



September 2014

EXPORT-IMPORT BANK

Enhancements Needed in Loan Guarantee Underwriting Procedures and for Documenting Fraud Processes

GAO Highlights

Highlights of [GAO-14-574](#), a report to congressional committees

Why GAO Did This Study

Ex-Im serves as the official export credit agency of the United States, providing a range of financial products to support the export of U.S. goods and services. Following the 2007-2009 financial crisis, increased demand for Ex-Im support resulted in significant increases in Ex-Im's outstanding financial commitments and risk exposure, which heightened interest in ensuring that Ex-Im has procedures in place to minimize financial risks.

GAO was mandated by the Export-Import Bank Reauthorization Act of 2012 to review the extent to which Ex-Im (1) adequately designed and implemented procedures to reasonably assure compliance with its underwriting process requirements for loan guarantee transactions and consistency with federal guidance and (2) adequately designed procedures to prevent, detect, and investigate fraudulent applications for loan guarantees. To address these objectives, GAO (1) reviewed Ex-Im's relevant procedures and federal guidance; (2) conducted tests on statistically random samples of loan guarantees authorized between October 1, 2011, and March 31, 2013; and (3) interviewed Ex-Im officials.

What GAO Recommends

GAO is making a number of recommendations to Ex-Im to enhance its loan guarantee underwriting process with additional procedures for ensuring compliance with Ex-Im and federal requirements, as well as for documenting fraud processes. In commenting on GAO's draft report, Ex-Im concurred with GAO's recommendations.

View [GAO-14-574](#). For more information, contact Steve Lord at (202) 512-4379 or lords@gao.gov or Gary Engel at (202) 512-3406 or engel@gao.gov.

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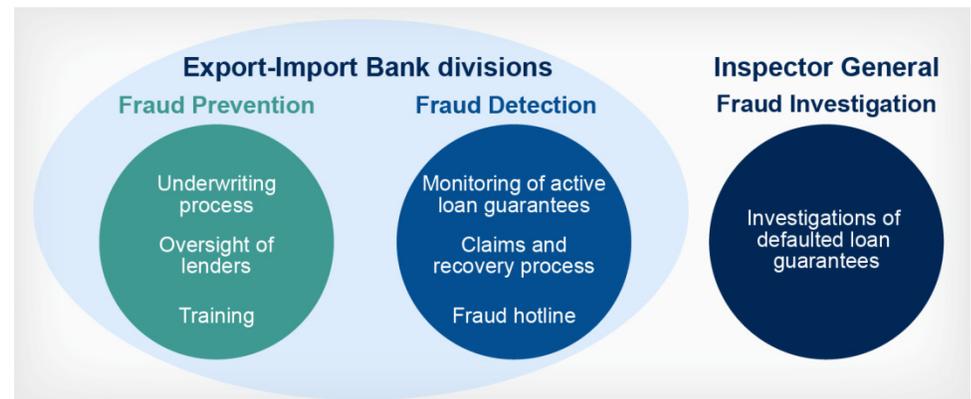
Enhancements Needed in Loan Guarantee Underwriting Procedures and for Documenting Fraud Processes

What GAO Found

The Export-Import Bank's (Ex-Im) *Loan, Guarantee, and Insurance Manual* (Manual) describes Ex-Im's underwriting procedures and generally provides loan officers with a framework to implement its underwriting process requirements for loan guarantee transactions. GAO's review of a statistical sample of loan guarantees indicated that Ex-Im implemented many key aspects of the underwriting process as required by the Manual. However, the Manual did not (1) include certain procedures or sufficiently detailed instructions to verify compliance with Ex-Im's requirements and consistency with federal guidance, such as a procedure to verify that loan guarantee transaction applicants did not have delinquent federal debt; (2) include instructions for loan officers to use credit reports and for the inclusion of all required documents and analyses in the loan file prior to approval; and (3) call for assessments of collateral, as required by federal guidance, for certain loan guarantee transactions prior to approval. Further, Ex-Im did not have mechanisms to verify compliance with certain established procedures, including documenting certain loan guarantee eligibility procedures. In addition, Ex-Im's current risk-based approach for scheduling examinations to monitor lenders with delegated authority to approve guaranteed loans was not documented. Improvements in these areas help enhance the assessment of transaction participant eligibility and the reasonable assurance of repayment, as well as help prevent fraud.

While Ex-Im has processes to prevent, detect, and investigate fraud, Ex-Im has not documented its overall processes for doing so. Such documentation is recommended by several authoritative auditing and antifraud organizations as a key step in evaluating and updating these processes. The processes Ex-Im used to prevent and detect fraud were part of its underwriting and monitoring of loan guarantees. A number of divisions within Ex-Im, as well as lenders, played a role in preventing fraudulent applications from being approved and monitoring activity that could help detect potential fraud. If a guaranteed loan defaults and an indicator of fraud existed, staff would work with Ex-Im's Office of Inspector General to leverage its investigative resources to pursue involved parties.

Key Aspects of Export-Import Bank's Fraud Processes



Source: GAO analysis of Ex-Im information. | GAO-14-574

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Abbreviations

AMD	Asset Management Division
CRC	Credit Review and Compliance Division
ECA	export credit agency
ERC	Enterprise Risk Committee
Ex-Im	Export-Import Bank of the United States
GC	General Counsel
IG	Office of Inspector General
OECD	Organisation for Economic Co-operation and Development
OMB	Office of Management and Budget

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September 9, 2014

The Honorable Tim Johnson
Chairman
The Honorable Mike Crapo
Ranking Member
Committee on Banking, Housing,
and Urban Affairs
United States Senate

The Honorable Jeb Hensarling
Chairman
The Honorable Maxine Waters
Ranking Member
Committee on Financial Services
House of Representatives

The Export-Import Bank of the United States (Ex-Im) serves as the official export credit agency of the United States. It provides a range of financial products, including direct loans, loan guarantees, and insurance for foreign customers of U.S. companies to support the export of U.S. goods and services, thereby supporting U.S. jobs. Following the financial crisis of 2007-2009, increased demand for Ex-Im credit authorizations—caused by a retreat of private sector lenders from the market—led to rapid increases in the size of Ex-Im’s portfolio.¹ From 2008 to 2013, Ex-Im’s outstanding financial commitments—and by extension its exposure—grew from about \$59 billion to about \$114 billion, primarily in its long-term loans and loan guarantees. Also, since 2008, Ex-Im has been “self-sustaining” for budgetary purposes by financing its operations, including administrative costs and actual and expected losses on its risk exposure,

¹All years in this report are federal fiscal years unless otherwise indicated. An authorization is an export financing transaction that Ex-Im has approved.

from actual and expected interest and fees charged to its customers.² But, because Ex-Im's portfolio contains a large volume of recent transactions, the long-term impact of this business on the federal budget is not yet known. Ex-Im must operate within the parameters and limits authorized by law. The Export-Import Bank Reauthorization Act of 2012,³ among other things, increased the agency's exposure limit—that is, the total outstanding value of all direct loans, loan guarantees, and insurance policies that Ex-Im cannot exceed—from \$100 billion in 2011 to as much as \$140 billion in 2014.

Ex-Im's charter requires the transactions the agency authorizes to have a reasonable assurance of repayment.⁴ To comply with this requirement, Ex-Im must manage the wide variety of risks associated with providing export financing, including credit, political, and operational risks. Ex-Im uses a number of risk-management techniques throughout the different stages of a transaction, including underwriting, legal review and documentation, monitoring and restructuring, and claims and recovery. The recent growth in Ex-Im's exposure has heightened interest in ensuring that Ex-Im has proper procedures in place to minimize these risks while meeting the needs of U.S. exporters.

The Export-Import Bank Reauthorization Act of 2012 mandated that GAO, among other things, evaluate Ex-Im's underwriting process and fraud

²Under the Federal Credit Reform Act of 1990, Pub. L. No. 101-508, title XIII, § 13201 (Nov. 5, 1990), classified at 2 U.S.C. §§ 661-661f, agencies, including Ex-Im, are required to estimate and request appropriations for the long-term costs, or subsidy costs, of their credit activities. Ex-Im's subsidy cost estimates take into account, among other things, interest and fees it charges its customers for loans, loan guarantees, and insurance, as well as estimated default costs. Based on these estimates, Ex-Im has been self-sustaining for budgetary purposes since 2008, meaning that it estimates that expected interest and fees will more than cover expected default costs. However, the actual long-term cost of Ex-Im's credit activities will not be known until these loans are repaid and insurance contracts expire.

³Pub. L. No. 112-122 (May 30, 2012).

⁴As a government corporation, the statutory text establishing Ex-Im and governing its operations is referred to as a charter. See Export-Import Bank Act of 1945, Pub. L. No. 79-173 (July 31, 1945), *classified in part, as amended*, at 12 U.S.C. §§ 635-635t. Ex-Im's charter includes a defined termination date, which has been periodically extended by laws reauthorizing the entity. Most recently, the Export-Import Bank Reauthorization Act of 2012, enacted on May 30, 2012, extended this termination date to September 30, 2014.

procedures for its loan and loan guarantee transactions.⁵ Since Ex-Im's Office of Inspector General (IG) recently analyzed the underwriting of direct loans, we limited our review to loan guarantee transactions.⁶ This report discusses the extent to which Ex-Im has (1) adequately designed and implemented procedures to reasonably assure compliance with its underwriting process requirements for loan guarantee transactions and consistency with federal guidance and (2) adequately designed procedures to prevent, detect, and investigate fraudulent applications for loan guarantees.

To evaluate Ex-Im's procedures related to underwriting loan guarantee transactions, we reviewed Ex-Im's Loan, Guarantee and Insurance Manual, which describes, among other things, Ex-Im's procedures to assess loan guarantee applications and prepare loan agreements. We also reviewed other relevant Ex-Im documents, including the Ex-Im charter, performance reports, and other policies and procedures. Additionally, we interviewed Ex-Im officials about the underwriting process. We also reviewed IG and GAO reports relevant to Ex-Im's underwriting process. We identified criteria from the Office of Management and Budget (OMB) and Department of the Treasury (Treasury) guidance on managing loan guarantee programs,⁷ as well as from Standards for Internal Control in the Federal Government.⁸ We conducted tests on statistically random samples of loan guarantees authorized from October 1, 2011, to March 31, 2013, and reviewed loan files for documentation of the underwriting process and projected the

⁵The underwriting process encompasses Ex-Im's underwriting guidelines, lending policies, due diligence procedures, and content guidelines. Content guidelines determine the U.S. export contract eligibility and the level of support available in an Ex-Im financing package. That is, Ex-Im's content eligibility criteria state that to be eligible for inclusion in an Ex-Im financing package, all products in an export contract must be shipped from the United States to the foreign buyer.

⁶Export-Import Bank of the United States, Office of Inspector General, *Export-Import Bank's Management of Direct Loans and Related Challenges*, OIG-AR-13-05 (Washington, D.C.: Sept. 26, 2013).

⁷Office of Management and Budget, *Policies for Federal Credit Programs and Non-Tax Receivables*, OMB Circular No. A-129 (revised 2013), and Department of the Treasury, Bureau of the Fiscal Service, *Managing Federal Receivables* (May 2005).

⁸GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999).

results of our statistical samples.⁹ We tested two samples representing (1) short-term loan guarantees and (2) medium- and long-term loan guarantees.¹⁰ The results from our samples apply to the universe of loan guarantees authorized from October 1, 2011 to March 31, 2013. We also reviewed Ex-Im's delegated authority lender examination reports for certain lenders of short-term loan guarantees. To assess the reliability of the data we used, we analyzed information related to data quality controls, reviewed the data for obvious errors in accuracy and completeness, compared data to published documents, and interviewed knowledgeable officials about the data. We concluded that the data elements we used were sufficiently reliable for purposes of selecting samples of transactions to review and describing Ex-Im's loan guarantee balances.

To evaluate Ex-Im's procedures to prevent, detect, and investigate fraudulent applications for loan guarantees, we reviewed previous GAO and Ex-Im IG reports and relevant Ex-Im documents; the Ex-Im charter; and other plans, performance reports, policies, and procedures. We interviewed Ex-Im and IG officials knowledgeable about procedures to prevent, detect, and investigate fraud and spoke with lenders to identify steps Ex-Im has taken to strengthen lender procedures related to potential fraud. Using the statistically random samples described above, we tested documentation of fraud prevention processes. We also reviewed documentation of cases illustrating how Ex-Im detected potential fraud under a variety of circumstances.

We conducted this performance audit from March 2013 to September 2014 in accordance with generally accepted government auditing

⁹Because we followed a probability procedure based on random selections, each of our samples is only one of a large number of samples that we might have drawn. Since each sample could have provided different estimates, we express our confidence in the precision of our particular sample results as a 95 percent confidence interval (e.g., plus or minus 7 percentage points). This is the interval that would contain the actual population value for 95 percent of the samples we could have drawn. Confidence intervals are provided along with each sample estimate in the report. A detailed description of our sampling methodology can be found in app. I.

¹⁰We selected two statistically random samples of (1) 58 loan guarantee transactions from a population of 792 total short-term loan guarantees authorized from October 1, 2011, to March 31, 2013, and (2) 54 loan guarantee transactions from a population of 275 total medium- and long-term loan guarantees authorized from October 1, 2011, to March 31, 2013.

standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Appendix I provides more information on our scope and methodology.

Background

Ex-Im is an independent agency operating under the Export-Import Bank Act of 1945, as amended. Its mission is to support the export of U.S. goods and services, thereby supporting U.S. jobs. Ex-Im's charter states that it should not compete with the private sector. Rather, Ex-Im's role is to assume the credit and country risks that the private sector is unable or unwilling to accept, while still maintaining a reasonable assurance of repayment. Ex-Im must operate within the parameters and limits authorized by law, including, for example, statutory mandates that it support small business and promote sub-Saharan African and environmentally beneficial exports. In addition, Ex-Im must provide financing on a competitive basis with other export credit agencies and minimize competition in government-supported export financing and must submit annual reports to Congress on its actions.¹¹

Ex-Im's Functional Areas and Products

Ex-Im operates in several functional areas under the leadership of its President who also serves as Chairman of Ex-Im's Board of Directors.¹² Functional areas include the Office of the Chief Financial Officer, Office of General Counsel, Office of Resource Management, and Export Finance Group. The Export Finance Group is subdivided into business divisions that are responsible for underwriting related to loan guarantees, including processing applications, evaluating compliance of transactions with credit and other policies, performing financial analysis, negotiating financing terms, coordinating and synthesizing input to credit recommendations

¹¹Official export credit agencies (ECA) are organizations that provide export credits with explicit government backing, where either the government or the government-owned ECA assumes all or a portion of the risk.

