Division of Administration
Office of Community Development
Business Recovery Grant and Loan Program

Agreed-Upon Procedures Report

Issued July 16, 2008

LEGISLATIVE AUDITOR
1600 NORTH THIRD STREET
POST OFFICE BOX 94397
BATON ROUGE, LOUISIANA 70804-9397

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LOUISIANA LEGISLATIVE AUDITOR
STEVE J. THERIOT, CPA

July 16, 2008

Independent Accountant's Report on the
Application of Agreed-Upon Procedures

MR. PAUL RAINWATER, EXECUTIVE DIRECTOR
LOUISIANA RECOVERY AUTHORITY
Baton Rouge, Louisiana

We have performed the procedures enumerated below from program inception through October 31, 2007, which were requested and agreed to by you, as executive director of the Office of Community Development (OCD), primarily to assist you in evaluating the operations of the state's Business Recovery Grant and Loan (BRGL) program. This agreed-upon procedures engagement was conducted in accordance with the attestation standards established by the American Institute of Certified Public Accountants and the applicable attestation standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The sufficiency of these procedures is solely the responsibility of management of OCD. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

The procedures we performed and our findings are as follows:

Business Recovery Grant and Loan Program: Grants

We reviewed 1,029 grant files totaling $18,126,387 prepared by the BRGL program intermediaries.[1] We conducted the following procedures to verify that awards granted were in compliance with the program guidelines and properly documented:

1. Procedure

   Verified the intermediaries completed the BRGL grant file review checklist.

[1] The BRGL program was administered by seven intermediaries and managed by the Louisiana Department of Economic Development (LED). The intermediaries hosted intake centers throughout their service areas to ensure business owners had convenient access to information, assistance, and applications. The intermediaries also reviewed the applications and supporting documentation for completeness and determined if the businesses were eligible to receive a grant or loan. Although LED made the final determination on the grant award amounts, the intermediaries requested the funds from LED and OCD and disbursed the funds to the applicants.

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Finding

Because of complications during the initial stages of the program, OCD and LED implemented a policy whereby the intermediaries were required to complete a checklist to document that they had gathered all appropriate documentation to support the funding decision. During our review, we noted that 967 grant files contained a completed BRGL grant file review checklist. We also noted that 62 grant files (1) contained a checklist completed by LED or OCD instead of the intermediary; (2) contained an incomplete grant checklist; or (3) did not contain a checklist.

2. Procedure

Verified the electronic files maintained by LED were consistent with the hard copy files maintained by the intermediaries.

Finding

The hard copy files are maintained by the seven intermediaries in offices located in New Orleans, Lafayette, and Houma. Since LED and OCD do not have immediate access to the hard copy files, they must rely upon the electronic file to make programmatic decisions. To make sound decisions, the files must be accurate. During our review, we noted that 849 electronic files maintained by LED were consistent with the corresponding hard copy grant files maintained by the intermediaries. For the remaining 180 electronic files, one or more fields in the electronic file were not consistent with the hard copy file, which could be problematic due to the limited accessibility of the hard copy files.

3a. Procedure

Verified the applicant files contained sufficient documentation to support that the businesses were operating[2] six months prior to the storm.

Finding

During our review, we noted that 1,003 grant files contained sufficient documentation indicating the businesses were operating[3] six months prior to the storm. This includes start-up businesses, which are an exception to this guideline. Start-up businesses that were legally registered six months before the storm, but

[2] Legally registered or in business as defined by program guidelines.
[3] Legally registered or in business as defined by program guidelines.

were not yet operating, were eligible for the minimum grant award of $10,000. We noted that 26 grant files did not contain sufficient documentation such as articles of incorporation, secretary of state registration, income statements, 2004 or prior business tax returns, or a business license to demonstrate that the business was operating or legally registered at least six months prior to the storm.

3b. Procedure

Verified the applicant files contained sufficient documentation to support that the businesses reopened or demonstrated the potential to reopen.

Finding

According to program policy, the businesses are required to reopen or plan to reopen in one of the 20 affected parishes[4] to be eligible for the program. During our review, we noted that 990 grant files contained sufficient documentation indicating the businesses reopened or demonstrated the potential to reopen and 39 grant files did not. Included in the 39 were five grant files that indicated the applicant planned to open a different type of business than the pre-storm business and four files that indicated the business relocated outside the affected area.

3c. Procedure

Verified the applicant files contained sufficient documentation to support that the businesses had no more than 50 pre-storm (as defined by program guidelines) full-time employees.

Finding

During our review, we noted that 1,015 grant files contained sufficient documentation to support the businesses had no more than 50 full-time employees. We also noted that 14 grant files did not contain sufficient documentation such as 941 payroll tax forms, payroll registers, or LA unemployment tax forms to support the number of employees.

3d. Procedure

Verified the applicant files contained sufficient documentation to support that single-employee businesses were sellers of tangible goods.

[4] BRGL program affected parishes include Acadia, Allen, Beauregard, Calcasieu, Cameron, Iberia, Jefferson, Jefferson Davis, Lafourche, Orleans, Plaquemines, St. Bernard, St. Charles, St. John the Baptist, St. Mary, St. Tammany, Tangipahoa, Terrebonne, Vermilion, and Washington.

Finding

The program guidelines failed to clearly define the meaning of "sellers of tangible goods." Therefore, if business owners produced evidence of selling even one item, they were considered eligible for the program. During our review, we noted that 352 grant files contained sufficient documentation to support the single-employee businesses sold tangible goods and 35 grant files did not. This procedure did not apply to 642 grant files because they were not single-employee businesses.

3e. Procedure

Verified the applicant files contained sufficient documentation to support the businesses were located in a qualifying zone.

Finding

The BRGL program guidelines established two zones: Zone A and Zone B. Zone A includes areas that experienced flooding and Zone B includes affected parishes that generally did not experience flooding.[5] During our review, we noted that 1,025 grant files contained sufficient documentation indicating the business was located in a qualifying zone. Four grant files contained documentation supporting that the business was located outside Zone A and B.

3f. Procedure

Verified the applicant files contained sufficient documentation to support that, if the businesses were located in Zone A, they experienced a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006.

Finding

This procedure did not apply to 142 grant files because the businesses were not located in Zone A. During our review, we noted that 702 grant files contained sufficient documentation to support the businesses experienced a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006 if they were located in Zone A and 185 grant files did not. Several factors contributed to the high number of exceptions including:

(1) mathematical errors in the revenue decline calculation where a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006 was not demonstrated;

[5] Zone A includes the parishes of Cameron, Orleans, Plaquemines, and St. Bernard, as well as any other Louisiana areas that flooded from hurricanes Katrina or Rita according to FEMA flood maps.
Zone B includes the parishes of Acadia, Allen, Beauregard, Calcasieu, Iberia, Jefferson, Jefferson Davis, Lafourche, St. Charles, St. John the Baptist, St. Mary, St. Tammany, Tangipahoa, Terrebonne, Vermilion, and Washington.

