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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

P-178250

AUG 6 1973

The Honorable Thomas S. Kleppe, Administrator
Small Business Administration

Dear Mr. Kleppe:

By letter dated March 19, 1973, your Director, Office of Loan Administration, requested our decision as to the propriety of payment by the Small Business Administration (SBA) of the claim of McLachlen National Bank, Washington, D.C., which claim is based on the facts described below. Since the Director does not appear to be an authorized certifying officer he is not entitled to an advance decision by our Office. Cf. 31 U.S.C. 82d. Hence, our reply is being made to you as head of the agency involved, pursuant to 31 U.S.C. 74. See 26 Comp. Gen. 797.

On January 27, 1972, SBA approved an economic opportunity loan to , doing business as Nate's Carry Out Shop in Washington, D.C. Only SBA money was involved in this \$24,000 loan. The money was disbursed to Mr. on three different occasions: on March 8, 1972, in the amount of \$16,166.57; on March 22, 1972, in the amount of \$3,700.00; and on April 21, 1972, in the amount of \$4,133.43.

In order to meet his creditors' demands, Mr. obtained interim financing from McLachlen Bank before and during the disbursement period of the SBA loan: sometime in February 1972 in the amount of \$3,500; on March 3, 1972, for \$1,500; and on March 29, 1972, in the amount of \$2,000. These interim loans were made subsequent to SBA loan approval and with SBA's knowledge. McLachlen in each instance looked to the SBA as a source of repayment. Mr. has repaid \$3,500 and \$1,500 obligations but the \$2,000 loan remains unpaid.

According to the statement by Mr. Clarence H. Chandler, Chief, Financing Division, SBA, the Bank prior to making a loan commitment to Mr. contacted Mr. Chandler to determine whether the SBA had in fact approved a loan to Mr. and requested that the Bank be made a co-payee on the SBA check, to which request SBA agreed. According to Mr. Chandler the Bank was made a co-payee on that SBA disbursement check to Mr. and Mr. paid off his first two interim Bank loans therefrom. In describing the third loan made by the Bank to Mr. , Mr. Chandler states:

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A few days later Mr. _____ again made a request to the Bank for an advance and during his visit to the Bank, I was contacted by the banker with a duplication of the original request [to be made a co-payee of the SBA disbursement check]. I raised the question as to the necessity of the advance since the check would be in within a few days and the urgent needs were satisfied in the prior disbursement. I also informed him that it would delay our disbursement if we would cancel our order for a check and issue a new one to include the bank as a payee.

The banker seemed determined on making the advance in spite of the aforementioned points presented to him and proceeded to make the funds available.

Upon finding this out I made a call to Mr. _____ and impressed upon him the importance of repaying the bank. He agreed that he would do so.

However, Mr. William A. Bryarly, Jr., First Vice President of McLachlen, states the facts with respect to the third loan as follows:

On March 29, 1972 Mr. _____ requested that \$2,000.00 be advanced to be repaid in the same manner as before. I again telephoned Mr. Chandler who agreed to protect the Bank's interest and send a check in joint names.

The SBA has carried out its agreement with regard to the \$3,500.00 and \$1,500.00 loans and the Bank has received payment in full. However, the Bank has not been paid the \$2,000.00 advanced on March 29, 1972 and apparently the funds from the direct SBA loan to Mr. _____ have been disbursed without issuance of the joint check as was promised by Mr. Chandler. The Bank has not dealt directly with Mr. _____ and would not have done business directly with him but for the assurance and promise of Mr. Chandler that the Bank's interests would be protected by payment of the advances at the time of disbursement of the SBA loan.

The Director, Office of Loan Administration states that SBA would like to reimburse the Bank in order to avoid a suit by the Bank and in order to prevent damaged relations with the banking community whose cooperation is, according to the Director, important to SBA's carrying out its responsibilities. The Director states:

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SBA feels that such interim financing by a bank provides significant benefits to our borrowers. During the time SBA is processing a loan application, and between disbursements of an SBA direct loan, interim financing facilities the borrower's operating capital position. Agreement by SBA to interim financing arrangements adds substantial convenience to our lending program. The financial structure of a small business in need of SBA assistance is sometimes marginal, and inevitable delay in loan disbursement by SBA, as lender of last resort, can be irreparably injurious to the small firm. While it is customary to amend an authorized use of SBA loan proceeds in order to accommodate interim financing, the procedure was not followed in this case.

The bank has not taken legal action against SBA to date, pending receipt of your opinion. We would like to avoid such a suit if possible, since the issue is reduced to one of fact and not law. While certainly the matter might be decided either way, experience suggests that, if brought before a jury, such issues are often resolved in favor of the plaintiff rather than the government. Suit avoidance would better serve our interest since the cost of defending such a suit would probably exceed the claim by a considerable sum. Corollary benefits, of course, would be the prevention of damaged relations with the banking community at large and acknowledgement of McLachlen's significant commitment to and involvement in SBA programs.

In addition to whether payment may be certified to the Bank, it is requested that we advise whether such payment, if authorized, may (1) be paid from the Business and Investment Fund (73x4154) and (2) it would be proper to pay accrued interest on the interim loan and, if so, at what rate.

We note that there is a dispute in this case as to whether the SBA, through one of its officials, verbally promised McLachlen that it would be made a co-payee on the final SBA check. The Bank's Executive Vice President, Mr. Bryarly, reports that he was advised that SBA would make the bank co-payee, but it does not appear from Mr. Chandler's statement quoted above that he made such a promise. In his letter the Director reports that SBA believes that a "misunderstanding of the spoken word may well have occurred, to the detriment of McLachlen" This Office is not equipped

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to interview witnesses and to determine credibility; therefore, our policy, in the absence of clear fraud or bad faith, is to accept the version of the facts set forth by the Government agency. Accordingly, we are required to assume that Mr. Chandler, in accordance with his affidavit, did not agree that the Bank would be made co-payee on the loan nor did he purport to commit the SBA to repay the loan to the Bank in the event the borrower did not.

From the record before us we find no basis for concluding that the Small Business Administration is any way obligated to the McLachlen National Bank. Rather, it appears from Mr. Chandler's statement and from the Director's letter to us that the Bank's Executive Vice President was not informed that the Bank would be made a co-payee on the check. From the facts and circumstances disclosed in the Director's letter and in the statements of the SBA officials concerned, we find no evidence which would establish a legal duty on the part of SBA to assure the repayment of Bank's loan through its own independent action.

As we stated in our decision of September 20, 1968, B-164162, ✓ to an SBA authorized certifying officer, while the provisions of section 634(b)(7) ✓ of title 15, U.S.C., grant the Administrator of Small Business broad authorities with respect to dealing with loans, we do not find such authority related to assuming the obligation of a borrower to a third party under the circumstances here involved. Accordingly, we must conclude that no part of McLachlen National Bank's claim may be certified for payment.

Sincerely yours,

PAUL G. DEMBING

For the

Comptroller General
of the United States