¹²Ex-Im's Board of Directors consists of five members, with one seat vacant as of July 2014. The Ex-Im President serves as Chairman, Ex-Im's First Vice-President serves as Vice Chairman, and three additional members are appointed for 4-year terms by the President of the United States by and with the advice and consent of the Senate.

from other divisions, and presenting credit recommendations for approvals.

Ex-Im offers export financing through direct loans, loan guarantees, and insurance. Ex-Im's loan guarantees cover the repayment risk on the foreign buyer's loan obligations incurred to purchase U.S. exports. Loan guarantees are classified as short, medium, or long term. Figure 1 highlights the basic differences between the three loan guarantee types. Further, while Ex-Im relies on the value of U.S. content as a proxy to evidence support for U.S. jobs, it also considers exporter-supplied data on jobs created or preserved. Because foreign content and local costs represent amounts that do not directly benefit the U.S. economy or U.S. employment, Ex-Im developed requirements that limit the extent to which such amounts are covered by its financing.¹³ Specifically, Ex-Im's content policy includes criteria for identifying exports eligible for Ex-Im support based on the amount of foreign labor, materials, and overhead included in the production of the exported goods or services. Eligibility criteria and the amount of financing Ex-Im will provide based on content value depends on the terms of the financing requested and, for short-term transactions, whether the exporter is a small business. Ex-Im's content policy is self-imposed and establishes (1) the level of financing available depending on the content of exported goods and services and terms of the transaction and (2) procedures for exporters to report content information to Ex-Im and for Ex-Im to assess the reasonableness of such information. When a loan guarantee transaction is approved, exporters are required to complete and provide an Exporter's Certificate in which they certify the amount of foreign and domestic content included in the goods or services financed by Ex-Im. The certificate warns exporters of the federal penalties for making false statements.

¹³Local costs represent the aggregate price of all goods originated or manufactured in the purchaser's country and all services provided by registered local business entities of the purchaser's country.

Figure 1: Types of Export-Import Bank (Ex-Im) Loan Guarantees



Source: GAO analysis of Ex-Im data. | GAO-14-574

- Short-term loan guarantees:** Ex-Im's short-term loan guarantee product is focused on working capital financing (hereinafter referred to as working capital loan guarantees). Working capital loan guarantees may be approved for a single transaction or a revolving line of credit that can be extended up to 3 years. In general, if the financed eligible product contains more than 50 percent U.S. content, then the entire

transaction value is eligible for an Ex-Im working capital loan guarantee.¹⁴ Generally, Ex-Im guarantees 90 percent of the loan's principal and interest if the borrower defaults. Therefore, the lender maintains the risk of the remaining 10 percent. Ex-Im's payment of working capital claims is conditional upon the guaranteed lenders' compliance with Ex-Im requirements, such as underwriting policies, deadlines for filing claims, payment of premiums and fees, and submission of proper documentation. Ex-Im has reported that over 80 percent of its working capital guarantee transactions are approved by lenders with delegated authority, which means that commercial lenders approve the guaranteed loans in accordance with agreed-upon underwriting requirements without first obtaining Ex-Im approval. If a lender does not have delegated authority, Ex-Im performs its own underwriting procedures and approves the guaranteed loans.

- **Medium- and long-term loan guarantees:** Financing eligibility for Ex-Im's medium- and long-term loan guarantee support is limited to the lesser of (1) 85 percent of eligible goods and services in the U.S. export contract or (2) 100 percent of the U.S. content.¹⁵ Ex-Im's medium- and long-term loan guarantees generally cover 100 percent of the loan's principal and interest if the buyer defaults. Ex-Im's guarantee to the lender is transferable, carrying the full faith and credit of the U.S. government, and is unconditional, meaning that Ex-Im must pay submitted claims regardless of the cause of default, as long as the claim is filed timely and no amendments were made without Ex-Im's consent. The underwriting of medium-term loan guarantees is generally performed by Ex-Im and approved by certain Ex-Im officers with delegated authority. For about 3 percent of medium-term loan guarantee transactions, Ex-Im has provided certain lenders delegated authority to underwrite and approve these guarantees. The

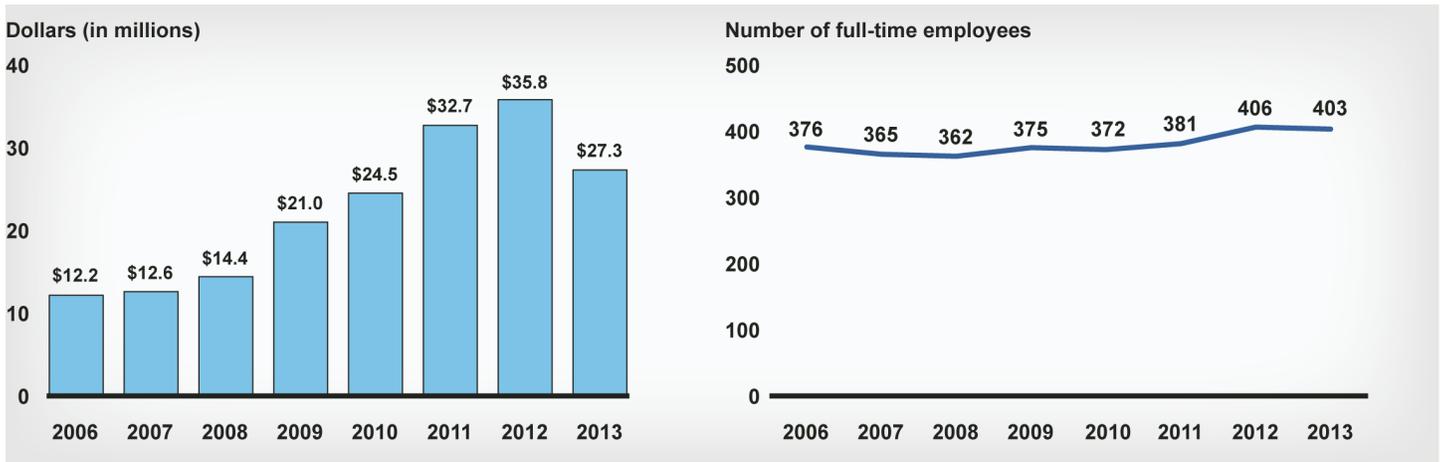
¹⁴In general, the entire product must be exported from the United States. When eligible content includes both direct and indirect costs, these costs are treated differently for small business and non-small business working capital transactions. Also, if an applicant is a small business and the financed product represents less than 50 percent U.S. content, then only the U.S. costs are eligible for an Ex-Im guarantee.

¹⁵Eligible goods could include foreign content if exported from the United States. Financing 85 percent of the value of these transactions is considered full financing because of provisions under an international arrangement that ECAs generally do not finance more than this for transactions with terms greater than 2 years. In addition, Ex-Im guarantees can cover some local costs, such as on-site construction services, beyond the value of the export contract.

underwriting of long-term loan guarantees is performed by Ex-Im and approved by the Ex-Im Board of Directors.

Ex-Im's annual authorizations for direct loans, loan guarantees, and insurance increased from about \$12 billion in 2006 to over \$27 billion in 2013, an increase of about 125 percent. Over the same period, Ex-Im's staff level, as measured by full-time employees, increased from 376 to 403, about 7 percent (see fig. 2).

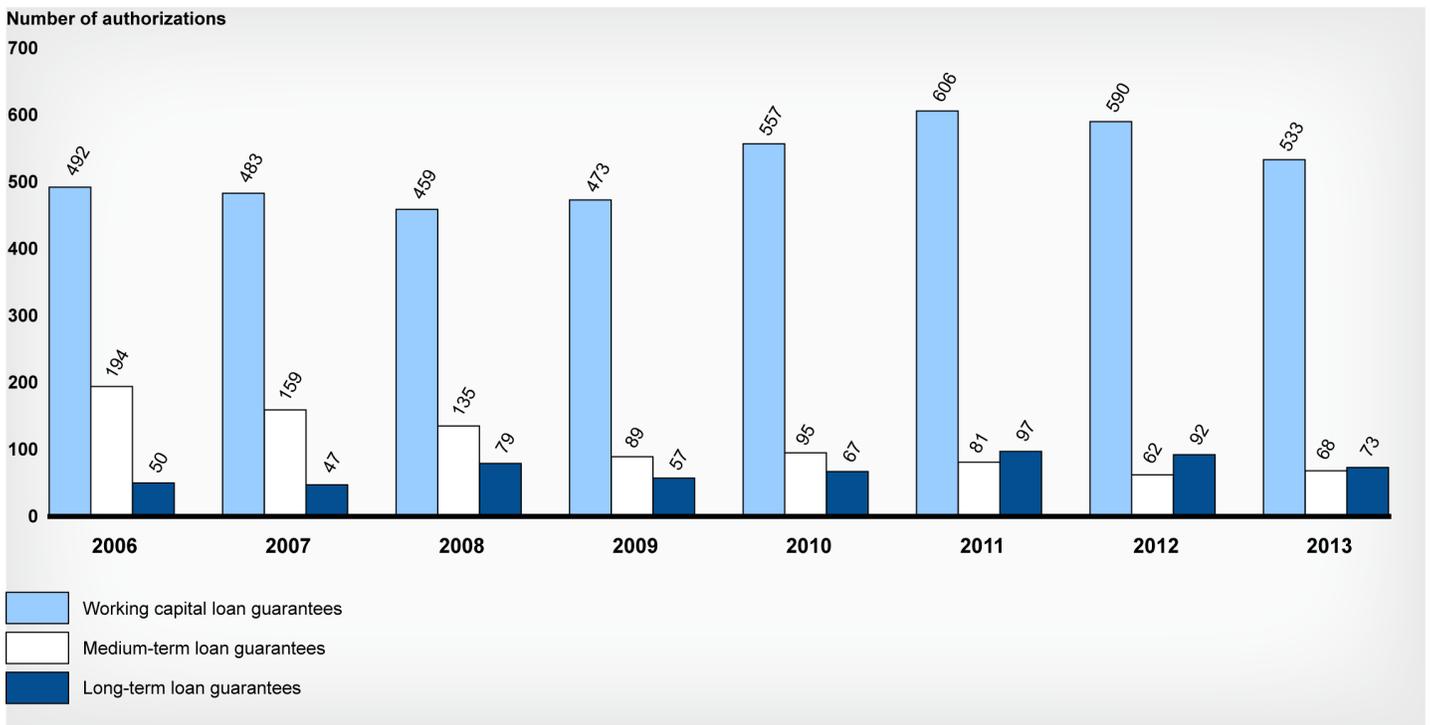
Figure 2: Export-Import Bank (Ex-Im) Authorization and Full-time Employees, 2006 through 2013



Source: GAO analysis of Ex-Im data. | GAO-14-574

Of the annual authorizations for all Ex-Im financing products, as shown in figure 3, Ex-Im's number of authorized transactions for working capital and long-term loan guarantees fluctuated from 2006 to 2013. However, the number of medium-term loan guarantee transactions decreased from 2006 to 2013. There were 533 working capital, 68 medium-term, and 73 long-term loan guarantee authorizations that totaled \$14.9 billion, or 55 percent, of Ex-Im's total annual authorizations in 2013.

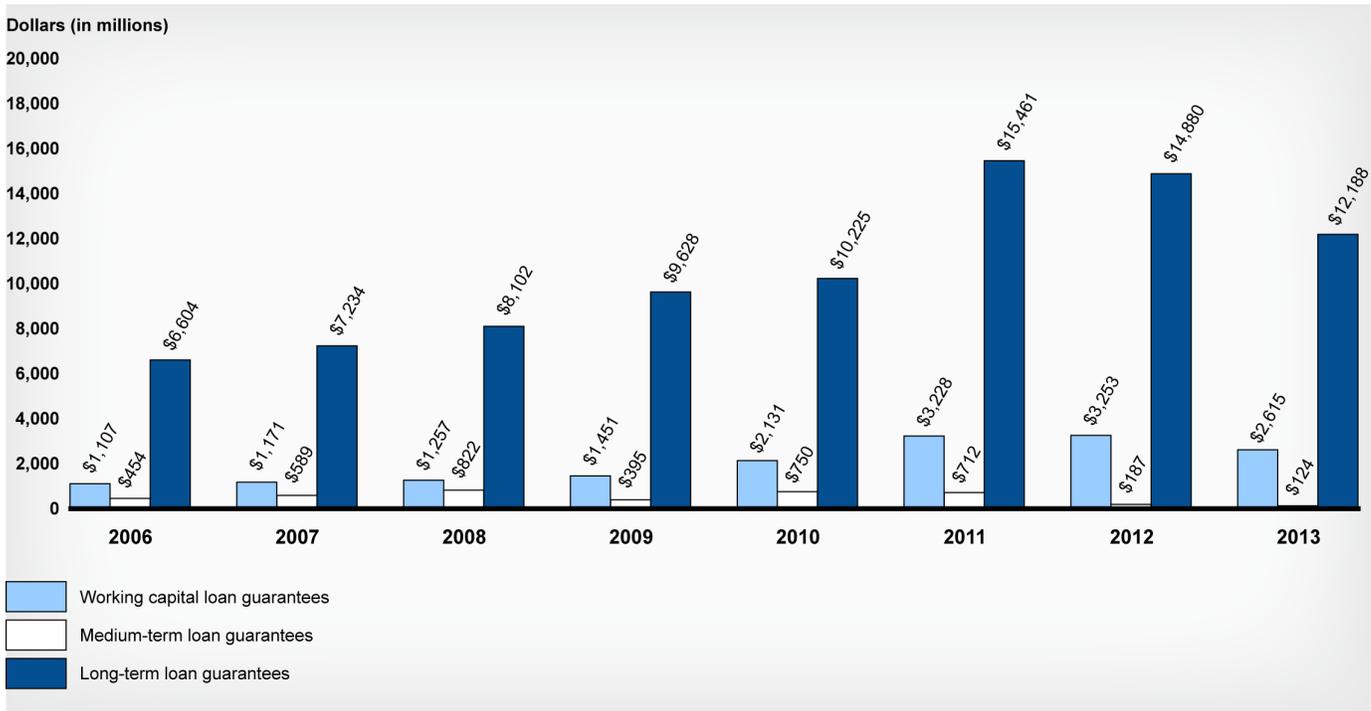
Figure 3: Number of Export-Import Bank (Ex-Im) Loan Guarantees Authorized, 2006 through 2013



Source: GAO analysis of Ex-Im data. | GAO-14-574

Although the number of working capital loan guarantees greatly exceeds the number of medium- and long-term loan guarantees, long-term loan guarantees account for the greatest dollar value of loan guarantees (see fig. 4). During the period 2006 through 2013, reported claim payments on defaulted loan guarantees have fluctuated and averaged \$76.5 million. Such claim payments ranged from a high of \$176.5 million in 2010 to lows of \$19.3 million and \$28.4 million in 2012 and 2013, respectively.