(2) net income or other figures such as depreciation used for the revenue decline calculation rather than gross revenue; and

(3) alternate quarters or years used for the revenue decline calculation but not supported by a reasonable explanation.

3g. Procedure

Verified the applicant files contained sufficient documentation to support that if the businesses were located in Zone B, they experienced a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006 and a $10,000 tangible loss.

Finding

This procedure did not apply to 891 grant files because the businesses were not located in Zone B. During our review, we noted that 92 grant files contained sufficient documentation to support the businesses experienced a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006 and a $10,000 tangible loss if they were located in Zone B and 46 grant files did not. The 46 exceptions were the result of the factors listed in procedure 3f as well as the failure to demonstrate a $10,000 tangible loss. According to program guidelines, insured and uninsured tangible losses were acceptable in determining the required $10,000 loss.

3h. Procedure

Verified the applicant files contained sufficient documentation to support that the correct grant amount was awarded based on the annual revenue of the business.

Finding

During our review, we noted that 844 grant files contained sufficient documentation to support that the correct grant amount was awarded based on the annual revenue of the businesses and 185 grant files did not. According to program guidelines, the grant award is based on annual revenue. LED determined the award amount through the use of its computer system, Sage. The intermediaries entered quarterly (in most cases) revenue information into Sage to determine the 30% revenue decline criterion. The amount entered for 2005 was then automatically adjusted to reflect an annual figure. The award was then determined based on the calculated annual amount. Often times the calculated annual revenue figures were not consistent with other information available in the hard copy files resulting in incorrect award amounts.

4. Procedure

Verified that if the applicants chose to use a quarter other than the second quarters of 2005 and 2006 for the revenue decline criterion, those applicants provided a signed explanation for why those quarters were not representative of their business as provided for in program policy.

Finding

Signed statements explaining why the second quarters of 2005 and 2006 were not representative of the business were provided for 163 grant files and were not provided for 51 grant files. We initially expected to find signed statements from applicants explaining why an alternate quarter was more representative of the normal business operations; however, in many cases the signed application for the program was used as the signed statement. However this is problematic because, in some cases, the applications appeared to be modified by someone other than the applicant.

5. Procedure

Verified that if applicants claimed all their records were destroyed, a signed statement of explanation attesting to a 30% revenue loss was provided.

Finding

Program guidelines do not clearly define when an attestation is acceptable leaving this guideline open to interpretation. Attestation issues are discussed in the additional information section of this report. However, during our review, we noted that signed statements of explanation attesting to the loss of records and a 30% revenue loss were provided for 22 grant files and were not provided for two grant files.

6. Procedure

Verified that in the absence of other documentation for all other program criteria, the applicants provided a signed statement of explanation attesting they met the specified criteria.

Finding

As mentioned previously, program guidelines do not clearly define when an attestation is acceptable leaving this guideline open to interpretation. Attestation issues are discussed in the additional information section of this report. During our review, we noted that 66 grant files contained signed statements of explanation attesting that the applicant met the specified criteria and five grant files did not.

We reviewed 1,029 grant files totaling $18,126,387. As a result of the procedures performed, we identified 112 grant files totaling $1,739,597 that do not appear to meet the requirements of the program and therefore are ineligible for the grant award. We also identified 118 grant files totaling $2,097,711 where eligibility could not be determined based on the documentation in the file and 66 files where the applicant appeared to be eligible for the grant although some documentation was missing from the file. We provided these results to OCD, LED, and the intermediaries who were given an opportunity to resolve the issues.

OCD, LED, and the intermediaries were able to obtain additional documentation demonstrating that 57 of the applicants initially identified as ineligible or where eligibility could not be determined are eligible for the program. In addition, OCD, LED, and the intermediaries were able to gather documentation to support the award decision for 50 grant files that were initially missing documentation.

After considering all of the additional information, we determined that 187 businesses still do not appear to be eligible for the grants they received. Those grant awards total $3,154,689. More detailed results from the initial review are located at Appendix A.

Business Recovery Grant and Loan Program: Loans

We reviewed 86 loan files totaling $6,968,500 prepared by the BRGL program intermediaries. Since standard underwriting guidelines were not established, the intermediaries were directed to use their own underwriting criteria. We conducted the following procedures to verify that loans granted were in compliance with the program guidelines and properly documented:

1. Procedure

   Verified the intermediaries completed the BRGL loan file review checklist.

   Finding

   During our review, we noted that 80 loan files contained a completed BRGL loan file review checklist and six loan files did not.

2. Procedure

   Verified the intermediaries complied with the specific BRGL program underwriting standards established by HUD and in accordance with the corresponding intermediaries' policies.

   Finding

   During our review, we noted that 68 loan files complied with the underwriting standards established by HUD and were in accordance with the corresponding intermediaries' policies and 18 loan files did not.

3. Procedure

Verified the electronic files maintained by LED were consistent with the hard copy files maintained by the intermediaries.

Finding

During our review, we noted that 83 electronic files maintained by LED were consistent with the corresponding hard copy loan files maintained by the intermediaries and three electronic files were not.

4a. Procedure

Verified the applicant files contained sufficient documentation to support that the businesses were operating[6] six months prior to the storm.

Finding

During our review, we noted that 85 loan files contained sufficient documentation to support that the businesses were operating[7] six months prior to the storm and one loan file did not.

4b. Procedure

Verified the applicant files contained sufficient documentation to support that the businesses reopened or demonstrated the potential to reopen.

Finding

During our review, we noted that 86 loan files contained sufficient documentation to support the businesses were reopened or demonstrated the potential to reopen.

4c. Procedure

Verified the applicant files contained sufficient documentation to support the businesses had no more than 50 full-time employees.

Finding

During our review, we noted that 84 loan files contained sufficient documentation to support the businesses had no more than 50 full-time employees and two loan files did not.

[6] Legally registered or in business as defined by program guidelines.
[7] Legally registered or in business as defined by program guidelines.

4d. Procedure

Verified the applicant files contained sufficient documentation to support that single-employee businesses were sellers of tangible goods.

Finding

During our review, we noted that 18 loan files contained sufficient documentation to support that the single-employee businesses were sellers of tangible goods and one grant file did not. This procedure did not apply to 67 loan files.

4e. Procedure

Verified the applicant files contained sufficient documentation to support that the businesses were located in an affected parish.[8]

Finding

During our review, we noted that 86 loan files contained sufficient documentation indicating that the businesses were located in an affected parish.

4f. Procedures

Verified the applicant files contained sufficient documentation to support that the businesses experienced a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006.

Finding

During our review, we noted that 64 loan files contained sufficient documentation indicating that the businesses experienced a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006 and 22 loan files did not.

