The Program receives annual appropriations; OMB then approves a multiplier, which leverages the appropriated funds by increasing the amount that can be loaned. When a loan is guaranteed, a portion of the annual appropriation and the 2 percent premium are deposited in a specific account held at the Department of the Treasury to cover any defaulted loans. If there are no defaults, the account is closed out, and any remaining funds go back to the United States General Account.

The Recovery Act appropriated \$10 million for the Program to guarantee loans to Indian-owned business entities, tribes, and business enterprises established and recognized by tribes. Of

the \$10 million, up to 5 percent (\$500,000) was allocated for administrative purposes. DOI could use 10 percent (\$50,000) of these funds for its own administrative costs. With the Recovery Act designated multiplier, the Program could have leveraged its remaining \$9.5 million allocation to guarantee up to \$122.8 million in loans.

During our review, we spoke with Program and Department staff, as well as lending institutions that received loan guarantees, and visited the facility that had been funded through the one Recovery Act loan guaranty made through the Program. We also contacted nine lending institutions that received a loan guaranty in fiscal year (FY) 2010, including the bank that received the single Recovery Act loan guaranty. We heard back from six of the nine lending institutions.

Findings

Failure to Follow Recovery Act Requirements

We found that only one loan, to the St. Croix Tribe of Chippewa Indians of Wisconsin (Tribe), for \$38,118,000 was guaranteed using \$2,946,521 of the Program's Recovery Act funds. The Heartland Business Bank provided the loan for the Tribe to complete the design and construction of a 47-room hotel, convention center, and casino. The hotel and convention center included, among other features, a restaurant, bar, indoor swimming pool, and gift shop. The Recovery Act loan guaranty covers only the hotel and convention center portion of the project. In order to comply with section 1604 of the Recovery Act, which prohibits the use of Recovery Act funds to create gambling establishments, the Tribe kept the casino portion of the project separate and secured a second, conventional loan through the Heartland Business Bank for \$17,500,000 to complete that part of the project.

We commend the bank, the Tribe, and the Program for attempting to comply with section 1604 of the Recovery Act. We note, however, that the Program failed to meet all of the criteria in the section, since the hotel portion of the project included a swimming pool, and section 1604 clearly states that Recovery Act funds may not be used to develop swimming pools. No actual Recovery Act funds were spent to build the pool; the funds did however guarantee the construction loan. When we questioned tribal officials about this matter, they indicated that they were never informed of this Recovery Act requirement. They also told us that the swimming pool had always been part of the construction plan.

Disincentives for Loans

The Program received \$10 million in Recovery Act appropriations but was only able to guarantee one loan. While we acknowledge that economic conditions at the time were volatile and lending institutions were reluctant to lend, we found the Program could have taken more proactive steps to guarantee additional loans.

In contrast to the Program, we found that the Small Business Administration (SBA) Recovery Act loan program was extremely successful. SBA obligated all of its original

\$375 million appropriation and was then able to secure an additional \$125 million to guarantee more loans. SBA had a two-pronged approach to administering its Recovery Act funds:

1. It raised its guaranty rate from the typical 75-85 percent to 90 percent.
2. It reduced or eliminated the premium charge to originate the loan.

SBA officials indicated that the reduction or elimination of this charge did provide an incentive for lenders to loan money again and for borrowers to apply for loans. Moreover, one lending institution we contacted about the OIEED Program indicated that the premium charge detracts from the Program's appeal. They stated that many borrowers could not afford the cost.

We appreciate that the Program already guarantees loans at a 90 percent rate and could not have increased its loan guaranty rate further, but we do believe that Program officials could have given greater consideration to decreasing or eliminating the loan origination premium. The officials told us they had considered reducing or eliminating the charge but decided not to because OMB had already approved the calculated annual subsidy rate to include the premium, and they believed they needed additional authority to eliminate the charge. If Program officials had followed up with OMB and eliminated the fee, they might have created added incentives for lenders and borrowers. While recalculating the subsidy rate to eliminate the premium charge may have created an administrative burden, doing so could have increased the effectiveness of the Program.

In response to our draft report, OIEED officials noted a concern that our comparison of the SBA loan program and the Indian Loan Guaranty Program may be misleading. Our intent was not to show a direct comparison between the two programs. We realize they are different and are governed by different rules and regulations, but we were highlighting the potential effect of removing the origination fee to provide an additional incentive for borrowers to seek loans and for lenders to negotiate loan agreements.