Figure 4: Dollar Value of Export-Import Bank (Ex-Im) Loan Guarantees Authorized, 2006 through 2013

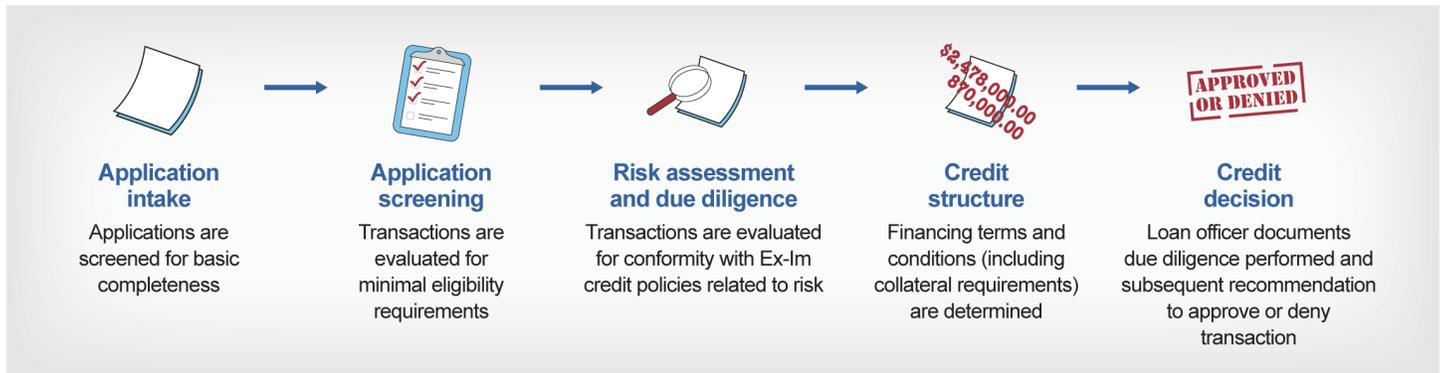


Source: GAO analysis of Ex-Im data. | GAO-14-574

Overview of Ex-Im's Underwriting Process

Ex-Im's *Loan, Guarantee and Insurance Manual* (Manual), which was updated in January 2013, February 2014, and March 2014, describes, among other things, Ex-Im's underwriting procedures for long-term, medium-term, and working capital loan guarantees. The Manual describes the responsibilities of Ex-Im's divisions (e.g., Transportation or Working Capital Finance) involved in the credit process, including application processing activities shown in figure 5. The underwriting of loans guaranteed by Ex-Im is performed by either Ex-Im loan officers or qualified lenders with delegated authority, which allows a lender to authorize a loan guaranteed by Ex-Im in accordance with agreed-upon underwriting requirements without first obtaining Ex-Im approval. All of the underwriting for long-term loan guarantees is performed by Ex-Im loan officers. According to Ex-Im officials, the underwriting process is essential to helping to prevent fraud because of the due diligence performed over the transactions and the transaction participants.

Figure 5: Export-Import Bank's (Ex-Im) Underwriting Activities



Source: GAO analysis of Ex-Im data. | GAO-14-574

Application intake. When an application is initially received, it is screened for basic completeness; follow-up on incomplete or unacceptable applications is performed; and once considered complete, it is assigned to a processing division.

Application screening. After an application is determined to be complete, it is assigned to the applicable Ex-Im division that oversees the type of transaction. For example, an application for the purchase of an aircraft would be assigned to the Transportation Division. Once assigned, a loan officer in that division is to assess the eligibility of the transaction, including eligibility of the export item, additionality,¹⁶ and eligibility of the country where goods are to be shipped. To ensure compliance with laws and regulations, the loan officer is to obtain and assess various certifications from transaction participants, such as Iran Sanctions

¹⁶Ex-Im's charter directs that Ex-Im should foster the expansion of U.S. exports and that it should supplement and encourage, rather than compete with, private capital. Therefore, Ex-Im directs its efforts at financing export transactions that are considered unlikely to proceed without Ex-Im support. Ex-Im refers to the likelihood that an export transaction will not go forward unless it provides support as additionality. The primary considerations in determining additionality are the availability of competing financing from other ECAs and the availability of private sector financing on acceptable terms.

Certifications¹⁷ and antilobbying statements.¹⁸ Loan officers are also required to submit the corporate and individual names and addresses of lenders, borrowers, guarantors, and other transaction participants to the Ex-Im Library. Library staff are then to conduct a Character, Reputational, and Transaction Integrity review—a procedure designed to, among other things, provide due diligence over various risks and to help prevent fraud by checking loan participants' information with approximately 20 databases. Databases include various U.S. government and international debarment and sanction lists, as well as lists maintained by international financial institutions, the World Bank, and the Inter-American Development Bank. These lists contain the names and addresses of individuals and organizations that have been debarred or placed on a sanctions list by major international financial institutions because of their involvement in irregular, fraudulent, or corrupt acts.

Risk assessment and due diligence. Once the transaction meets minimum eligibility requirements for Ex-Im support, the loan officer performs a series of due diligence activities to determine (1) whether the transaction provides a reasonable assurance of repayment, (2) any potential material issues regarding the transaction or the participants that could preclude Ex-Im support or affect the material terms of the proposed transaction, and (3) the appropriate risk level and pricing for the transaction. As part of the financial evaluation of the transaction, the loan officer obtains and analyzes the borrower's audited financial statements, credit reports¹⁹ or rating agency reports, financial projections, and other relevant information. A credit report is generally required for medium- and

¹⁷For all transactions subject to approval by the Board of Directors, the borrower and guarantor lender (if any) must submit a certification with respect to certain activities prohibited by the Iran Sanctions Act of 1996, Pub. L. No. 104-172 (Aug. 5, 1996), *classified as amended* at 50 U.S.C. § 1701 note; the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010, Pub. L. No. 111-195 (July 1, 2010); and the Iranian Transactions Regulations, 31 C.F.R. part 560.

¹⁸Recipients of federal loans, grants, contracts, and cooperative agreements are prohibited from spending federally appropriated funds to influence or lobby certain U.S. government employees, including Ex-Im employees, in connection with the granting of those federal awards. 31 U.S.C. §1352.

¹⁹A credit report is a document created by a credit reporting agency that summarizes the financial history of a party (a person or a business). Examples of information found in a credit report include the amount of credit available to a party, how much of its credit limit a party tends to rely on for purchases, whether the party has a history of paying its bills on time, and whether a party has previously gone through bankruptcy.

long-term loan guarantee transactions, except when the primary source of repayment is another government or a financial institution. If there are any exceptions to credit information requirements, credit standards, or Ex-Im policy, the loan officer is required to document the rationale for exceptional treatment. As needed, the loan officer obtains input from other Ex-Im staff, such as attorneys, economists, or engineers, to reach a conclusion regarding the legal, technical, or country risks and the level of environmental or social impacts of the proposed transaction. In addition, Ex-Im may utilize external financial, legal, and technical advisors to assist in the due diligence process. With the assistance from these other Ex-Im staff and external advisors, as needed, the loan officer is in a position to confirm the eligibility of exports for financing and the eligibility of the U.S. and foreign content included in the transaction.²⁰ Ex-Im has established detailed policy on the amount of foreign content it will finance. Based on this due diligence, the loan officer is to assess the transaction for risk and assign an overall risk rating to the transaction. This rating is used, in part, to determine the exposure fee Ex-Im will charge the borrower for guaranteeing the transaction. Greater risks result in higher fees.

Credit structure. After the risk assessment and due diligence is performed, the loan officer determines the financing terms and conditions to be recommended. The loan officer is generally required to structure the transaction to include a security interest (collateral) in the financed goods or other assets of the borrower. If it is determined that collateral is not necessary, the loan officer is to document the explanation and other mitigating factors to indicate this is acceptable to Ex-Im (e.g., Ex-Im support is small relative to borrower's size). For all aircraft transactions, the loan officer is required to perform an assessment and loan-to-value analysis of the collateral,²¹ and the financing terms must include requirements for the borrower to maintain the ownership and condition of collateral.

Credit decision. The loan officer is to document the due diligence performed, including any analyses performed by external advisors, in a credit or board memo, which also contains the loan officer's

²⁰"Content" refers to the country of origin of the goods and services that make up an export contract. According to Ex-Im, its content policy is "the proxy to connect its activities to jobs, and the most fitting policy tool to promote U.S. employment."

²¹The loan-to-value analysis compares the expected future values of the financed aircraft with the estimated Ex-Im exposure balance over the term of the financing.

recommendation to approve or decline the transaction. These memos and applicable supporting documentation are then to be forwarded to the approving party. The credit memo applicable to working capital or medium-term transactions is to be provided to Ex-Im officials with individual delegated authority to approve transactions of \$10 million and under.²² Board memos for long-term transactions or transactions greater than \$10 million or those within certain sensitive sectors (e.g., steel) are to be presented to the Ex-Im Board of Directors for consideration and approval.

Underwriting Delegated Authority Transactions

When the underwriting and credit decision is delegated to preapproved lenders, Ex-Im does not perform the underwriting procedures. However, Ex-Im's established procedures call for delegated authority lender examinations to be performed at least annually to assess lenders' compliance with Ex-Im's underwriting standards. To conduct these examinations, an Ex-Im examiner selects a sample of the lender's outstanding Ex-Im guaranteed loans to analyze.²³ The examiner is to assess the lender's credit underwriting practices to ensure they meet Ex-Im's requirements and include due diligence and financial analyses. The examiner is required to review a loan's application, authorization notice, credit memo, and loan agreement. Any exceptions to Ex-Im standards are to be noted in the examination report. Based on the seriousness of any exception(s), the lender receives either a Pass, Pass with Qualification, or Fail rating. Pass ratings indicate substantial compliance with only minor weaknesses; Pass with Qualification indicates overall adequate compliance except within a limited area of concern; Fail indicates a lack of compliance. A Pass with Qualification rating requires subsequent corrective action, while a Fail rating requires immediate suspension of delegated authority.

Management of Loan Guarantee Programs

Government-wide guidance for federal agencies to follow for the management and operation of a loan guarantee program include the following:

²²The \$10 million threshold for individual delegated authority does not include any exposure fees associated with a loan guarantee transaction.

²³Ex-Im's policies state that the sample must include (1) any loan facility of \$5 million or more, (2) at least 25 percent of the total dollar amount of the outstanding portfolio, (3) at least 25 percent of the total number of loan facilities in the portfolio, and (4) a sample of both new and renewed loans. In addition, if a lender has three or fewer outstanding loans, all of the loans should be reviewed.

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- OMB Circular No. A-129, *Policies for Federal Credit Programs and Non-Tax Receivables*, revised in January 2013, prescribes policies and procedures for designing and managing federal credit programs, including requirements for applicant screening, assessing creditworthiness, loan documentation, and collateral.
 - Treasury’s Bureau of the Fiscal Service’s *Managing Federal Receivables* provides federal agencies with a general overview of standards, guidance, and procedures for successful management of credit activities, including requirements for evaluating and documenting loan applications.

Underwriting Guidance Was Established, but It Did Not Reasonably Assure Consistent Implementation and Compliance with Certain Requirements

The Manual, which describes Ex-Im’s loan guarantee underwriting procedures, provided a framework for Ex-Im officials to implement Ex-Im’s underwriting process requirements for loan guarantee transactions, and Ex-Im implemented many key aspects of its underwriting process as required by the Manual. For example, Ex-Im consistently documented (1) transaction participant information, (2) due diligence over borrower creditworthiness and eligibility of costs, (3) loan guarantee terms and conditions, and (4) loan guarantee transaction approvals. However, the Manual did not adequately address the underwriting process in the following four areas: (1) application screening, (2) risk assessment and due diligence, (3) credit structure, and (4) credit decision. Specifically, the Manual did not include certain procedures that should be performed, or sufficiently detailed instructions on how certain procedures should be performed and documented, to reasonably assure compliance with Ex-Im’s requirements and consistency with federal guidance prior to loan guarantee approval. Further, Ex-Im did not have mechanisms to verify compliance with certain established procedures related to loan guarantee transactions prior to approval. In addition, while Ex-Im’s process for scheduling its delegated authority lender examinations was consistent with federal guidance, it was not documented or consistent with its established procedures.

Certain Application Screening Procedures Were Not Fully Consistent with Federal Guidance or Consistently Implemented

Ex-Im’s Manual generally provided loan officers guidance to screen application documentation and verify that loan guarantee transactions met certain eligibility criteria consistent with federal guidance. However, the Manual did not address the federal requirement that applicants must not be delinquent on federal debt to be eligible for financing. Further, the Manual did not include mechanisms to verify that certain application screening procedures were documented prior to loan guarantee approval, such as obtaining credit reports and documenting certain other eligibility procedures.

Application Screening
Documentation

We estimated that Ex-Im documented transaction participants, such as the applicant, borrower, guarantor, buyer, lender, end user, exporter, supplier, and guaranteed lender, for 100 percent of the medium- and long-term loan guarantee transactions.²⁴ In addition, Ex-Im generally obtained from applicants and documented in the loan files the antilobbying statements, environmental screening documents, and Iran Sanctions Certifications, where applicable.