4g. Procedure

Verified the applicant files contained sufficient documentation to support that the correct loan amount was awarded based on the businesses' demonstrated need and ability to repay.

[8] BRGL program affected parishes included Calcasieu, Cameron, Jefferson, Orleans, Plaquemines, St. Bernard, St. Tammany, Vermilion, Acadia, Allen, Beauregard, Iberia, Jefferson Davis, Lafourche, St. Charles, St. John the Baptist, St. Mary, Tangipahoa, Terrebonne, and Washington.

Finding

As mentioned earlier, the intermediaries were allowed to use their own underwriting guidelines. As a result, various types of cash flow analyses were used to determine a business' ability to repay the loan. Many of the cash flow analyses did not demonstrate the ability of the business to repay the loan because of apparent overstatement of projected income or understatement of projected expenses.

During our review, we noted that 60 loan files contained sufficient documentation to support the loan amount awarded and 26 loan files did not.

4h. Procedure

Verified the applicant files contained sufficient documentation to support that all principals with more than 10% ownership had signed a personal guarantee.

Finding

During our review, we noted that 84 loan files contained a signed personal guarantee for all principals with more than 10% ownership and two loan files did not.

5. Procedure

Verified that if the applicants chose to use quarters other than the second quarters of 2005 and 2006 for the revenue decline criterion, the applicants provided a signed explanation for why those quarters were not representative of their businesses.

Finding

Signed statements explaining why the second quarters of 2005 and 2006 were not representative of the business were provided for 14 loan files and were not provided for five grant files.

6. Procedure

Verified that if applicants claimed all their records were destroyed, a signed statement of explanation attesting to a 30% revenue loss was provided.

Finding

This procedure did not apply to any loan files in the sample.

7. Procedure

Verified that in the absence of other documentation for all other program criteria, the applicants provided a signed statement of explanation attesting they met the specified criteria.

Finding

During our review, we noted that for the one file where this procedure was applicable, a signed statement of explanation attesting that the applicant met the specified criteria was provided.

We reviewed 86 loan files totaling $6,968,500. As a result of the procedures performed, we identified 20 loan files totaling $1,785,000 that did not appear to meet the requirements of the program and therefore were ineligible for the loan. We also identified 14 files totaling $975,000 where eligibility could not be determined based on the documentation included in the file and five files where the applicant appeared to be eligible for the loan although some documentation was missing from the file. We provided these results to OCD, LED, and the intermediaries who were given an opportunity to resolve the issues.

OCD, LED, and the intermediaries were able to obtain additional documentation demonstrating that seven of the applicants initially identified as ineligible or where eligibility could not be determined are eligible for the program. In addition, OCD, LED, and the intermediaries were able to gather documentation to support the award decision for four loan files that were initially missing documentation.

After considering all additional information, we determined that 28 businesses still do not appear to be eligible for the loans they received. Those loans total $2,240,000.

Additional Information

During the application of these procedures, additional information came to our attention that we want to bring to management's attention.

Attestation

BRGL program guidelines allowed applicants to provide signed statements of explanation attesting to a 30% revenue loss between the second quarter of 2005 and the second quarter of 2006. Signed statements were also accepted as evidence for other criteria in the absence of other documentation. Attestations were used to approve 135 grant and loan files for funding. Because attestations are not always reliable, we recommended that OCD and LED revise the program guidelines to exclude applicant attestations except where the applicant demonstrates that all their records were lost and use only reliable supporting documentation to support grant and loan eligibility and awards. LED and OCD are currently working to revise the program guidelines for the second phase of the program. Under these guidelines, attestations are not an acceptable method for documenting program eligibility.

In phase two, attestations should not be necessary to demonstrate the revenue decline criterion because the decline determination will be calculated by comparing the annual decline between 2004 and 2006 as demonstrated through tax returns. Applicants can request these records from the Department of Revenue which will help to alleviate the missing records problem. In special circumstances, eligibility will be determined by LED and OCD on a case-by-case basis.

Sage CRM Database

The Sage Customer Relationship Management (CRM) database is used by OCD and LED to manage BRGL applications. Since the intermediaries did not consistently update the database, the only readily available means to determine which loans are closed, which grants only received the first half of the grant payment, and which applicants received both grant payments by October 31, 2007, is through the intermediaries.

We determined the population of grants using the invoices for the second payment. Only by direct feedback from the intermediaries were we able to obtain the population of closed loan files and grants where only the first half of the grant payment had been made. However, we were not able to determine if these lists were complete.

For Phase II, LED is planning to make changes that will increase the reliability of the Sage CRM database. If changes are not made to increase the reliability of the database, program administrators could potentially be hindered in making eligibility and award decisions due to inaccurate data in the electronic files and limited availability of hard copy files.

We were not engaged to and did not conduct an examination, the objective of which would be to express an opinion on OCD's compliance with federal and state regulations, OCD's internal control over compliance with federal and state regulations, or OCD's financial statements. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters may have come to our attention that would have been reported to you.

This report is intended primarily for the information and use of OCD and LED. However, by provisions of state law, this report is a public document and has been distributed to the appropriate public officials.

Respectfully submitted,

Steve J. Theriot, CPA
Legislative Auditor

DP:JM:sr

BRGL

Engagement Results

Business Recovery Grant & Loan Program: Grant Results

	Total Y	Total N	Total NA	Grand Total	% Requirement Not Met
Has intermediary completed the BRGL Grant File Review Checklist?	967	62	-	1029	6.0%
Does the information in the electronic file (LED) agree to the hard copy file?	849	180	-	1029	17.5%
Business was in business six months prior to the storm (legally registered)?	1003	26	-	1029	2.5%
Business reopened or has demonstrated the potential to reopen?	990	39	-	1029	3.8%
Business had no more than 50 full-time employees?	1015	14	-	1029	1.4%
Single employee business was seller of tangible goods?	352	35	642	1029	3.4%
Business was located in a Qualifying Zone (Zone A or B)?	1025	4	-	1029	0.4%
If located in Zone A, business experienced a 30% decline in gross revenue between the 2nd quarters of 2005 and 2006?	702	185	142	1029	18.0%
If located in Zone B, business experienced a 30% decline in gross revenue between the 2nd quarters of 2005 and 2006 *AND* a $10,000 tangible loss?	92	46	891	1029	4.5%
The correct grant amount was awarded based on the annual revenue of the business?	844	185	0	1029	18.0%
If applicant chose a quarter other than the 2nd quarters of '05 and '06 for revenue decline, has applicant provided a signed statement of explanation for why those quarters are not representative of their business?	163	51	815	1029	5.0%
If applicant's records have been destroyed, has the applicant provided a signed statement of explanation attesting to a 30% revenue loss?	22	2	1005	1029	0.2%
In the absence of other documentation for all other program criteria, did applicant provide a signed statement of *explanation* attesting that they met the specified criteria?	66	5	958	1029	0.5%