Inadequate Planning

We also believe that Program officials did not have a sound plan in place for expending the Program's Recovery Act funds and informing lenders of its potential to guarantee loans. Program officials told us they had not changed their business practices to accommodate the influx of Recovery Act funds. Of the six lending institutions we contacted, two were unaware that the Program had received Recovery Act funds, were never contacted by the Program regarding these funds, and did not know they were eligible to receive a guaranty on a loan.

In addition, Program staff could not provide us with a spending plan and budget for the administrative funds the Program received. One staff member indicated that a draft plan and budget had been created but was never published or approved. We were told that the Program used the administrative funds to pay two employees' salaries and other expenses, including travel charges, phone charges, training, printing, and miscellaneous expenses. According to documentation we received from Program officials, the Program only expended \$231,314, or about 50 percent, of its allocated administrative budget.

As a result of only one loan being secured under the Program, on August 10, 2010, Congress rescinded \$6,820,000 of the Program's unobligated funding. Program officials also speculated that their annual appropriation was dramatically scaled back for FY 2012 because they were unable to expend most of their Recovery Act funding (see figure 1). OMB officials verified this speculation.

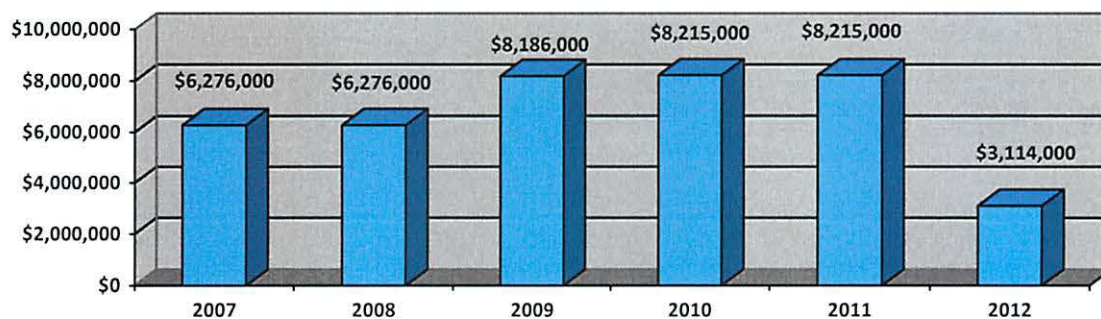


Figure 1: Annual Fiscal Year Appropriations for Indian Loan Guaranty Program

In response to our draft report, OIEED officials noted that they did have a plan in place to expend the Program funding. They participated in the development of the Department's Recovery and Implementation Plans, which helped guide their efforts to implement the Recovery Act. They also designated two employees to work on the Recovery Act efforts by attending seminars and workshops, among other events, to help publicize the program. The Program also worked with Bureau of Indian Affairs officials on both a Regional and Agency level to communicate their ability to guarantee more loans under the Recovery Act. In addition to this, they developed a Recovery Act Loan Guarantee flyer that was distributed at meetings, via conventional mailing, and to the Program's regional Zone Managers as well as other Program employees. While we appreciate their efforts to publicize the Program, the fact remains that only one loan was guaranteed with Recovery Act funding and \$6,820,000 of Recovery Act funds were rescinded.

Inaccurate Reporting on Recovery Act Projects

The *U.S Department of the Interior American Recovery and Reinvestment Act Plan*¹ (August 2010), found on DOI's Recovery Act Web site, notes the number of Program loans guaranteed in FYs 2009 and 2010. The Plan implies that the Program guaranteed 26 loans in FY 2009 and 7 during the first half of FY 2010 under the Recovery Act. Program officials, however, indicated to us that they included all loans guaranteed in FYs 2009 and 2010, regardless of funding source. Since this is a Recovery Act plan, readers will likely assume that the information in it refers only to Recovery Act funding. It does not, so the information in the Plan is misleading.

¹ See link:

<http://www.recovery.gov/Transparency/agency/Recovery%20Plans/Revised%20DOI%20Recovery%20Act%20Plan%20-%20June%202010.pdf>

The Recovery.gov Web site reports that \$2,946,521 of Recovery Act funds were expended by the Program to support the one loan that was guaranteed for \$38,118,000, but the Program did not report on its \$231,314 in administrative costs.