Delinquent Federal Debt

While Ex-Im's loan guarantee applications require applicants to disclose if they are delinquent on federal debt, as required by OMB Circular No. A-129, Ex-Im's Manual did not include procedures for Ex-Im to verify the information provided by the applicant as required by Treasury's Managing Federal Receivables. To determine whether an applicant is delinquent on federal debt, this federal guidance states that agencies are required to use credit reports as a screening tool and should use appropriate databases, such as the Department of Housing and Urban Development's Credit Alert Verification Reporting System or Treasury's Do Not Pay List, to identify delinquencies on federal debt.²⁵ While Ex-Im's Character, Reputational, and Transaction Integrity review process called for transaction participants' information to be checked against various databases, it did not include the recommended databases that could identify delinquent federal debt of the transaction participants. Further, while Ex-Im's Manual required loan officers to obtain credit reports with applications for transactions with specific risks,²⁶ the Manual did not state that the credit reports should be used to identify whether transaction applicants have delinquent federal debt. Having procedures and data to

²⁴The 95 percent confidence interval for the medium- and long-term loan guarantee transactions is between 95 percent and 100 percent.

²⁵The Department of Housing and Urban Development's Credit Alert Verification Reporting System was developed in June 1987 as a shared database of defaulted federal debtors, and enables processors of applications for federal credit to identify individuals who are in default or have had claims paid on direct or guaranteed federal loans or are delinquent on other debts owed to federal agencies. The Do Not Pay List is a web-based single-entry access portal that federal agencies can use to gain access to several databases to assist in determining whether an individual or entity is ineligible, in part because of delinquent federal debt, to receive federal payments or engage in federal contracts or grants.

²⁶A credit report is generally required for medium- and long-term loan guarantee transactions, except when the primary source of repayment is another government or a financial institution. We use the term credit report to refer to both a credit bureau report on an individual guarantor or a Dunn and Bradstreet report if the guarantor is a business.

verify that transaction applicants are not delinquent on federal debt helps assure applicant eligibility is consistent with federal guidance.

Credit Reports

Ex-Im did not consistently follow its established procedures for obtaining credit reports or did not document why the credit reports were not applicable. Specifically, we estimated that credit reports were not obtained, and Ex-Im did not document why they would not be applicable, for 61 percent of the medium- and long-term loan guarantees.²⁷ Ex-Im officials told us that they did not always enforce the requirement to obtain credit reports because information in such reports could be stale or erroneous and did not heavily influence the overall eligibility determination. Additionally, loan officers told us that credit reports were not needed for aircraft transactions because of the extensive financial analyses performed during the underwriting of these transactions as well as the prior approvals of the applicants' creditworthiness for previous transactions.²⁸ For example, Ex-Im officials indicated that on such large, longer-term financing, the applicant must provide 3 years of audited financial statements, as well as a thorough explanation of its business plan. Ex-Im officials stated that a loan officer's due diligence provides information that is more extensive than that obtained through a review of a credit report. Nevertheless, Ex-Im did not have a mechanism to verify that credit reports were obtained in accordance with established procedures or that reasons for credit reports not being applicable were documented prior to loan guarantee approval. Obtaining credit reports for transaction participants, when available, could provide additional information to further enhance the loan officers' knowledge about the financial condition of the transaction borrower and the risk associated with the proposed transaction.

Other Eligibility Procedures

Ex-Im loan officers did not consistently implement established procedures for documenting the determination of certain other eligibility related information for loan guarantee transactions.

- **Character, Reputational, and Transaction Integrity reviews.** We estimated that Ex-Im documented its Character, Reputational, and

²⁷The 95 percent confidence interval for this estimate is between 48 percent and 73 percent.

²⁸Our total sample of 54 medium- and long-term loan guarantee transactions included 19 aircraft transactions. From those 19, we found two instances where credit reports were obtained.

Transaction Integrity reviews, including any identified issues and how they were resolved, as called for by Ex-Im's established procedures, for 100 percent of the working capital loan guarantees. However, we estimated that about 4 percent of the medium- and long-term loan guarantee transactions did not include all documentation related to these reviews being performed.²⁹

- **Export item eligibility and country eligibility.** According to Ex-Im's Manual, export item eligibility and country eligibility should be determined and documented during the loan guarantee application screening process as part of Ex-Im's minimum eligibility requirements. However, while loan files we reviewed documented the export item and country involved in the transaction, we estimated that 39 percent of the medium- and long-term loan guarantee transactions did not have specific statements regarding the determination of export item, and we estimated that 41 percent of the medium- and long-term loan guarantee transactions did not have specific statements regarding the determination of country eligibility.³⁰

OMB Circular No. A-129 and Treasury's guidance state that agencies shall determine and document that applicants comply with statutory, regulatory, and administrative eligibility requirements. In addition, internal control standards require controls and transactions to be clearly documented and documentation to be readily available for examination.³¹ When we inquired about these eligibility documentation issues, loan officers indicated that the supporting documentation for the Character, Reputational, and Transaction Integrity review was not uploaded into the system for inclusion in the loan files, and based on their institutional knowledge of prior history with applicants, country eligibility, and export items, eligibility was clear and did not need to be documented. However,

²⁹The 95 percent confidence interval for working capital loan guarantee transactions is between 95 percent and 100 percent. The 95 percent confidence interval for medium- and long-term loan guarantee transactions is between .7 percent and 12 percent. All exceptions that we identified related to medium-term loan guarantee transactions.

³⁰All exceptions that we identified related to medium-term loan guarantee transactions. The 95 percent confidence interval for the loan guarantees that lacked statements regarding the determination of export item eligibility is between 27 percent and 52 percent. The 95 percent confidence interval for the loan guarantees that lacked statements regarding the country eligibility is between 29 percent and 54 percent.

³¹[GAO/AIMD-00-21.3.1.](#)

overreliance on this institutional knowledge could create inconsistencies in the underwriting process and could lead to transactions not being documented in accordance with established procedures. Further, when institutional knowledge is a part of the basis for loan guarantee approval, there is a risk that such knowledge could be lost if employee turnover takes place. Ex-Im did not have a mechanism in place to verify that these procedures related to eligibility requirements were performed and documented prior to loan guarantee approval. Consistently performing and documenting eligibility determinations helps ensure transaction and applicant eligibility.

In September 2013, the IG reported, based on its review of Ex-Im's underwriting of direct loans, that Ex-Im lacked documented support for statements regarding additionality (the justification for Ex-Im support). We observed a similar issue during our review of a sample of working capital and medium- and long-term loan guarantee transactions. In its September 2013 report, the IG recommended that Ex-Im update procedures for loan officers to maintain detailed documentation regarding the need for Ex-Im support.³² Ex-Im agreed with the IG recommendation and stated that the Ex-Im Manual would be updated to require loan officers to maintain detailed documentation regarding the need for Ex-Im support. As of July 2014, Ex-Im had updated the Manual for verification procedures over additionality for long-term transactions and Ex-Im officials stated that they are considering ways to further document additionality statements for working capital and medium-term transactions.

³²Export-Import Bank of the United States, Office of Inspector General, OIG-AR-13-05.

Ex-Im Performed Risk and Due Diligence Analyses, but Certain Necessary Steps Were Either Not Documented or Not Required

We estimated that Ex-Im documented 100 percent of its financial analysis of the applicants' creditworthiness, the eligibility of costs, the value of U.S. and foreign content, the budget-cost level, the engineering report, and environmental analyses, where applicable, for the working capital and medium- and long-term loan guarantee transactions.³³ In addition, Ex-Im also documented in the loan files the economic impact analysis required by the Manual, where applicable.³⁴ We also estimated that Ex-Im documented 100 percent of its due diligence for country risk, sovereign risk, political risk, financial institution risk, and nonfinancial institution risk factors for medium- and long-term loan guarantee transactions.³⁵ Further, for 19 out of 19 aircraft loan guarantee transactions that we reviewed, Ex-Im documented the credit and legal strengths, weaknesses, and uncertainties related to the proposed transaction. Moreover, for 11 out of 11 medium-term loan guarantee transactions in excess of \$1 million that we reviewed, Ex-Im documented the transaction risk classification in the loan file, as required by the Manual. However, loan officers did not document the analysis of country exposure,³⁶ as required by Ex-Im's established procedures, for an estimated 11 percent of the medium- and long-term loan guarantee transactions.³⁷

Further, as noted above, credit reports were required for certain loan guarantee transactions. Also, Ex-Im's Manual called for loan officers to document any mitigating factors for issues identified during the risk assessment and due diligence process. However, the Manual did not include detailed instructions for loan officers to use information in credit reports to enhance their financial analysis of transaction participants'

³³The 95 percent confidence interval for the working capital and medium- and long-term loan guarantee transactions is between 95 percent and 100 percent.

³⁴An economic impact analysis is an assessment of whether the extension of Ex-Im financing support is likely to cause substantial injury to U.S. industry or would result in the production of substantially the same product that is the subject of specified trade measures.

³⁵The 95 percent confidence interval for the medium- and long-term loan guarantee transactions is between 95 percent and 100 percent.

³⁶The country exposure analysis provides a breakdown of Ex-Im's outstanding financing regarding a specific country by type of risk (e.g., sovereign, public nonsovereign, private, and financial institution).

³⁷All exceptions that we identified related to medium-term loan guarantee transactions. The 95 percent confidence interval for this estimate is between 5 percent and 22 percent.

creditworthiness during the risk assessment and due diligence process. During our review of a sample of loan files, we noted that certain approved transaction participants' credit reports contained issues, such as outstanding liens and poor credit history, yet the loan files did not contain documentation that these issues were identified by the loan officers or how these issues were mitigated. We inquired with Ex-Im loan officers about how these issues were mitigated, and they provided reasonable explanations.

OMB Circular No. A-129 states that loan origination files should contain credit reports and credit analyses. Further, internal control standards require that controls and transactions be clearly documented and documentation be readily available for examination.³⁸ However, Ex-Im did not have a mechanism in place to verify that the country exposure and information in credit reports were considered and documented during the risk assessment and due diligence process prior to loan guarantee approval. Ex-Im officials stated that the Credit Review and Compliance Division (CRC) directly monitors loan guarantee transactions by selecting and reviewing a random sample of loan guarantee transactions for compliance with Ex-Im's established procedures. However, these reviews occur after the loan guarantees have been approved by Ex-Im and the funds have been disbursed by the lenders. Consistently performing and documenting reviews and key decisions related to risk assessments and due diligence helps ensure that Ex-Im's financing is provided to applicants representing reasonable assurance of repayment.

To be eligible for Ex-Im financing, exported goods and services must meet Ex-Im's content requirements intended to ensure that U.S. jobs benefit from Ex-Im programs. In December 2013, the Ex-Im IG reported that only long-term loan guarantee transactions were subjected to procedures that could identify content-related discrepancies.³⁹ Further, the IG reported that because of the lack of verification efforts and identified concerns regarding exporter certifications of content value, Ex-Im had limited assurance that content requirements are met and therefore that (1) Ex-Im finances only eligible exports and (2) its financing activities

³⁸[GAO/AIMD-00-21.3.1](#).

³⁹Export-Import Bank of the United States, Office of the Inspector General, *Export-Import Bank's Content Policy: Opportunities Exist to Improve Controls and Address the Impact of Voluntary Reporting*, OIG-AR-14-01 (Washington D.C.: Dec. 11, 2013).

effectively achieve the agency's mission of maintaining or increasing U.S. employment. The IG also noted that Ex-Im relied on criminal penalty warnings to deter exporters from making false statements instead of confirming foreign and domestic content for working capital and medium-term transactions. We also found that Ex-Im relied on exporter self-certifications of each export's foreign and U.S. content information when performing its due diligence process for working capital and medium-term loan guarantee transactions. In its December 2013 report, the IG recommended that Ex-Im implement procedures to verify the accuracy of exporter self-certifications of content information for a representative sample of transactions each fiscal year. Ex-Im agreed with the recommendation, and in June 2014, procedures to verify a representative sample of exporters' self-certifications each fiscal year were approved for use. Ex-Im officials stated that they are now in the process of implementing the procedures.

Ex-Im Documented Credit Structure Terms and Conditions, but Certain Collateral Requirements Were Not Consistent with Federal Guidance

Generally, Ex-Im's Manual provided loan officers with detailed guidance for determining and documenting key credit structure components—financing terms and conditions, including collateral requirements—of a loan guarantee transaction. We estimated that Ex-Im implemented established procedures and documented 100 percent of certain credit structure components of the loan guarantee transactions, such as transaction participants, financed amount, repayment terms, and exposure fee.⁴⁰ In addition, while Ex-Im generally identified collateral associated with its transactions, it did not consistently document an assessment of collateral prior to loan guarantee approval. Specifically, Ex-Im's established procedures for nonaircraft medium- and long-term loan guarantees did not call for assessments of collateral prior to approval of the transactions as recommended by federal guidance, including OMB Circular No. A-129. We estimated that 37 percent of the medium- and long-term loan guarantee transactions did not have documentation to show that the identified collateral was assessed prior to loan guarantee approval.⁴¹

⁴⁰The 95 percent confidence interval for the working capital and medium- and long-term loan guarantee transactions is between 95 percent and 100 percent.

⁴¹The 95 percent confidence interval for this estimate is between 26 percent and 50 percent.

As stated in OMB Circular No. A-129, the government can reduce its risk of default and potential losses through well-managed collateral requirements for many types of loans during the application screening process. Collateral requirements were clearly defined in Ex-Im's Manual for aircraft and working capital loan guarantee transactions, but these requirements were not clearly defined in Ex-Im's Manual for nonaircraft medium- and long-term loan guarantee transactions. For example, procedures specific to aircraft transactions require an analysis of collateral and require that the ownership and condition of the collateral be maintained. Ex-Im documented detailed assessments of collateral for all long-term aircraft transactions we reviewed. Further, the procedures specific to working capital loan guarantee transactions state that the transactions must be fully collateralized at all times. The collateral for these transactions typically consists of export-related inventory, export-related accounts receivable, and export-related general intangibles.