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Business Recovery Grant & Loan Program: Loan Results

	Total Y	Total N	Total NA	Grand Total	% Requirement Not Met
Has intermediary completed the BRGL Loan File Review Checklist?	80	6	-	86	7.0%
Has intermediary complied with the specific BRGL program underwriting standards est. by the corresponding intermediary?	68	18	-	86	20.9%
Does the information in the electronic file (LED) agree to the hard copy file?	83	3	-	86	3.5%
Business was in business six months prior to the storm (legally registered)?	85	1	-	86	1.2%
Business reopened or has demonstrated the potential to reopen?	86	0	-	86	0.0%
Business had no more than 50 full-time employees?	84	2	-	86	2.3%
Single employee business was seller of tangible goods?	18	1	67	86	1.2%
Business was located in an affected parish?	86	0	0	86	0.0%
Business experienced a 30% decline in gross revenue between the 2nd quarters of 2005 and 2006?	64	22	0	86	25.6%
The correct loan amount was awarded based on the business' demonstrated need and ability to repay?	60	26	0	86	30.2%
All principals of companies with more than 10% ownership have a signed personal guarantee?	84	2	-	86	2.3%
If applicant chose quarters other than the 2nd quarters of '05 and '06 for revenue decline, has applicant provided a signed statement of explanation for why those quarters are not representative of their business?	14	5	67	86	5.8%
If applicant's records have been destroyed, has the applicant provided a signed statement of explanation attesting to a 30% revenue loss?	-	-	86	86	0.0%
In the absence of other documentation for all other program criteria, did applicant provide a signed statement of *explanation* attesting that they met the specified criteria?	1	-	85	86	0.0%

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Management's Response

BOBBY JINDAL
GOVERNOR

ANGELE DAVIS
COMMISSIONER OF ADMINISTRATION

State of Louisiana

Division of Administration
Office of Community Development
Disaster Recovery Unit

July 1, 2008

Mr. Steve J. Theriot, CPA
Legislative Auditor
Office of the Louisiana Legislative Auditor
1600 N. Third St.
P.O. Box 94397
Baton Rouge, LA 70804-9397

RE: Application of Agreed-Upon Procedures
Business Recovery Grant and Loan Program

Dear Mr. Theriot:

The Division of Administration, Office of Community Development (OCD) appreciates the opportunity to respond to the findings by the Louisiana Legislative Auditor (LLA), Recovery Assistance Division (RAD) in its agreed-upon procedures report on the State's Business Recovery Grant and Loan (SBGL) program. The OCD contracted with the RAD to perform and report on a number of agreed-upon procedures in order for OCD to evaluate the operations of the SBGL program.

OCD concurs with the findings and recommendations of the RAD.

OCD has received, reviewed, and enclosed the Louisiana Economic Development's (LED) response to the findings contained in the agreed-upon procedures report. OCD will continue to work closely with LED to develop an appropriate corrective plan of action to address each of the findings and recommendations contained in the report.

We greatly appreciate the cooperation and diligence of your staff in conducting this engagement. If you have any questions or require additional information, please let me know.

Sincerely,

Paul Rainwater
Senior Executive Director
Office of Community Development/DRU

PR/SU

Enclosure

c: Ms. Angele Davis
Ms. Sharon Robinson
Ms. Susan Elkins
Mr. Thomas Brennan
Mr. Richard Gray
Mr. Stephen Upton

BOBBY JINDAL
GOVERNOR

STEPHEN MORET
SECRETARY

State of Louisiana

LOUISIANA ECONOMIC DEVELOPMENT

June 30, 2008

Paul Rainwater
Executive Director
Louisiana Recovery Authority
150 Third Street, Suite 200
Baton Rouge, Louisiana 70801

Dear Mr. Rainwater:

This is in response to the Legislative Auditors' evaluation of the Business Recovery Grant and Loan Program. LED appreciates the professionalism and thoroughness of the staff of the Office of Legislative Auditor (LLA), and feels that through our joint effort, we have built an even better Phase II of the program.

16 months after the storms, Louisiana's small businesses, the backbone of the economy, were in deep crisis. Over 80,000 had been impacted by Katrina and Rita, and thousands were on the verge of shutting down due to the slow return of markets and the lack of other support(e.g., SBA loans). Because this was seen as an emergency, Louisiana Economic Development (LED) was asked by the governor to quick-launch a pilot initiative - the Business Recovery Grant and Loan Program, Phase I (BRGL P1) - in a period of weeks. LED was not afforded the months typically allowed to plan and organize a program of this magnitude. Nevertheless, LED is proud of the critical and substantive assistance that the BRGL P1 delivered to thousands of worthy businesses across Louisiana.

Although LED may have some differences of interpretation, it does agree with the future-oriented recommendations of the LLA, and has implemented them. LED looks forward to continuing to work with the LLA and OCD, as well as the Louisiana Recovery Authority (LRA) on the BRGL P2, so we can continue to serve the needs of the small business community of our State as it recovers from the devastating effects of the storms.

BACKGROUND

The Business Recovery Services division of Louisiana Economic Development was established in the fall of 2006 to manage a $38M loan program "Small Firm Loan and Grant" (SFLG) and a $9.5M technical assistance program. The loan program would have served perhaps 400 businesses. With a staff of five (2-3 dedicated to the SFLG) Business

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Recovery Services would have had adequate resources to develop, implement and monitor these two programs.

In December 2006, after hearing first-hand of the need, Governor Blanco determined to transform the SFLG into a majority grant program, the "Louisiana Business Recovery Grant and Loan Program." Business Recovery Services was suddenly asked to manage a program that would now be $143M in size, and would directly involve approximately 6,500 businesses – **over a 15 times explosion in size.**

Original Program (SFLG)	New Program (BRGL)	Change
$38M	$143M	**3.5x growth**
~400 awards	~6,500 awards	**16x growth**

[It should be noted that the intermediaries responded to the original RFP for the SFLG (predominantly) loan program, not the BRGL P1 (predominantly) grant program. Given the massively increased demands of the BRGL P1, four of the eleven chosen intermediaries actually dropped out of the program; the remaining seven made significant efforts to staff-up and redeploy resources in order to successfully deliver for their constituents and the state of Louisiana. It should also be noted here that LED had not signed a contract with any of the intermediaries when the program began.]

Until September, 2007 the total number of individuals in Business Recovery Services remained at five, with 2.5 FTEs working on the BRGL P1 on a daily basis (0.5 Director + 1 Program Manager + 3x0.5 support staff). LED performed as much monitoring as possible with a single program manager. Also, because of limited resources, LED relied on a "train-the-trainer" methodology, whereby program leads from each intermediary were trained, and then asked to train their staff. Phase 1 program materials, developed by LED and reviewed and accepted by OCD, included:

- BRGL Application Process Overview
- BRGL Funding Process Overview
- BRGL Application Checklist
- BRGL Eligibility Checklist
- BRGL Grant Application
- BRGL Loan Underwriting Checklist
- BRGL Program FAQs
- BRGL Workshop and Intake Center Schedule

Additional funds to hire monitoring resources were approved by OCD the week of September 17, 2007. By the end of 2007, LED had increased its BRGL staff from 2.5 to 8 FTEs. To date, the program has 9 FTEs dedicated to the program, including five compliance staff positions.