We contacted officials at the Department who noted that the Program, being administered by Indian Affairs, was arranged in such a manner that the administrative portions of the Program's funds were provided via a reimbursable agreement from the Guaranteed Loan Account (14-2629) to the Office of the Secretary Salaries and Expenses account (14-0101). The Department official noted that it is virtually impossible to trace the administrative portion of the Program's budget, given the way reimbursable funding was reported throughout the Government. In reviewing the Recovery Act Financial Activity Report, downloaded from Recovery.gov, we disagree with this comment. The Financial Activity Report shows total obligations of \$249,768 under the Salaries and Expenses Account (14-0101) for the Program. This figure is different from the \$231,314 figure that Program officials indicated was spent on administration. We asked officials at Indian Affairs to reconcile the \$249,768 from the Financial Activity Report with the \$231,314, but they were unable to do so. An official told us that the \$231,314 figure was in fact the correct amount obligated and spent on administering the Program.

Administrative Burden of the Loan Application

According to its Web site, the Program is designed to help finance both small and large loans for businesses. Of the six lending institutions we contacted, however, four stated that they were not willing to make smaller loans because they considered them unprofitable and the paperwork to be too burdensome. In order to make the process profitable and less cumbersome for lenders, the lending institutions suggested that the Program make the following changes:

1. Require less documentation for small loans.
2. Streamline the process for experienced lenders by letting them underwrite the loan internally.
3. Create preapproval documents for small ticket loans.
4. Create an online application and approval tool with a scorecard system for approving or denying the application.

Administrative Support Costs

We contacted officials at both the Program and bureau levels to understand whether 10 percent of the \$500,000 in administrative funds had been transferred to DOI per the *American Recovery and Reinvestment Act Administrative Support Cost Guidelines – Version 1.2* (figure 2). Neither Program nor bureau officials could provide us with sufficient answers or documentation regarding the matter. We were therefore unable to trace and verify what happened to the \$50,000 in administrative support costs and whether the amount was ever actually transferred to DOI.

Disposition of Funds	Amount
Loan Guaranty	\$2,946,521
Rescission	\$6,820,000
Administrative Costs	\$231,314
DOI Administrative Costs	\$50,000
Total	\$10,047,835

Figure 2: Disposition of Program Funds.

In response to our draft report, a senior official at the Department confirmed that Indian Affairs did not transfer \$50,000 to the Working Capital Fund out of Recovery Act Loan Guaranty appropriations. Instead, all Indian Affairs Recovery Act oversight costs were paid out of the Recovery Act construction account via a reimbursable agreement with the Department. This alleviates our concern that the Program exceeded its authorized funding.

Recommendations

We recommend that the OIEED Director:

1. Restructure the loan guaranty document related to the agreement between the St. Croix Tribe of Chippewa Indians and Heartland Business Bank to omit the swimming pool.
2. Implement a more active outreach effort to encourage more lenders to participate in the Program.
3. Amend the August 2010 *U.S. Department of the Interior American Recovery and Reinvestment Act Plan* to show that only one loan was guaranteed under the Recovery Act.
4. Reconcile the \$249,768 figure from the Financial Activity Report with the \$231,314 figure that the Program indicated was spent on administration.
5. Create a preapproval document for loans below a certain threshold to streamline the process for applying for a small loan guaranty.

In response to our draft report, we note that OIEED concurs with recommendations 1, 2, 3, and 5 and is taking action to implement those recommendations.

Please provide a written response to this advisory within 30 days of receipt detailing the corrective actions DOI will implement to meet our recommendations, as well as targeted completion dates and title(s) of the official(s) responsible for implementation. We will post this advisory on our Web site (www.doi.gov/recovery/) and on Recovery.gov. Information contained in this advisory may also be included in our semiannual reports to Congress. We performed our work in accordance with the applicable Quality Standards for Inspection and Evaluation adopted by the Council of the Inspectors General on Integrity and Efficiency. Please contact me if you have any questions.

cc: Deputy Secretary, U.S. Department of the Interior
Assistant Secretary – Indian Affairs
Director, Office of Executive Secretariat and Regulatory Affairs
Director, Office of Acquisition and Property Management
Acting Director, Office of Financial Management
Director, Office of Indian Energy and Economic Development
Departmental GAO/ OIG Audit Liaison
Audit Liaison, Office of the Secretary
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