In February 2014, Ex-Im updated its procedures for collateral requirements. This additional guidance contained more details related to the identification of collateral; however, it did not include steps for an assessment of collateral as recommended by federal guidance. Ex-Im officials stated that lenders are usually required to provide evidence of obtained collateral in financed goods, which is to be reviewed by Ex-Im staff. However, this documentation was not maintained with underwriting documents, and loan officers generally told us that they did not rely on collateral during the underwriting process because it contributes to recoveries in the event of a default rather than to determining the reasonable assurance of repayment. Further, Ex-Im officials stated that since collateral is often negotiated and documented after loan approval, it may not be possible to assess collateral prior to approval. Ex-Im officials stated that the loan guarantees (including collateral) are monitored by Ex-Im's Asset Management Division (AMD) once the loan guarantees become operative (approved by Ex-Im). However, having procedures for documenting an assessment of collateral prior to loan guarantee approval helps in the assessment of the overall financial risk of the proposed loan guarantee transaction.

Approvals Were Documented, but Some Credit Decisions Were Made without Ensuring Loan Documentation Completeness

Ex-Im's Manual described the tasks that need to be performed during the underwriting process and included credit memo templates to support a decision for various types of guarantees. However, the Manual did not include detailed instructions for preparation and inclusion of all required documents or analyses in a loan file prior to loan guarantee approval.

We estimated that Ex-Im documented the approvals of 100 percent of all loan guarantee transactions with signatures on various loan guarantee documents.⁴² In addition, when lenders with delegated authority performed the underwriting for working capital loan guarantee transactions, we estimated that Ex-Im officials completed and signed the delegated authority checklist for 100 percent of the transactions.⁴³ These checklists included transaction information such as the lender, borrower, loan amount, type of facility, letters of credit, warranties, disbursement date, primary and secondary collateral, and the terms of the loan. Although Ex-Im's Manual described the tasks that needed to be performed during the underwriting process, it was not clear as to what documentation needed to be included in the loan file or when certain documentation was not required. Both OMB Circular No. A-129 and Treasury guidance state that loan origination files should contain loan applications, credit reports, credit analyses, loan contracts, and other documents necessary to conform to private sector standards for that type of loan. In addition, internal control standards state that all transactions and other significant events need to be clearly documented, and the documentation should be readily available for examination. Further, the standards state that all documentation and records should be properly managed and maintained.⁴⁴ Detailed instructions help to reasonably assure that complete documentation is included in the loan file prior to loan guarantee approval, providing further support for the final credit decision.

In September 2013, the IG reported on Ex-Im's underwriting of direct loans and found that loan officers did not always complete various checklists intended to reasonably assure that (1) all required commitment

⁴²The 95 percent confidence interval for the working capital and medium- and long-term loan guarantee transactions is between 95 percent and 100 percent.

⁴³The 95 percent confidence interval for the working capital loan guarantee transactions is between 95 percent and 100 percent.

⁴⁴[GAO/AIMD-00-21.3.1](#).

documents are obtained prior to loan guarantee approval, (2) borrowers are eligible, and (3) loan applications are complete and comply with Ex-Im credit policies and standards.⁴⁵ The IG found that loan officers generally relied on their institutional knowledge of Ex-Im operations when underwriting loans. We found a similar condition with regard to the underwriting of loan guarantee transactions. In its September 2013 report, the IG recommended that Ex-Im develop a systematic quality control review program or other mechanism(s) necessary to prevent, detect, and correct Ex-Im staff noncompliance with federal and agency credit program policy. Ex-Im agreed with the recommendation and stated that it would expand the scope of postauthorization reviews to assess compliance with federal and Ex-Im credit program policies. As of July 2014, Ex-Im had updated the Manual to include transaction assessments that call for standardized audits to evaluate transaction compliance with federal and Ex-Im credit program policies.

In its September 2013 report, the IG also noted that Ex-Im's record-keeping practices were inadequate.⁴⁶ The IG noted that while the stated goal of Ex-Im's Records Management Policy is the efficient and effective management of records and access, it did not address "how, where and by whom" loan documentation is to be maintained. Examples included records maintained by various individuals and divisions, requested files that could not be easily located, and disagreement on when and what files were to be transferred to Ex-Im's central records facility. The IG noted that the lack of access to certain files hindered its ability to assess Ex-Im's operations. We were similarly hindered in our testing of loan guarantee transactions. For example, we estimate that in 57 percent of the medium- and long-term loan guarantee transactions, all loan documentation was not kept in the loan file.⁴⁷ In its September 2013 report, the IG recommended that Ex-Im evaluate its record-keeping practices to identify operational risks and to develop and implement a plan to address deficiencies. Ex-Im agreed with the recommendation and stated that it would evaluate its record-keeping practices and implement improvements in this area to address any deficiencies and operational

⁴⁵Export-Import Bank of the United States, Office of Inspector General, OIG-AR-13-05.

⁴⁶Export-Import Bank of the United States, Office of Inspector General, OIG-AR-13-05.

⁴⁷The 95 percent confidence interval for this estimate is between 44 percent and 70 percent.

risks. As of July 2014, Ex-Im officials stated that Ex-Im is in the process of developing an electronic application to address this recommendation.

Process for Scheduling Delegated Authority Lender Examinations Was Consistent with Federal Guidance but Was Not Documented

Ex-Im used a risk-based approach to schedule delegated authority lender examinations to verify that approvals made under delegated authority were done according to Ex-Im standards. However, this risk-based approach for scheduling these examinations was not documented. Ex-Im's written procedures require examinations of its delegated authority lenders for working capital guarantee transactions at least yearly or more frequently if follow-up examinations are required to verify that corrective action is taken by the lender on any weaknesses found during the annual examination. However, Ex-Im officials stated that because of a lack of needed staff and resources, Ex-Im was using a risk-based approach to schedule the examinations, which was in accordance with OMB Circular No. A-129. Under this risk-based approach, lenders with less risk and less volume may have their examinations extended past the 12-month period. For example, for the 18 lenders that approved working capital loan guarantees in our review, Ex-Im performed annual examinations for 4 lenders, performed less frequent examinations for 12 lenders, and did not perform examinations for 2 of the lenders. Internal control standards call for internal controls to be clearly documented.⁴⁸ Documenting the risk-based approach helps ensure consistent scheduling of the delegated authority lender examinations.

While Ex-Im Has Taken Steps to Prevent, Detect, and Investigate Fraud, It Has Not Documented Its Overall Fraud Processes

While Ex-Im has taken steps to prevent, detect, and investigate fraud and officials could describe the steps they use, Ex-Im has not documented its overall fraud process, which is recommended by several authoritative auditing and antifraud organizations as a key step in evaluating and updating these processes. According to Ex-Im officials, the underwriting process is essential to helping to prevent fraud because Ex-Im loan officers undertake a series of assessments to evaluate transaction risk.⁴⁹ Detecting fraud is a potential outcome of the processes Ex-Im uses to monitor guaranteed loans as well as the steps it uses in its claims and recoveries process once a loan defaults. Lenders also play a role in detecting fraud and are required to communicate information to Ex-Im

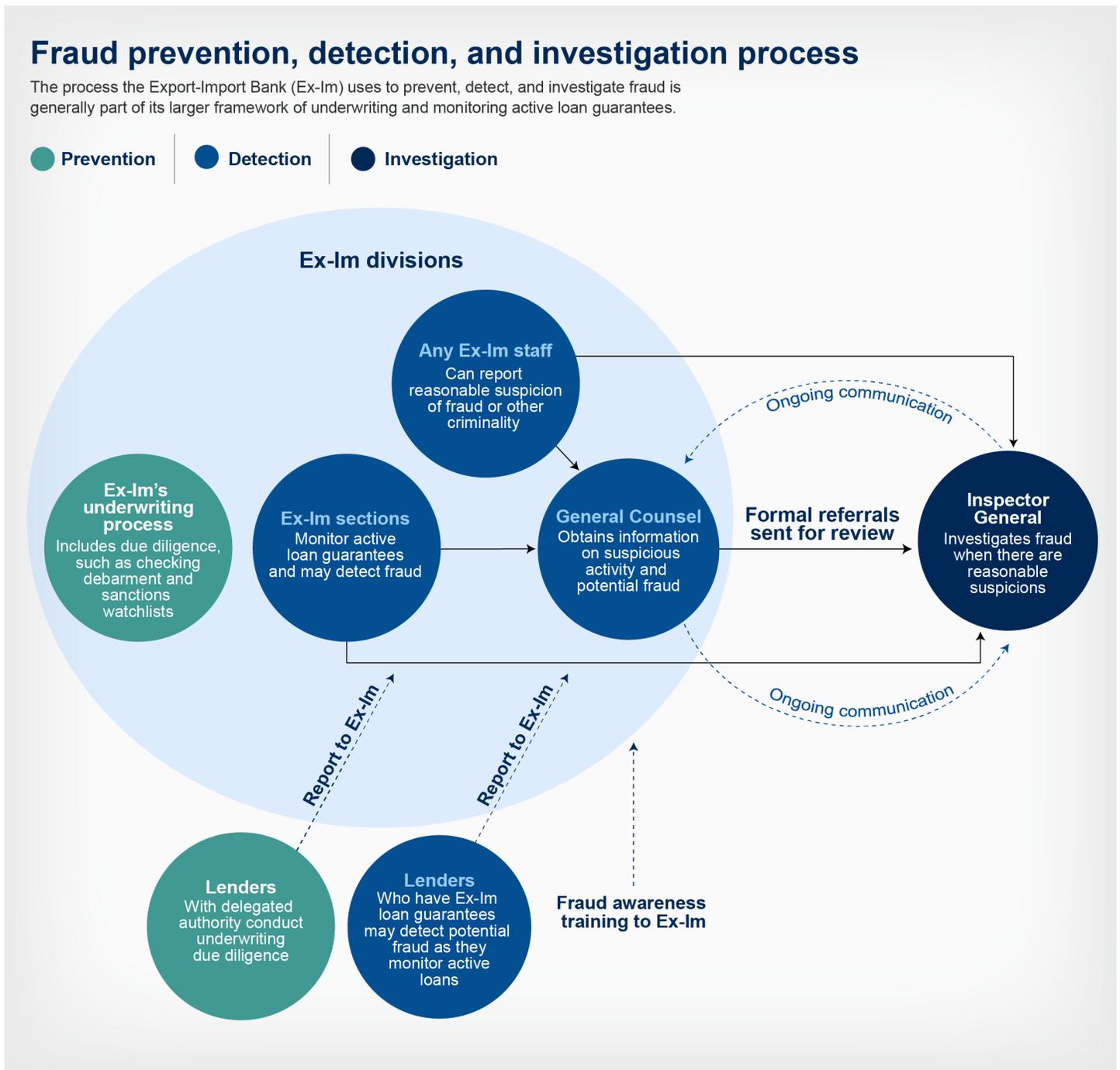
⁴⁸GAO/AIMD-00-21.3.1.

⁴⁹The underwriting process would not necessarily prevent all incidences of fraud, such as fraud because of collusion.

about significant changes in the risk of a loan guarantee. When Ex-Im employees suspect fraud in a loan guarantee, they are to contact Ex-Im's General Counsel (GC) or the IG with these concerns.⁵⁰ Ex-Im's GC compiles relevant information and evidence from sources within Ex-Im and, as appropriate, makes a formal referral to the IG, which is responsible for investigating allegations of potential fraud in Ex-Im's portfolio of loan guarantees (see fig. 6 for an overview of Ex-Im's fraud prevention, detection, and investigation processes).

⁵⁰The IG is an independent office within Ex-Im headed by the Inspector General who is presidentially appointed and Senate confirmed. Pursuant to the Inspector General Act of 1978, Pub. L. No. 95-452 (Oct. 12, 1978), *codified as amended at* 5 U.S.C. app., the IG is under the "general supervision" of the head of the establishment (for Ex-Im, the Chairman and President), but operates independently and has its own budget and personnel authority and a separate appropriation.

Figure 6: Overview of Export-Import Bank's Fraud Prevention, Detection, and Investigation Process



Source: GAO analysis of Ex-Im information. | GAO-14-574

Ex-Im Has Not Documented Its Overall Fraud Process

Ex-Im has not documented its overall process for fraud prevention, detection, and investigation, including mapping out the respective roles and responsibilities of Ex-Im divisions and lenders that are key participants in Ex-Im's efforts in these areas. Auditing and antifraud organizations recommend documenting an organization's fraud policy in part because clearly defined roles and responsibilities help an organization more coherently respond to the risk of fraud.⁵¹ In addition, according to these organizations, documenting an overall antifraud policy is also a key step in enabling an agency to evaluate and test its antifraud processes for effectiveness and to update these processes as appropriate. Furthermore, if an organization publicly communicates certain aspects of its fraud detection policy, it can create a deterrent effect. Likewise, internal control standards call for internal controls to be clearly documented and communicated to employees.⁵²

As shown in figure 6 and discussed below, Ex-Im uses a variety of organizational divisions in its efforts to prevent, detect, and investigate fraud, as well as lenders and the IG. Ex-Im officials told us that Ex-Im had not yet documented its overall approach to fraud, including clearly describing the processes and roles and responsibilities of divisions within Ex-Im. These officials explained that after a large fraud scheme involving the San Antonio Trade Group was uncovered in 2008,⁵³ Ex-Im focused on improving awareness of fraud across all of the divisions in Ex-Im so that its staff developed and exercised professional skepticism to stay aware of fraud indicators. Creating a strong control environment in which staff are aware of and committed to fraud prevention and detection is a best practice recommended by audit and fraud examination associations. Documenting the antifraud process, including the respective roles and responsibilities of various organizational units involved in the process,

⁵¹Institute of Internal Auditors, American Institute of Certified Public Accountants, and Association of Certified Fraud Examiners, *Managing the Business Risk of Fraud: A Practical Guide*.

⁵²[GAO/AIMD-00-21.3.1](#).

⁵³In October 2008, the owner of San Antonio Trade Group, Inc. pled guilty to charges including conspiracy, wire fraud, and money laundering and was sentenced to 117 months in federal prison and ordered to pay restitution of \$10 million and a \$1.1 million special assessment. The owner admitted that from February 2003 to November 2006, he schemed to defraud Ex-Im by stealing millions of dollars in loan proceeds from private U.S. lenders to Mexican business owners and causing multimillion-dollar losses to Ex-Im as it guaranteed those loans based on false applications and support documentation submitted by the owner.

helps to create a sound control environment and to update the approach based on changes in technology, processes, and organization. In addition, documenting the roles and responsibilities of the organizational units helps to identify aspects of the process that could be strengthened.