Now that additional staff has been added, LED has gone beyond the train-the-trainer methodology relied upon in Phase 1. Training sessions for the second phase have been completed at both the general and targeted (intermediary-specific) level.

Documentation Issues

It should be recognized that documentation was an inevitable challenge for a program attempting to serve businesses whose documents, computers, safes, etc. had literally been washed away in a sea of brackish water and mud.

With the above in mind, the spirit of the program, as conceived by the LRA, was to direct funds to a set of worthy, viable businesses, by employing a set of substantive – but flexible and inclusive – documentation requirements.

Ultimately, many of the documentation issues come down to interpretation of the guidelines. To address some of the particular documentation issues noted:

- The issue with file documentation for the 30% decline was not necessarily one of missing documentation, but clarity. That is, it may have been difficult to understand how the calculation was made – but the underlying documentation was indeed present (This has been addressed with the Grant File Review Sheet) [31 files]
- It was always the intention of both OCD and LED that the application, itself, could be used as a statement of explanation, and a separate sheet of paper was not necessary. The LLA seemed to have a different, much more literal interpretation.
- It was not required in the Guidelines for the grant to prove 51% ownership (while acknowledging it was in the original action plan) [24 files]
- There is no specifically required documentation for businesses that had not yet reopened to prove their potential to re-open [13 files]

Based upon results of the initial LLA and OCD audits, LED and OCD established a set of actions that are summarized in the action plan, from August 17, 2007 (SEE BELOW). LED aggressively implemented these agreed-upon actions with OCD to remediate any documentation and other issues from the first phase of the program. These actions are summarized in the below plan, from August 17, 2007:

ACTION PLAN

Note: all intermediaries will be given a template to assist in their file review, and each intermediary will be given specific advice as to issues of particular importance. With this in mind, the below plan is based on the assumption that intermediaries now have a clearer understanding what adjustments have to be made; what additional documentation is required; and, what types of business pose particular problems and will make the appropriate corrections before submission.

Group 1) Intermediaries: ASI, JEDCO, RLC, Seedco
• Invoices will be processed and paid for grants as submitted
• Intermediaries will have responsibility to certify that all files submitted are complete and accurate
• LED/OCD will conduct an initial audit of 20% of submitted files in order to verify compliance

Group 2) Intermediary: NewCorp
• Intermediary will have responsibility to certify that all files submitted are complete and accurate
• LED/OCD will conduct an audit of 50% of submitted files in order to verify compliance
• Following satisfactory audit results (>95%), invoices will be processed and paid for grants as submitted
• If audit results are not satisfactory, audit percentage will move to 100%

Group 3) Intermediaries: ARDD, SCPD
• Intermediaries will have responsibility to certify that all files submitted are complete and accurate
• LED/OCD will conduct an audit of 100% submitted files in order to verify compliance
• Invoices will be processed and paid for grants as cleared by the audit

Original Invoice #13, $5.1M
• OCD will reimburse LED for this invoice at the following rates:
- RLC 99%
- JEDCO 96%
- ASI 93%
- Seedco 80%

• The balance on the above percentages will be paid upon an audit of the files that results in a >95% confidence rate
• OCD will reimburse LED for ARDD, NewCorp and SCPD following a 100% review of the files, net of amounts for ineligible files and award adjustments

Loans
• Loans will be reviewed by OCD/LED for:
- Eligibility
- Viability
- Adherence to intermediaries' individual underwriting guidelines (to be provided)

• Loans will initially be reviewed according to DOA survey tables, percentage may be decreased as compliance is demonstrated

General Notes
• Intermediaries will receive specific instructions and assistance to address any problems determined in the first audit, including consulting before submission
• Seedco will indicate which files need to be adjusted in Sage to account for seasonality

• Based on performance in audits, at the discretion of OCD and LED, an intermediary's status may be changed from requiring the audit pre- versus post- invoice payment
• Attestations bearing on eligibility issues must be specific to the issue and in writing from the applicant. Statements of explanation must have a "because" clause stating the reason or facts for the attestation
• When OCD/LED is conducting the review, files will be looked at once and their status will be determined on that one review
* * * * *

LED, with its increased compliance staff and in partnership with OCD, has reviewed between 20% and 100% of each intermediary's program files, in order to ensure that files were complete and accurate.

Despite the challenges, LED feels that roles and responsibilities have now been clarified, and expects good interagency coordination going forward.

CONCLUSION

With the benefit of additional time and resources, LED has refined policies and procedures from the first phase of the BRGL. For the second phase, which began June 9, 2008, LED has instituted the following:

- A formal policy change procedure in the event of any necessity of change, involving OCD, LRA and LED
- A comprehensive set of formal eligibility requirements, implementation procedures, and other relevant policies
- A full training schedule, for not only intermediary leadership, but staff, as well.
- A full monitoring plan, including Performance, Financial, Capacity and general CDBG monitoring.

In conjunction with OCD, LED developed a 40-page, comprehensive, forward-looking monitoring plan, which includes:

- **Performance Monitoring**: Is the intermediary following program guidelines and procedures?
- **Financial Monitoring**: Does the intermediary have proper financial processes and controls in place?
- **Capacity Monitoring**: Does the intermediary have sufficient capacity to perform the above, and can it benefit from additional technical assistance?
- **Additional CDBG Monitoring**: Are all HUD CDBG regulations (e.g., procurement) being followed?

The comprehensive formal policies and procedures established for the second phase include:

- **Intermediary capacity requirements**
- **Grant eligibility requirements**
- **Use of grant proceeds**
- **Application review process**
- **Award disbursement process**
- **Intermediary fees and responsibilities**
- **LED monitoring plan, including CDBG requirements**
- **Organizational roles and responsibilities**

Overall, LED is confident that the plans now in place will ensure that issues raised by the performance audit are being addressed. Importantly, the documentation issues that have been found have been and/or are being rectified by the intermediaries according to LED's plan. This ensures that all files are ultimately complete and accurate.

Sincerely,

Fran Gladden

Fran Gladden
Undersecretary, LED

AUDIT FINDINGS

LED agrees with some of the findings, and all of the recommendations, made by the auditors. However, it is important to note that the challenges faced at the onset of the program greatly affected the overall findings.