Ex-Im Considers Its Underwriting Process Essential to Helping Prevent Fraudulent Applications from Being Approved

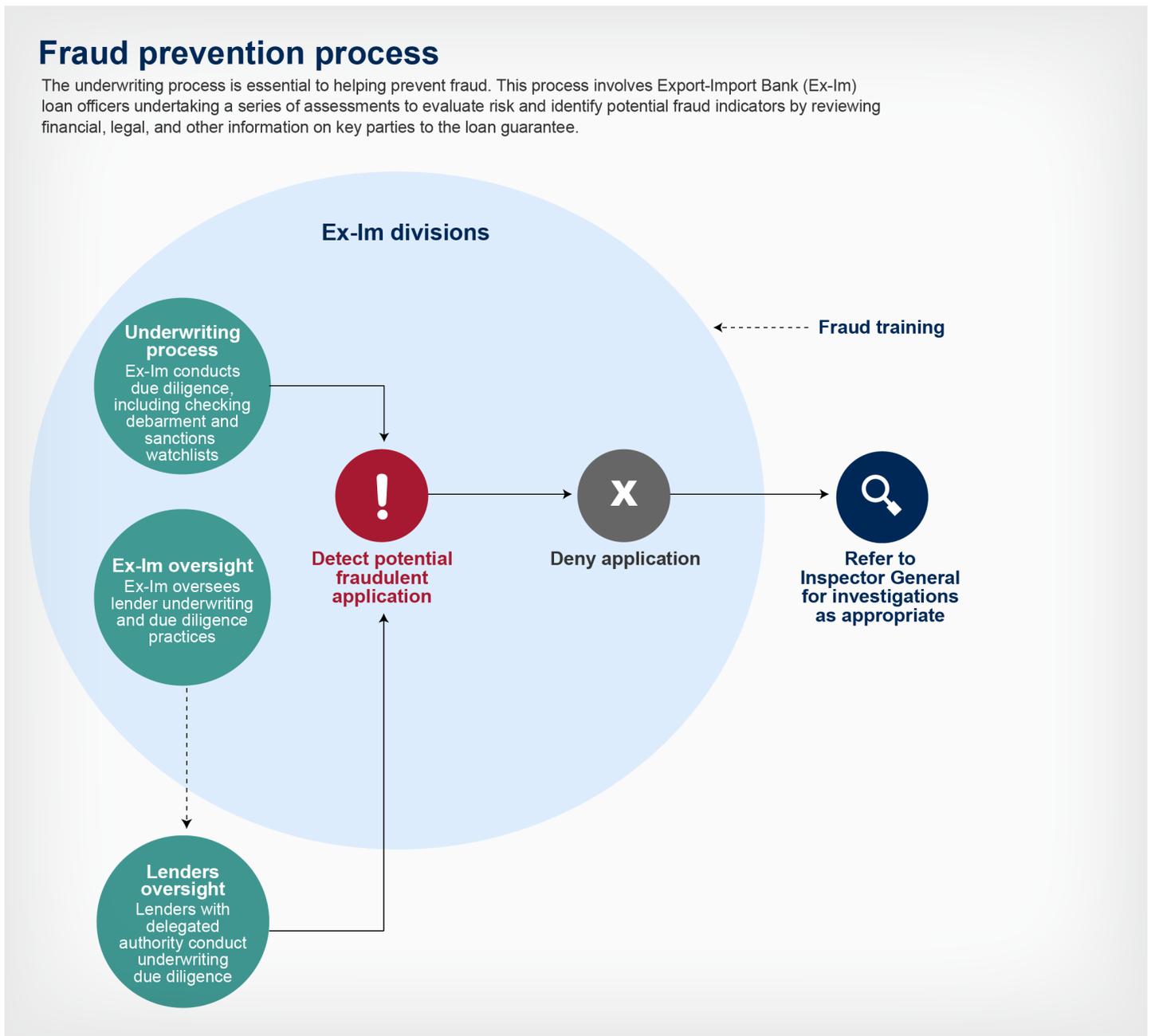
A key principle in any organization's approach to proactively managing fraud risk is to develop effective fraud prevention techniques because preventing dollars from being paid fraudulently is more effective and efficient than attempting to recover these dollars once they have been paid.⁵⁴ Ex-Im officials indicated that the underwriting process is essential to helping to prevent fraud because Ex-Im loan officers undertake a series of assessments to evaluate risk and identify potential fraud indicators by reviewing financial, legal, and other documentation on key parties to a proposed loan guarantee. (See fig. 7 for an overview of fraud prevention processes.) Because the underwriting process involves loan officers reviewing applicant documentation, Ex-Im officials stated that the loan officers sometimes prevent fraudulent applications from being approved when they identify falsified documentation. For example, in one case, an Ex-Im loan officer noticed that the signatures on a new application were identical to the signatures on a previous application as were the submitted financials (for instance, the amount of reported rent was identical to that on a previous application). Ex-Im officials stated that if issues are identified during underwriting, the primary recourse is to deny the application, but loan officers can also report the problem to Ex-Im's GC for further review and follow-up or to the IG for investigation.

⁵⁴Institute of Internal Auditors, American Institute of Certified Public Accountants, and Association of Certified Fraud Examiners, *Managing the Business Risk of Fraud: A Practical Guide*; Institute of Internal Auditors, *Internal Auditing and Fraud* (December 2009); and GAO, *Highlights of a Forum: Data Analytics for Oversight and Law Enforcement*, [GAO-13-680SP](#) (Washington, D.C.: July 2013).

Figure 7: Overview of Export-Import Bank's Fraud Prevention Process

Fraud prevention process

The underwriting process is essential to helping prevent fraud. This process involves Export-Import Bank (Ex-Im) loan officers undertaking a series of assessments to evaluate risk and identify potential fraud indicators by reviewing financial, legal, and other information on key parties to the loan guarantee.



Source: GAO analysis of Ex-Im information. | GAO-14-574

In addition to loan officers identifying potentially falsified documentation, Ex-Im officials identified the following aspects of the underwriting process as contributing more directly to fraud prevention. As noted earlier, however, we identified issues in some of these areas that could limit the effect these areas have on the overall fraud prevention process.

- **Character reviews of key parties to the transaction:** Ex-Im's Character, Reputational, and Transaction Integrity review is designed to identify, among other things, potential risks related to the possibility that parties to the transaction are not legitimate or have been involved with fraud, corruption, or other suspect practices. Before recommending approval of a loan guarantee, loan officers are required to submit the corporate and individual names and addresses of lenders, borrowers, guarantors, and other transaction participants to the Ex-Im Library. As noted earlier, library staff search a series of 20 databases that include various U.S. government and international debarment and sanction lists for any red flags. This practice is similar to searching major international financial institutions' debarment lists—an approach recommended by the Organisation for Economic Co-operation and Development for export credit agencies.⁵⁵
- **Credit review:** Once a transaction is considered eligible for Ex-Im support, the loan officer reviews the creditworthiness of the borrowers involved in the proposed loan guarantee transaction, which can help prevent opportunities for fraud, according to Ex-Im officials.
- **Collateral requirements:** Ex-Im requires collateral for medium-term loan guarantee transactions, which officials told us was in response to higher levels of fraud in this type of loan guarantee. Since this requirement was introduced, officials told us they have seen a decrease in the frequency of fraud within medium-term loan guarantee transactions, which they believe can be attributed at least in part to the collateral requirements.

⁵⁵The Organisation for Economic Co-operation and Development (OECD) is an international economic organization of 34 countries whose mission is to promote economic growth, financial stability, trade and investment, technology, innovation, and development cooperation. It exists as a forum of governments committed to democracy and the market economy, and provides a platform for its members to seek solutions to common problems, including those related to economic, social, and environmental changes. The debarment list review of major international financial institutions was one of the measures included in the OECD Recommendation on Bribery and Officially Supported Export Credits that was adopted by the OECD Council in December 2006.

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- **Oversight of delegated authority lenders:** Since Ex-Im does not perform underwriting for loan guarantees that fall under delegated authority, Ex-Im's fraud prevention activities rely on the delegated authority lenders and Ex-Im's oversight of these lenders. Ex-Im accomplishes this oversight through the delegated authority lender examinations.
 - **Fraud awareness training:** In accordance with best practices from auditing and antifraud organizations, having a strong training program is another element of an effective fraud prevention strategy.⁵⁶ Ex-Im officials reported providing fraud training to their staff using several different sources. Officials stated that the IG generally conducts fraud training for Ex-Im staff about every 18 months. For example, officials reported that the IG provided fraud awareness training to Ex-Im's AMD in November 2013 on lessons learned through fraud investigations, money laundering trends, and economic and trade finance schemes. Ex-Im also leverages its internal knowledge of fraud by having its CRC provide agency-wide training on fraud tricks to be aware of. It also supplemented the training with a fraud tips and tricks memo—which lists common fraud indicators and their potential significance—that it provided to Ex-Im staff. Ex-Im staff also told us that a vendor was awarded a 5-year contract to offer formalized fraud training to include two classes each year for Ex-Im staff. This training occurred in January and June 2014.

Ex-Im's Processes to Monitor Risk and Collect Claims Have Occasionally Detected Fraud

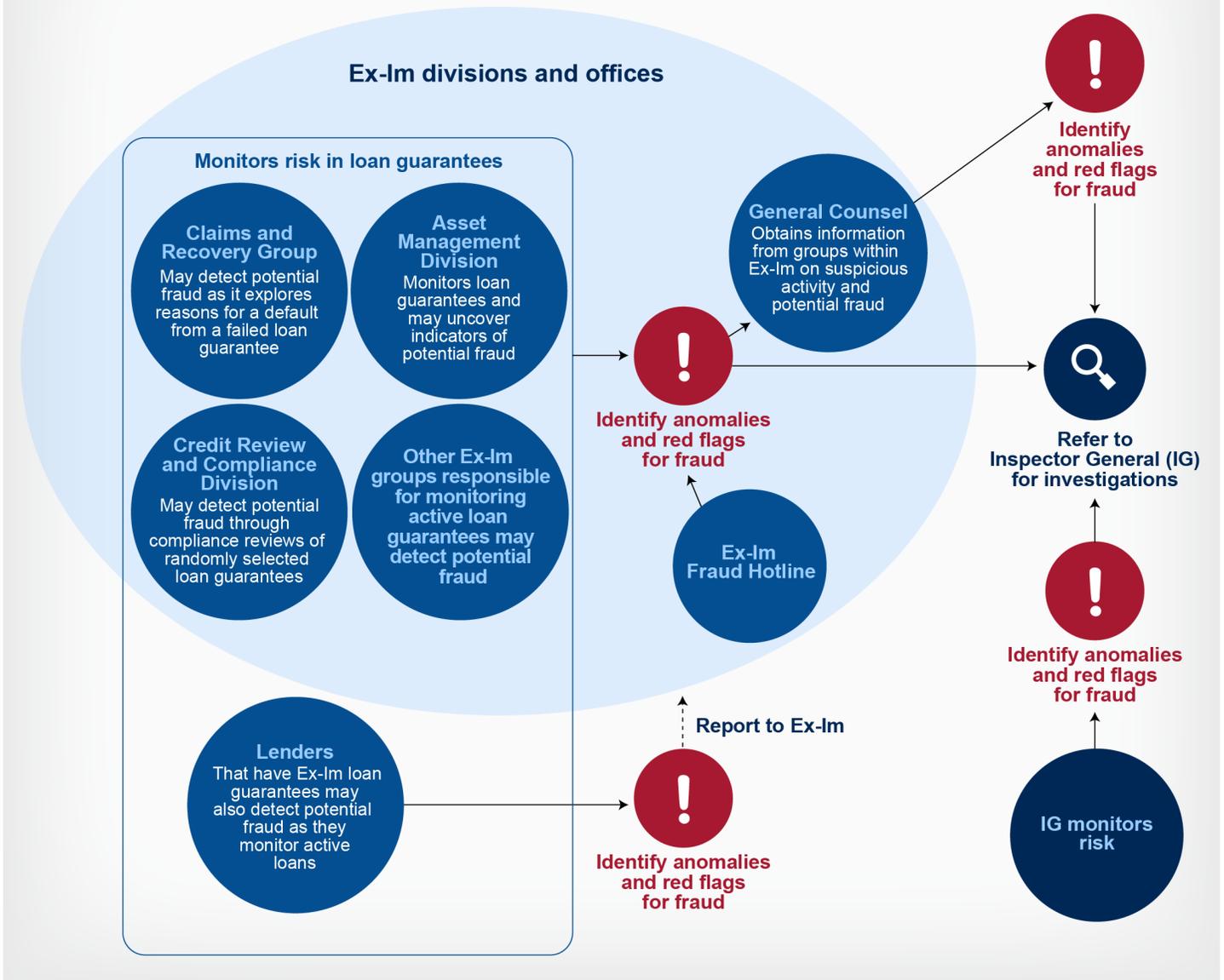
Ex-Im's fraud detection process is a part of its overall monitoring of risk in its loan guarantee portfolio and the steps it uses during its claims and recovery process (see fig. 8).

⁵⁶Institute of Internal Auditors, American Institute of Certified Public Accountants, and Association of Certified Fraud Examiners, *Managing the Business Risk of Fraud: A Practical Guide*, and Institute of Internal Auditors, *Internal Auditing and Fraud*.

Figure 8: Overview of Export-Import Bank's Fraud Detection Process

Fraud detection process

The Export-Import Bank's (Ex-Im) fraud detection process is part of its overall monitoring of risk in its loan guarantee portfolio and the steps it uses during its claims and recovery processes.



Source: GAO analysis of Ex-Im information. | GAO-14-574

Monitoring Risk in Its Portfolio

Ex-Im officials stated that once a loan guarantee is active, they use the following processes to monitor risk in Ex-Im's portfolio and that these risk monitoring processes sometimes help officials detect fraud.⁵⁷

- Ex-Im's CRC directly monitors loan guarantee transactions by selecting and reviewing a random sample of loan guarantee transactions for compliance with internal Ex-Im policies and procedures and ensures that the transactions occurred as outlined in the terms of the loans. According to Ex-Im officials, these reviews occur after the guarantees have been approved by Ex-Im and the funds have been disbursed by the lenders. Officials stated that these reviews have the potential to uncover irregularities and indicators of potential fraud—such as goods not being delivered or inappropriate documentation—which would result in staff communicating their concerns to Ex-Im's GC or making a referral to the IG for further investigation.
- Ex-Im's AMD monitors the credit and restructuring of medium- and long-term loan guarantees by annually reviewing each loan guarantee to determine if any changes in the risk rating are necessary. Officials stated that this review can create an opportunity to detect potential fraud.⁵⁸ According to Ex-Im's IG, which tracks the sources of referrals it receives, AMD has referred 64 cases of potential fraud to the IG for investigation since 2007.