A. Business Recovery Grant Program

1. Finding

Due to complications during the initial stages of the program, OCD and LED implemented a policy whereby the intermediaries were required to complete a checklist to document that they had gathered all of the appropriate documentation to support the funding decision. During our review, we noted that 967 grant files contained a completed BRGL grant file review checklist. We also noted that 62 grant files:

- contained a checklist completed by LED or OCD instead of the intermediary;
- contained an incomplete grant checklist; or
- did not contain a checklist.

Response- Partially Agree

Some of the files were reviewed by the LLA before the intermediaries had the opportunity to go back and complete file review sheets.

The policy implemented by OCD and LED was agreed upon on August 17, 2007. The intention of the plan was for the intermediaries to be "forward-facing" by completing the file review sheets and reviewing files as the 2nd disbursement requests were submitted. Over half (54%) of the files reviewed during this audit were "Invoice 13" files, which were paid both 1st and 2nd disbursement prior to the initial LLA Audit, the OCD/LED audit and the August 17th processing plan agreed upon by OCD and LED. An additional 40 files (4%) belonged to the sub-set of files that did not request 2nd disbursement.

While it was important for the "Invoice 13" files to be reviewed and properly documented, it was more important to assist the hundreds of businesses who had submitted 2nd disbursement requests during the audit process and had been waiting months for additional funds. When the audit began in October 2008, the intermediaries' resources were devoted to improving those files pending receipt of the 2nd disbursement. The intermediaries have continued to gather additional information files are being reviewed.

Phase II of the program requires that an Underwriting and File Review Checklist be completed and placed in each file prior to disbursing funds. LED has also implemented a comprehensive monitoring plan which includes a sample review of files prior to invoicing.

2. Finding

The hard copy files are maintained by the seven intermediaries in offices located in New Orleans, Lafayette and Houma. Since LED and OCD do not have immediate access to the hard copy files, they must rely upon the electronic file to make programmatic decisions. In order to make sound decisions the files must be accurate. During our review, we noted that 849 electronic files maintained by LED were consistent with the corresponding hard copy grant files maintained by the intermediaries. For the remaining 180 electronic files one or more fields in the electronic file were not consistent with the hard copy file, which could be problematic due to the limited accessibility of the hard copy files.

Response- Partially Agree

At the onset of the program, the intermediaries were instructed to input all pertinent information for each applicant into the LED database system, SAGE. While LED acknowledges that there were some errors made during input, the vast majority of discrepancies between the SAGE file and the hard copies were a result of additional information requested and received by the intermediaries from the business owners during review of the files. The intermediaries were instructed by LED not to make changes in SAGE after the initial decision was made so that the system would not be affected by frequent and undocumented changes. Since all pending files were reviewed prior to 2nd disbursement, the intermediaries ensured that all files met the eligibility requirements, despite possible incorrect information entered in SAGE.

Per the Cooperative Endeavor Agreements between the intermediaries and LED, the intermediaries are required to furnish access to its books, records and accounts to OCD, LED, HUD or any other authorized Federal officials.

For Phase II, LED has implemented a process in which the database manager will perform periodic checks of the SAGE system by intermediary to uncover possible input errors and inconsistencies.

3a. Finding

During our review, we noted that 1,003 grant files contained sufficient documentation indicating the businesses were operating (legally registered or in business as defined by program guidelines) six months prior to the storm. This includes start-up businesses, which are an exception to this guideline. Start-up businesses that were legally registered six months before the storm, but were not yet operating, were eligible for the minimum grant award of $10,000. We noted that 26 grant files did not contain sufficient documentation such as articles of incorporation, secretary of State registration, income statements, 2004 or prior tax returns, or a business license to demonstrate that the business was operating or legally registered at least six months prior to the storm.

Response- Disagree

At the onset of the program, there was no required documentation to prove that a business was legally operating prior to the storm – just the attestation on the application. Once guidelines were in place, the intermediaries took steps to gather information, resulting in a minimal number of files missing this documentation.

Phase II has a clear set of documentation requirements that must be met for an application to be accepted by the intermediary. Once accepted, the file is included in the sample of files to be reviewed by LED during the monitoring process.

3b. Finding

According to program policy, the businesses are required to reopen or plan to reopen in one of the 20 affected parishes[1] to be eligible for the program. During our review, we noted that 990 grant files contained sufficient documentation indicating the businesses reopened or demonstrated the potential to reopen and 39 grant files did not. Included in the 39 are five grant files that indicated the applicant planned to open a different type of business than the pre-storm business and four files that indicated the business relocated outside the affected area.

Response- Disagree

The initial guidelines to the program did not contain a specific definition or requirement for "viability". It was later determined that the business needed to prove that they were open or planned to reopen in one of the affected parishes in order to receive the second disbursement, with no specific documentation required to provide that proof. A statement included on the second disbursement request form that the business would reopen was acceptable. There is currently no requirement that a business needs to be reopen to receive the first disbursement.

The guidelines for Phase II have been revised by requiring that businesses must be open at the time of the application appointment in order to be considered for the award.

3c. Finding

During our review, we noted that 1,015 grant files contained sufficient documentation to support the businesses had no more than 50 full-time employees. We also noted that 14 grant files did not contain sufficient documentation such as 941 payroll tax forms, payroll registers, or LA unemployment tax forms to support the number of employees.

Response- Disagree

At the onset of the program, there was no required documentation to prove the number of employees. Once documentation guidelines were in place, the intermediaries took steps to gather information, resulting in a minimal number of files missing this ex post facto documentation.

Phase II has a clear set of documentation requirements that must be met for an application to be accepted by the intermediary. Once accepted, the file is included in the sample of files to be reviewed by LED during the monitoring process.

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[1] BRGL program affected parishes include Calcasieu, Cameron, Jefferson, Orleans, Plaquemines, St. Bernard, St. Tammany, Vermilion, Acadia, Allen, Beauregard, Iberia, Jefferson Davis, Lafourche, St. Charles, St. John the Baptist, St. Mary, Tangipahoa, Terrebonne, and Washington.

3d. Finding

The program guidelines failed to clearly define the meaning of "sellers of tangible goods". Therefore, if a business owner produced evidence of selling even one item, they were considered eligible for the program. During our review, we noted that 352 grant files contained sufficient documentation to support the single-employee businesses sold tangible goods and 35 grant files did not. This procedure did not apply to 642 grant files because they were not single-employee businesses.

Response- Disagree

This is not true. A tangible good was interpreted literally, that is, a good with physical substance (as opposed to a service). There was no minimum threshold for this requirement. That was the clear requirement.

Further, the intermediaries in some cases used a "common sense" approach to making the determination. For example, a beauty salon was assumed to sell hair products to clients, although the tax returns did not specify cost of goods sold. The auditors required hard proof of these common-sense assumptions that in some cases was not provided. In Phase II, the requirement that single-employee business sell tangible goods has been eliminated.

3e. Finding

The BRGL program guidelines established two zones - Zone A and Zone B. Zone A includes areas that experienced flooding and Zone B includes affected parishes that generally did not experience flooding.[2] During our review, we noted that 1,025 grant files contained sufficient documentation indicating the business was located in a qualifying zone. Four grant files contained documentation supporting that the business was located outside Zone A and B.

Response- Agree

Phase II has a clear set of documentation requirements that must be met for an application to be accepted by the intermediary. Once accepted, the file is included in the sample of files to be reviewed by LED during the monitoring process.

3f. Finding

This procedure did not apply to 142 grant files because the businesses were not located in Zone A. During our review, we noted that 702 grant files contained sufficient documentation to support the businesses experienced a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006 if they were located in Zone A and 185 grant files did not. Several factors contributed to the high number of exceptions including:

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[2] Zone A includes the parishes of Cameron, Orleans, Plaquemines, and St. Bernard, as well as any other Louisiana areas that flooded from hurricanes Katrina or Rita according to FEMA flood maps.
Zone B includes the parishes of Calcasieu, Jefferson, St. Tammany, Vermilion, Acadia, Allen, Beauregard, Iberia, Jefferson Davis, Lafourche, St. Charles, St. John the Baptist, St. Mary, Tangipahoa, Terrebonne, and Washington.

- mathematical errors in the revenue decline calculation where a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006 was not demonstrated;
- net income or other figures such as depreciation used for the revenue decline calculation rather than gross revenue; and
- alternate quarters or years used for the revenue decline calculation but not supported by a reasonable explanation.

Response- Partially Agree
While LED acknowledges that there were mathematical and other errors made by the intermediaries, over half of the files that did not meet this criterion was a result of alternate periods used or alternate calculation methods. An acceptable explanation for the use of an alternate quarter to calculate the revenue decline was not clearly defined in the guidelines. Intermediaries also used alternate means to calculate the decline for certain seasonal industries, such as fishing.

For example, one business had a 70% decline in Q1, a 29% decline in Q2 (for a 50% average decline, well above the 30% threshold), but was deemed ineligible by the LLA.

It is also important to note that two of the five intermediaries accounted for nearly half of the total number of exceptions, indicating that the majority of the intermediaries performed well in this category.

Phase II has been simplified by reducing the decline percentage from 30% to 20% and requiring that the decline be calculated based on annual tax returns only. LED has also instituted an exceptions request process, whereby intermediaries who demonstrate a strong case for an exception to the general policy may submit an exceptions request, which must be approved by LED and OCD.

3g. Finding
This procedure did not apply to 891 grant files because the businesses were not located in Zone B. During our review, we noted that 92 grant files contained sufficient documentation to support the businesses experienced a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006 and a $10,000 tangible loss if they were located in Zone B and 46 grant files did not. The 46 exceptions were the result of the factors listed in procedure 3f as well as the failure to demonstrate a $10,000 tangible loss. According to program guidelines, insured and uninsured tangible losses were acceptable in determining the required $10,000 loss.

Response- Partially Agree
As stated in the response for 3f, a large number of the exceptions are attributed to the use of alternate quarters and alternate calculation methods. Two out of five intermediaries account for 67% of the total number of exceptions.

In addition to the above noted changes made to Phase II, the requirement for the proof of a $20,000 tangible loss for Zone B businesses has also been eliminated. All businesses located in any of the ten eligible parishes will now be held to the same set of guidelines.

3h. Finding

During our review, we noted that 844 grant files contained sufficient documentation to support that the correct grant amount was awarded based on the annual revenue of the businesses and 185 grant files did not. According to program guidelines, the grant award is based on annual revenue. LED determined the award amount through the use of their computer system, Sage. The intermediaries entered quarterly (in most cases) revenue information into Sage to determine the 30% revenue decline criterion. The amount entered for 2005 was then automatically adjusted to reflect an annual figure. The award was then determined based on the calculated annual amount. Often times the calculated annual revenue figures were not consistent with other information available in the hard copy files resulting in incorrect award amounts.

Response- Partially Agree

After the start of the program, it was decided that award amount would be based on the pre-storm annual revenue of the business. An assumption was made that annualizing the quarterly figure would be a good way to estimate actual annual revenue. The intermediaries were not required to calculate the award amount. The intermediaries were instructed to enter the calculations in SAGE, which automatically performed the calculations. We acknowledge that SAGE could not calculate every scenario. This was not an error made by the intermediaries.

For Phase II, the award has been changed from a separate grant and loan to a 20% grant and 80% loan combination. The award amount is determined by the intermediary based on need and repayment ability. The maximum total award amount has been reduced from $250,000 in Phase I to $100,000 in Phase II with the ability to increase to $250,000 through the exception process. The maximum grant amount in any case is $20,000.

4. Finding

Signed statements explaining why the second quarters of 2005 and 2006 were not representative of the business were provided for 163 grant files and were not provided for 51 grant files. We initially expected to find signed statements from applicants explaining why an alternate quarter was more representative of the normal business operations; however, in many cases the signed application for the program was used as the signed statement. However this is problematic because, in some cases, the applications appeared to be modified by someone other than the applicant.

Response- Partially Agree

As previously stated, an acceptable explanation for the use of an alternate quarter to calculate the revenue decline was not defined in the guidelines. The auditors interpreted the guidelines to mean that the only acceptable explanation was that the business operated seasonally. OCD and LED interpreted the guidelines more generally and accepted explanations that appeared reasonable. The audit results include several files in which different conclusions were reached by an OCD/LED team and the LLA audit team.

Although we agree that some applications appear to be modified by someone other than the applicant, the signed application was intended to serve as an attestation by OCD and LED.

5. Finding

Program guidelines do not clearly define when an attestation is acceptable leaving this guideline open to interpretation. Attestation issues are discussed in the additional information section of this report. However, during our review, we noted that signed statements of explanation attesting to the loss of records and a 30% revenue loss were provided for 22 grant files and were not provided for two grant files.

and

6. Finding

As mentioned previously, program guidelines do not define when an attestation is acceptable leaving this guideline open to interpretation. Attestation issues are discussed in the additional information section of this report. During our review, we noted that 66 grant files contained signed statements of explanation attesting that the applicant met the specified criteria and five grant files did not.

Response- Agree

Given the critical need for this program and the magnitude of loss, the initial guidelines allowed for the acceptance of attestation to prove a loss. Many businesses had lost all documentation in the storm and were struggling to get their businesses operational.

General Eligibility

It should be noted that the vast majority of that small set of businesses deemed ineligible are still worthy, legitimate businesses that simply did not fit with the program's stringent guidelines (e.g., a fisherman who sustained tens of thousands in losses, but still managed to work in 2006).

As with the documentation issues, some of the ineligible files are due to difference of opinion/interpretation.