⁵⁷We have previously made recommendations to Ex-Im to help manage operational risks stemming from Ex-Im's increased business volume, which include the risk of fraud. In addition, the Ex-Im IG recommended that Ex-Im develop a systematic approach related to addressing portfolio risk, and appoint a chief risk officer to oversee the design and implementation of an agency-wide risk management function, including development of an overarching risk management policy. In response, in 2013, Ex-Im established the Enterprise Risk Committee (ERC) responsible for creating a risk management strategy that includes objectives, assignment of responsibilities, key performance indicators, and key risk indicators. Ex-Im officials stated that the ERC has been meeting on a monthly basis since November 2013, acting as a senior management working group across divisions, and in December 2013 Ex-Im hired its Executive Vice President and Chief Risk Officer, who serves as the Chair of the ERC. Officials told us that the ERC is focused on broadly defined risk across Ex-Im.

⁵⁸Ex-Im's Transportation Portfolio Management Division had similar responsibilities to monitor compliance, but for transportation-related borrowers and guarantors, which tend to involve large, long-term direct loans and loan guarantees.

Reporting Requirements for Lenders

Ex-Im also tracks the status and probability of repayment of the loans it guarantees through lender reporting requirements, which Ex-Im officials noted provide another mechanism for Ex-Im to possibly detect fraud. Lender reporting requirements are outlined in the terms of a Master Guarantee Agreement—a document signed by Ex-Im and the lender to describe the responsibilities of each party. Specifically, lenders are required to inform Ex-Im of “material changes” in a guaranteed loan, meaning any changes a lender reasonably determines could materially and adversely affect the borrower’s ability to repay its debt, and that can stem from a poor business climate or potential fraud. For example, one lender contacted Ex-Im officials when a random audit, which the lender performed in 2006 as part of its own monitoring activities, found suspicious invoices for the sale of over \$1 million of heavy equipment. Specifically, the lender found that an exporter provided false bills of lading—including one on which the vessel listed had never traveled to the port indicated. Also, the buyers listed on the false bills of lading claimed they never placed orders for the equipment. According to IG officials, this case was investigated by the IG, and in 2010, the owner of the export company was convicted of mail fraud.

In addition, lenders indicated that they communicate with Ex-Im about changes to a loan guarantee that did not constitute material changes but represent causes for concern. For example, officials from one lender informed Ex-Im when they learned that an equipment company appeared to have a partial ownership in the exporter that the equipment company used to ship its product—a situation that can facilitate collusion by producing false shipping documents for products that were paid for through an Ex-Im guaranteed loan but were never actually shipped.

Claims and Recovery Process

When a guaranteed loan defaults, the guaranteed lender or exporter will typically file a claim with Ex-Im. As part of the claims process, Ex-Im’s Claims and Recovery Group typically drafts and sends a “demand for payment” letter to the delinquent borrower, and these letters sometimes elicit suspicious responses that may indicate defaults because of fraud. For instance, in response to a demand for payment letter, a borrower disputed Ex-Im’s claim and provided documentation that it had made timely payment to the lender through a wire transfer. Claims officials also discovered that the exporter had submitted three other claims for reimbursement to Ex-Im around the same time. Given the payment made by the buyer, Ex-Im officials concluded it was likely that the exporter submitted a fraudulent claim to Ex-Im and referred the exporter to Ex-Im’s IG for further investigation, which was ongoing as of July 2014.

Ex-Im officials stated that the recovery process, in which Ex-Im determines the best options for maximizing the amount the defaulted party repays the lender, is the most common way that Ex-Im detects fraud. Because the recovery process involves activities such as physical reviews of the borrower's assets and recovery officials going on-site to meet with the parties involved with the transaction, Ex-Im officials said that this process provides the most definitive opportunities to uncover discrepancies that indicate fraud. For example, in one case Ex-Im's recovery officials determined that the exporter and buyer of a defaulted loan guarantee were family members and business-related documentation showed a likely relationship between the companies, such as having the same address for the borrower and exporter on bills of lading and websites.

Monitoring Trends and Patterns

Ex-Im officials stated that the Claims and Recovery Group observes trends and patterns in claims that can aid Ex-Im in detecting fraud. For example, Claims and Recovery staff may observe a concentration of claims by certain buyers, exporters, or lenders or in certain geographic areas and industries (e.g., farming equipment, energy projects, or agricultural products such as seed). Officials described two instances in which country-based fraud patterns were identified by their staff. In the first instance, the staff reviewing claims realized that there was an increase in claims from the Philippines. Officials noted that the pattern was not immediately apparent because a number of different parties were involved in the claims but they considered the increase in claims from a single country to be a potential fraud indicator, and claims staff referred these claims to Ex-Im's GC for investigation. In another case, claims staff noticed a spike in claims from a single lender for loans to buyers in a single country. Further review by staff from CRC uncovered other anomalies involving this lender. The reviews by both claims staff and CRC led to uncovering a fraud scheme involving the lender's staff in that foreign country.

Role of Ex-Im General Counsel

According to Ex-Im officials, Ex-Im's GC plays a role in fraud detection by collecting additional information on fraud concerns reported to GC by Ex-Im staff and developing formal referrals to Ex-Im's IG when additional

information indicates that such action is warranted.⁵⁹ GC officials explained that if a preliminary assessment suggests that a crime may have occurred, they will make a formal referral to the IG. If the concerns do not rise to that level, GC will make an informal referral to share information with the IG. According to the IG, since 2007, Ex-Im's GC has made 104 referrals for investigation to the IG of information that Ex-Im employees believed indicated potential fraud.

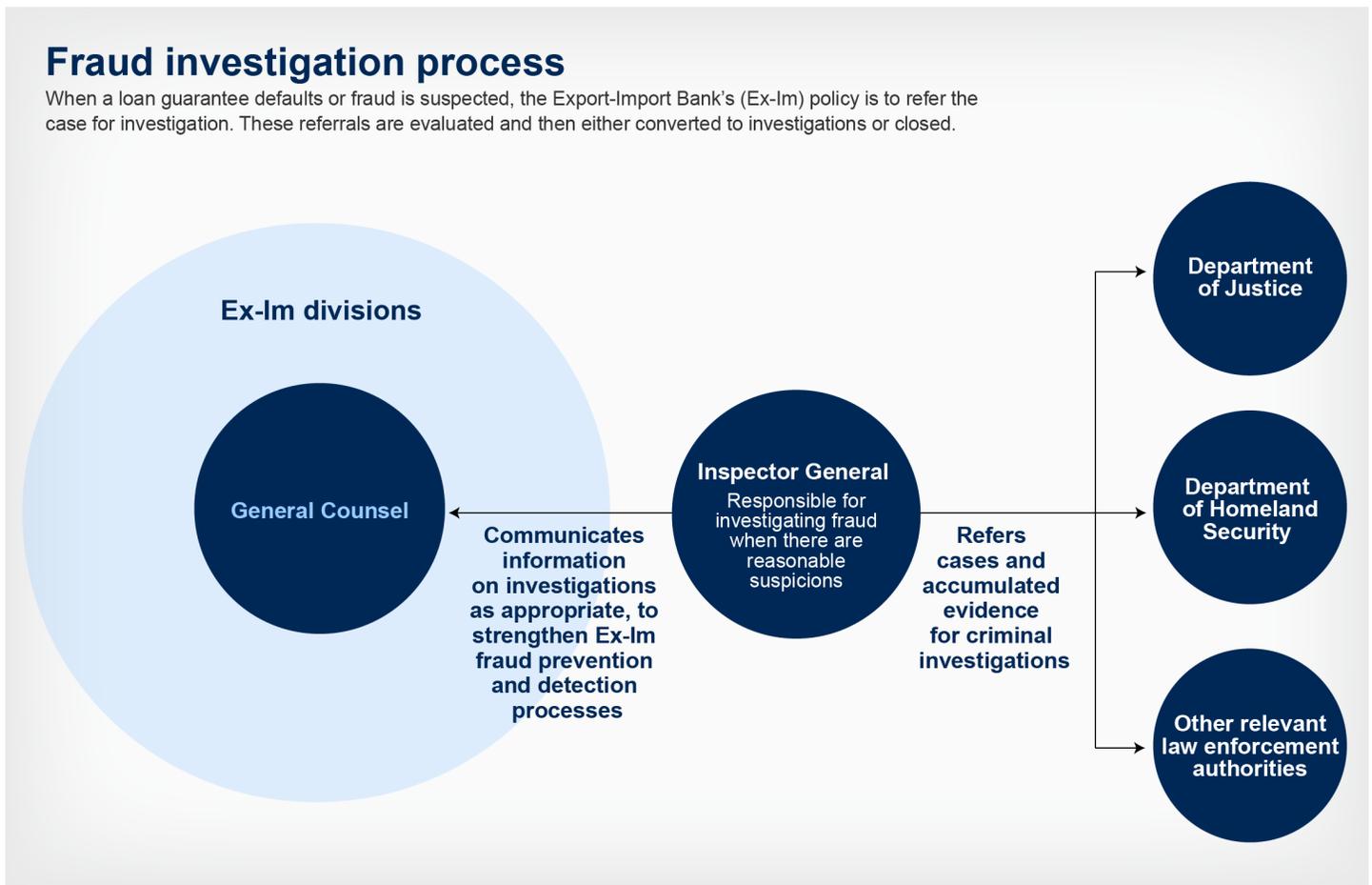
When a Loan Guarantee Defaults and Fraud Is Suspected, Ex-Im Refers the Case for Investigation

If Ex-Im staff determined that fraud may be the underlying cause of a default, Ex-Im can work with the IG to leverage the IG's investigative resources to pursue involved parties (see fig. 9).⁶⁰ According to Ex-Im officials, determining whether a default occurred because of fraud can be complex—there is no single formula for determining whether a guaranteed loan defaulted because of fraud or for another reason, and this determination can take time. IG officials stated that many of the guaranteed loans that defaulted because of fraud may not be flagged until 6 months after a loan was disbursed, depending on the terms of the loan, because some loans do not require an initial payment for 6 months or longer. In addition, IG officials stated that sometimes parties that obtained financing through fraudulent means that were not detected during the underwriting process will actually make an initial payment or two in order to seem more legitimate and put additional time and space between them and a default and investigation. When a guaranteed loan defaults within 6 to 12 months between the first advance and first payment in the loan term, Ex-Im officials said that they generally consider the default to be a potential fraud situation because it is less likely that a loan would make it through the underwriting process and be extended only to have its business condition deteriorate so quickly that it would default early in the life of the guaranteed loan.

⁵⁹According to Ex-Im officials, employees can go directly to the Ex-Im IG with concerns or they can refer cases to Ex-Im's GC so that GC can conduct additional due diligence to compile additional relevant information regarding a fraud allegation that Ex-Im may subsequently refer to the IG. GC officials noted that they conveyed to employees that employees have free and unfettered access to the IG but that it was helpful for GC to remain cognizant of potential fraud since Ex-Im had concerns about such instances that may be different in focus than those of the IG.

⁶⁰The IG consists of both auditors, who review Ex-Im's internal activities, and criminal investigators and analysts, who follow up on allegations of waste, fraud, and abuse. As of July 2014, the IG's Office of Investigation was staffed with the Assistant Inspector General for Investigations, the Deputy Assistant Inspector General for Investigations, two special agents, an investigative analyst, and a financial analyst.

Figure 9: Overview of Export-Import Bank's Fraud Investigation Process



Source: GAO analysis of Ex-Im information. | GAO-14-574

The IG receives information on potential fraud from several sources, including Ex-Im's GC, other Ex-Im staff, and its anonymous tip hotline. IG officials told us that information on potential fraud is initially processed in the IG's case management system as complaint evaluations, which are evaluated and then either converted to investigations or closed. The IG also stated that it partners with the Department of Homeland Security and other law enforcement agencies, such as Interpol, U.S. Customs and Border Protection, and the U.S. Marshals Service, to leverage their resources in investigations and refers investigative matters to other law enforcement agencies for further criminal investigation. Since its inception in 2007, the IG reported processing 325 complaint evaluations with over

120 of these resulting in investigations, and since January 2009, the IG reported obtaining 70 indictments, garnering approximately \$224 million in criminal fines, forfeitures, and restitution and approximately \$54 million in direct repayments and cost savings to Ex-Im.

When appropriate, the IG communicates information about potential fraud to GC to help broaden Ex-Im's awareness of parties and schemes that could make Ex-Im vulnerable to fraud. Since 2009, in 471 instances the Ex-Im IG provided investigative information to Ex-Im's GC concerning potential fraud that the IG believed was appropriate for enhanced due diligence. For instance, according to a director in the Trade Finance Group, an individual applied for every form of financing Ex-Im offered and consistently supplied substantially incomplete documentation for the applications. The IG determined that the individual also applied for Ex-Im financing under a different company's name that the IG had flagged for concern. The IG provided this information to GC so that Ex-Im could conduct additional due diligence on the company to ensure that no potentially fraudulent applications had been approved.

Conclusions

Ex-Im's Manual for underwriting provided a framework for loan officers to determine that only qualified applicants representing reasonable assurance of repayment were provided loan guarantees. While loan officers documented many key aspects of the underwriting process as required by the Manual, the process could be enhanced if certain procedures to be performed and sufficiently detailed instructions on how certain procedures should be performed and documented were included in the Manual. For example, the Manual did not include procedures for verifying that loan guarantee transaction applicants were not delinquent on federal debt, or for performing assessments of collateral for nonaircraft medium- and long-term loan guarantee transactions. In addition, mechanisms to oversee compliance with Ex-Im's established procedures, including those related to documenting the determination of export item and country eligibility and documenting the analysis of country exposure, did not exist. Furthermore, while Ex-Im implemented a risk-based approach to delegated authority lender examinations, the approach was not documented. Improvements in these areas could help enhance the assessment of transaction participant eligibility and the reasonable assurance of repayment and the oversight of lenders, as well as help prevent fraud.