Example ineligible files had:

- A Q1-to-Q1 revenue decline of 32%
- A Q2-to-Q2 revenue decline of 29%
- A six-month average revenue decline of 41% with a Q2-to-Q2 revenue decline of 29% [qualifying threshold is 30%]
- A formal letter saying that Q1 was a better comparison for past performance but was deemed ineligible because the letter does not adequately prove seasonality

B. Business Recovery Loan Program

1. Finding

During our review, we noted that 80 loan files contained a completed BRGL loan file review checklist and six loan files did not.

Response- Partially Agree

As noted in the grant section, this was not a requirement at the onset of the program. Since most loans had been funded prior to the initial audit, the intermediaries were focused on closing out pending grant files when this audit took place.

2. Finding

During our review, we noted that 68 loan files complied with the underwriting standards established by HUD and were in accordance with the corresponding intermediaries' policies and 18 loan files did not.

Response- Partially Agree

HUD does not have an existing set of underwriting guidelines. The only guidelines required for this program were established by the individual intermediaries. The majority of the intermediaries involved with this program have long-established underwriting criteria and an overwhelming success rate with other lending programs. Their underwriters are experienced credit risk analysts. The program did not have a mechanism in place for qualifying applicants that did not meet the intermediaries' specific underwriting criteria; therefore, most of them noted the exceptions along with the mitigating reasons for approval.

In Phase II of the BRGL, a minimum set of underwriting criteria has been established. There is also an exceptions request process for approving applicants that do not meet the minimum criteria.

3. Finding

During our review, we noted that 83 electronic files maintained by LED were consistent with the corresponding hard copy loan files maintained by the intermediaries and three electronic files were not.

Response- Partially Agree

Since most loans were funded and closed prior to the audit, most loan files were not reviewed by the intermediaries. This finding was a result of grant files for which additional information had been submitted prior to releasing second disbursement.

Per the Cooperative Endeavor Agreements between the intermediaries and LED, the intermediaries are required to furnish access to its books, records and accounts to OCD, LED, HUD or any other authorized Federal officials.

For Phase II, LED has implemented a process in which the database manager will perform periodic checks of the SAGE system by intermediary to uncover possible input errors and inconsistencies.

4a. Finding

During our review, we noted that 85 loan files contained sufficient documentation to support that the businesses were operating (legally registered) six months prior to the storm and one loan file did not.

and

4b. Finding

During our review, we noted that 86 loan files contained sufficient documentation to support the businesses were reopened or demonstrated the potential to reopen.

and

4c. Finding

During our review, we noted that 84 loan files contained sufficient documentation to support the businesses had no more than 50 full-time employees and two loan files did not.

and

4d. Finding

During our review, we noted that 18 loan files contained sufficient documentation to support that single-employee businesses were sellers of tangible goods and one grant file did not. This procedure did not apply to 67 loan files.

and

4e. Finding

During our review, we noted that 86 loan files contained sufficient documentation indicating that the businesses were located in an affected parish.

Response- Agree

The above findings illustrate the fact that the intermediaries gathered more financial and other documentation used to support repayment ability that also assisted in proving the other eligibility requirements. In Phase II, the documentation requirements have been clearly outlined for the intermediaries.

4f. Finding

During our review, we noted that 64 loan files contained sufficient documentation indicating that the businesses experienced a 30% decline in gross revenue between the second quarter of 2005 and the second quarter of 2006 and 22 loan files did not.

Response- Partially Agree
While LED acknowledges that there were mathematical and other errors made by the intermediaries, over half of the files that did not meet this criterion was a result of alternate periods used or alternate calculation methods. An acceptable explanation for the use of an alternate quarter to calculate the revenue decline was not clearly defined in the guidelines. Intermediaries also used alternate means to calculate the decline for certain seasonal industries, such as fishing.

It is also important to note that one intermediary accounted for over 60% of the loan files deemed ineligible, indicating that the majority of the intermediaries performed well in this category.

Phase II has been simplified by reducing the decline percentage from 30% to 20% and requiring that the decline be calculated based on annual tax returns only. LED has also instituted an exceptions request process, whereby intermediaries who demonstrate a strong case for an exception to the general policy may submit an exceptions request, which must be approved by LED and OCD.

4g. Finding

As mentioned earlier, the intermediaries were allowed to use their own underwriting guidelines. As a result, various types of cash flow analyses were used to determine a business' ability to repay the loan. Many of the cash flow analyses did not demonstrate the ability of the business to repay the loan due to apparent overstatement of projected income or understatement of projected expenses.

During our review, we noted that 60 loan files contained sufficient documentation to support the loan amount awarded and 26 loan files did not.

Response- Partially Agree
While LED agrees that some intermediaries deviated from the stated guidelines in some cases, it is unreasonable for the LLA to question the underwriting of intermediaries who are experts at this work, and typically have a 90%+ repayment rate on loans such as these.

4h. Finding

During our review, we noted that 84 loan files contained a signed personal guarantee for all principals with more than 10% ownership and two loan files did not.

Response- Agree
A signed personal guaranty was required for all 10% or more owners.

5. Finding

Signed statements explaining why the second quarters of 2005 and 2006 were not representative of the business were provided for 14 loan files and were not provided for five grant files.

Response

As previously stated, an acceptable explanation for the use of an alternate quarter to calculate the revenue decline was not defined in the guidelines. The auditors interpreted the guidelines to mean that the only acceptable explanation was that the business operated seasonally. OCD and LED interpreted the guidelines more generally and accepted explanations that appeared reasonable. The audit results include several files in which different conclusions were reached by an OCD/LED team and the LLA audit team.

The signed application was intended to serve as an attestation by OCD and LED.

6. Finding

This procedure did not apply to any loan files in the sample.

and

7. Finding

During our review we noted that for the one file where this procedure was applicable, a signed statement of explanation attesting that the applicant met the specified criteria was provided.

Response- Agree

General

In addition to the responses noted in the grant section, there are several other items worth noting in regards to the loans.

- HUD does not have an existing set of underwriting guidelines. The only guidelines required for this program were established by the individual intermediaries.
- The majority of the intermediaries involved with this program have long-established underwriting criteria and an overwhelming success rate with other lending programs. Their underwriters are experienced credit risk analysts.
- One intermediary accounted for over 60% of the loan files deemed ineligible.

There have been significant changes made to Phase II to address the loan issues, including:

- The establishment of a set of minimum underwriting standards, including a minimum credit score and minimum debt coverage ratio.
- The requirement that lower-performing intermediaries hire a program manager experienced with finance and loan-underwriting.
- An exceptions request process in which the intermediaries must submit requests for exceptions to the standard underwriting guidelines to both LED and OCD.

Going forward LED looks forward to continuing to implement the recommendations of the Office of Legislative Auditors, to ensure that the next phase of the Business Recovery Grant and Loan program continues to be both efficient and compliant. LED is confident that it will have the full partnership of other state agencies in this endeavor, which will provide critical support to the small business community of Louisiana as it continues to recover from the destruction of Katrina and Rita.