Ex-Im also has not documented its overall process for preventing, detecting, and investigating fraud, including describing the roles and responsibilities of the divisions and officials within Ex-Im and of key

participants in these processes. Doing so would aid in codifying institutional knowledge of these processes and facilitate communication about fraud for employees or lenders who may be new to Ex-Im. In addition, documenting these processes may be particularly important for Ex-Im because a number of divisions are involved in preventing, detecting, and investigating fraud, including but not limited to its AMD, Claims and Recovery Group, GC, and key participants such as Ex-Im's lenders. Documenting the current fraud process is a key step in facilitating evaluations and testing the effectiveness of these processes.

Recommendations for Executive Action

We recommend that the Chairman of the Export-Import Bank of the United States direct the appropriate officials to take the following six actions:

- Develop and implement procedures, prior to loan guarantee approval, for (1) verifying that transaction applicants are not delinquent on federal debt, including using credit reports to make such a determination, and (2) performing assessments of collateral for nonaircraft medium- and long-term loan guarantee transactions.
- Establish mechanisms to oversee compliance with Ex-Im's existing procedures, prior to loan guarantee approval, for (1) obtaining credit reports for transaction borrowers or documenting why they were not applicable; (2) documenting certain eligibility procedures, including the Character, Reputational, and Transaction Integrity reviews for medium- and long-term loan guarantee transactions, export item eligibility, and country eligibility; and (3) documenting the analysis of country exposure.
- Develop and implement detailed instructions, prior to loan guarantee approval, for (1) preparing and including all required documents or analyses in the loan file and (2) using credit reports in the risk assessment and due diligence process.
- Update the Character, Reputational, and Transaction Integrity review process to include the search of databases to help identify transaction applicants with delinquent federal debt that would then not be eligible for loan guarantees.
- Document Ex-Im's current risk-based approach for scheduling delegated authority lender examinations.

-
- Document Ex-Im’s overall fraud process, including describing the roles and responsibilities of Ex-Im divisions and officials that are key participants in Ex-Im’s fraud processes.

Agency Comments and Our Evaluation

We provided a draft of this report to Ex-Im for review and comment. In written comments on a draft of this report, which are reprinted in appendix II, Ex-Im concurred with our six recommendations. Ex-Im also provided technical comments that we incorporated into the final report, as appropriate.

In its written comments, Ex-Im described planned actions to address our recommendations. For example, Ex-Im stated that it will develop and implement procedures for verifying that transaction applicants are not delinquent on federal debt. Ex-Im also stated that management is reviewing its current Character, Reputational, and Transaction Integrity process to assess the inclusion of the Do Not Pay List database. Additionally, Ex-Im stated that it would update its Manual to include current practices related to collateral assessments of nonaircraft medium- and long-term loan guarantee transactions, as well as potential enhancements. Further, Ex-Im stated that it will develop and implement instructions for loan officers regarding the preparation and inclusion of all required documents in a loan file and mechanisms to oversee compliance with Ex-Im’s existing procedures prior to loan guarantee approval. Ex-Im also stated that it would document its risk-based approach for scheduling delegated authority lender examinations and its fraud process, including a description of roles and responsibilities. If implemented effectively, Ex-Im’s planned actions should address the intent of our recommendations.

We are sending copies of this report to appropriate congressional committees, the Chairman of the U.S. Export-Import Bank of the United States, and the Ex-Im Inspector General. The report is also available at no charge on the GAO website at <http://www.gao.gov>.

If you or your staff have any questions about this report, please contact Steve Lord at (202) 512-6722 or lords@gao.gov or Gary Engel at (202) 512-3406 or engelg@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page

of this report. GAO staff who made major contributions to this report are listed in appendix III.



Stephen M. Lord
Managing Director, Forensic Audits and Investigative Service



Gary T. Engel
Director, Financial Management and Assurance

Appendix I: Objectives, Scope, and Methodology

Our objectives were to examine the extent to which the Export-Import Bank of the United States (Ex-Im) (1) adequately designed and implemented procedures to reasonably assure compliance with its underwriting process requirements for loan guarantee transactions and consistency with federal guidance and (2) adequately designed procedures to prevent, detect, and investigate fraudulent applications for loan guarantees.

To assess Ex-Im's design of procedures related to underwriting loan guarantee transactions, we reviewed relevant requirements and guidance, including the Office of Management and Budget's Circular No. A-129, *Policies for Federal Credit Programs and Non-Tax Receivables*; the Department of the Treasury Bureau of the Fiscal Service's *Managing Federal Receivables: A Guide for Managing Loans and Administrative Debt*; GAO's *Standards for Internal Control in the Federal Government*; and the Bureau of Industry and Security's "Know Your Customer" Lending Guidance. We also examined Ex-Im's charter, credit framework, content policy, and other due diligence procedures. We compared the various requirements and guidance to Ex-Im's Loan, Guarantee and Insurance Manual (Manual), which describes, among other things, Ex-Im's procedures for assessing loan guarantee applications and preparing loan agreements.¹ In addition, we reviewed Ex-Im's Office of Inspector General (IG) reports since 2009 related to underwriting issues, various laws applicable to Ex-Im, and GAO reports related to Ex-Im. We also discussed underwriting requirements and the due diligence process with Ex-Im officials. For the implementation of the underwriting process, we identified key procedures from Ex-Im's Manual. We also reviewed Ex-Im's loan files used to document procedures performed during the underwriting process and Ex-Im's financial statements from 2011 through 2013 along with other reports summarizing loan guarantee amounts.

To select loan files to review, we obtained Ex-Im's population of all authorized loan guarantee transactions from October 1, 2011, to March 31, 2013, which included data such as borrower, authorization amount and date, lender name, and product type. The total loan guarantee population contained 275 medium- and long-term loan guarantees totaling \$21.9 billion and 792 working capital loan guarantees

¹Since procedures related to underwriting were recently updated by Ex-Im, we reviewed the procedures in place when the loan guarantees in our review were approved as well as the revised procedures.

totaling \$4.0 billion, which were authorized by Ex-Im from October 1, 2011, to March 31, 2013. To assess the reliability of data provided by Ex-Im, we analyzed information related to data elements and controls, reviewed the data for obvious errors in accuracy and completeness, compared data to published documents, and interviewed knowledgeable Ex-Im officials about the data. We concluded that the data elements we used were sufficiently reliable for purposes of selecting samples of loan guarantee transactions to review and for describing Ex-Im's loan guarantee balances.

Because of the differences in the underwriting process between the working capital loan guarantees and the medium- and long-term loan guarantees, we divided the population into two groups. The medium- and long-term guarantees were combined in one group while the working capital loan guarantees were placed in another group. For each sample, we made estimates for an attribute measure at the 95 percent level of confidence. From the sample design, we were able to conclude that the population error rate was less than 5 percent at the 95 percent level of confidence when no control violations were discovered in the sample. The final samples for the medium- and long-term transactions and the working capital transactions were 54 and 58, respectively.

Because we followed a probability procedure based on random selections, each of our samples is only one of a large number of samples that we might have drawn. Since each sample could have provided different estimates, we express our confidence in the precision of our particular sample's results as a 95 percent confidence interval (e.g., plus or minus 7 percentage points). This is the interval that would contain the actual population value for 95 percent of the samples we could have drawn. Confidence intervals are provided along with each sample estimate in the report. The results from our samples apply to the universe of loan guarantees authorized from October 1, 2011, to March 31, 2013.

Based on our review of the Manual and the key procedures we identified, we developed a data collection instrument for working capital loan guarantee transactions and another data collection instrument for medium- and long-term loan guarantee transactions, which we used to test the two samples extracted from the loan guarantee population.

Working capital loan guarantees. We divided our working capital loan guarantee data collection instrument into delegated authority and nondelegated authority transactions. For each nondelegated authority working capital loan guarantee transaction in our sample, we reviewed

the credit memo to determine if Ex-Im documented the following: credit reports on individual guarantor(s) or Dunn and Bradstreet reports if the guarantor was a business, analysis of contract and payment terms, financial analysis, bank references, collateral, and additionality. We also tested to see if exporter eligibility; Character, Reputational, and Transaction Integrity reviews, which included due diligence for Iran sanctions and other reputational risks; and appropriate signatures for approval from Ex-Im management were documented. For delegated authority working capital loan guarantees, we reviewed the selected transactions for exporter credit reports to determine if Ex-Im addressed any risks associated with the transaction participants and reviewed Dunn and Bradstreet reports on the exporter. We tested to see if all required information and approvals were contained in Ex-Im's Application Processing System, including documentation of the type of loan facility, a product description, primary and secondary collateral, use of proceeds, export markets, export value, loan amount, additionality, and any environmental impacts. In addition, we tested to see if the loan amount on our sample was equal to the loan amount reported in the Application Processing System and that the transaction was properly classified as a working capital transaction. We also tested to see if an Ex-Im program management assistant completed and signed a delegated authority checklist for the borrower that contained information such as the lender, borrower, loan amount, type of facility, letters of credit, warranties, final disbursement date, primary and secondary collateral, and term of the loan. We also tested to see if an appropriate Ex-Im official signed the delegated authority checklist. For each of the delegated authority working capital loan guarantee transactions in our sample, we examined Ex-Im's available examination reports for the applicable delegated authority lenders and tested to see if the approved loan guarantee transaction were within delegated authority lender levels. We requested the three most recent examinations conducted for the 18 lenders involved in the delegated authority transactions from our sample (47 out of the 58 items in our sample were done under delegated authority). For 12 lenders, we received three reports; we received one report for 4 of the lenders and no report for 2 of the lenders.

Medium- and long-term loan guarantees. The key procedures relate to the following four underwriting activities:

(1) Application screening. For this activity, we evaluated the documentation of the eligibility of loan guarantee participants and whether the information contained in the loan guarantee transactions met minimum eligibility criteria standards. We tested to see if the sample

items contained complete transactional party information, including applicant, borrower, guarantor, buyer, lender, end user, exporter, supplier, and guaranteed lender. We determined if the eligibility of the export item was clearly stated or could be clearly assumed in the sample documents. We also tested to see if additionality, country eligibility, and any applicable State Department clearance were recorded. We tested to see if Ex-Im's Credit Review and Compliance Division documented the Character, Reputational, and Transaction Integrity review process prior to loan guarantee approval which included the full request, the participants screened list, and the results of the Ex-Im library's research and determined if issues identified in this review were resolved by viewing the board memo for each long-term loan guarantee transaction and the credit memo for each medium-term loan guarantee transaction. For all board-approved transactions, we also tested to see if the Iran Sanctions Certification was obtained.² For all medium- and long-term loan guarantee transactions, we tested to see if a credit report, a Dunn and Bradstreet report, or both dated within 6 months of the application date, were obtained and maintained or, if not, whether Ex-Im documented why these reports were not applicable. Further, we tested to see if the loan guarantee application contained an antilobbying statement and an Environmental Screening Document.

(2) Risk assessment and due diligence. For this activity, we evaluated the documentation related to financial risk factors and the commercial viability of the loan guarantee transaction. We tested to see if the engineering memo for long-term loan guarantee transactions and the credit memo for medium-term loan guarantee transactions documented the eligibility of costs and the value and eligibility of U.S. and foreign content. For long-term loan guarantee transactions, we tested to see if Ex-Im documented the environmental impact in the engineering report. For medium-term loan guarantee transactions, we tested to see if the Vice President of Ex-Im's Engineering and Environment Division conducted an environmental impact analysis. For long-term loan guarantee transactions that were authorized after May 30, 2012, we tested to see if a summary of economic impact analysis was included.³

²The Iran Sanctions Certification replaced the Prohibited Producer/Refiner questionnaire that was previously required.

³The Export-Import Bank Authorization Act of 2012, Pub. L. No. 112-122, § 12 (May 30, 2012), added an explicit requirement that Ex-Im retain documentation in support of its economic impact analyses.

We also tested to see if Ex-Im documented its due diligence over certain applicable risks and the mitigation of those risks. These risks included country exposure and technical and environmental risk for long-term loan guarantee transactions. In addition, we tested to see if Ex-Im performed due diligence for sovereign risk, political risk, financial institution risk, and nonfinancial institution risk factors for both medium- and long-term loan guarantee transactions. We also reviewed credit and board memos to determine if Ex-Im summarized risks included in credit reports and the mitigating factors for those risks. We further reviewed loan files to determine if the overall budget cost level for both medium- and long-term loan guarantee transactions were documented. For aircraft transactions, we tested to see if the credit and legal strength, weakness, and uncertainties analyses were completed. For medium-term loan guarantee transactions in excess of \$1 million, we tested to see if the transaction risk classification was assessed and documented in the loan file. We tested the appendixes of the credit memo for long-term loan guarantee transactions to see if the financial assessment, engineering report, country risk assessment, risk rating summary, economic analysis, and any special conditions were documented.

(3) Credit structure. For this activity, we evaluated the documentation of the financing terms and conditions, including collateral to be recommended for the loan guarantee transaction. For medium- and long-term loan guarantee transactions, we reviewed the loan file to determine if Ex-Im documented the exposure fee calculator worksheet; the repayment terms, to ensure that the terms did not exceed the useful life of the collateral or scope of supply; the long-term action sheet; and the medium-term decision memo. We tested to see if collateral for the loan guarantee had been identified and assessed and to see if the loan agreement included requirements for the borrower to maintain the collateral, where applicable.

(4) Credit decision. For this activity, we evaluated the approved amount, proper categorization of the loan guarantee, and the appropriate records storage for the loan documentation. For long-term and aircraft loan guarantee transactions, we tested to see if there was approval by an Ex-Im loan officer, an Ex-Im lawyer, and the Vice President of Trade Finance on the credit memo. For medium-term loan guarantee transactions, we tested to see if the credit memo was signed by the appropriate official. For long-term loan guarantee transactions, we tested to see if approval signatures on the board memo were documented. For all selected loan guarantee transactions, we tested to see if the actual loan amount per Ex-Im's Application Processing System was equal to the loan agreement and

equal to or less than the financed amount approved. We also tested to see if the loan agreement was signed by all applicable parties and that the transaction was approved by the appropriate authority level. In addition, we tested to see if the loan was properly categorized as medium or long term and that the loan documentation was kept in the appropriate records storage location.

For any unresolved issues found on both the working capital and medium- and long-term loan guarantee data collection instruments, we followed up with Ex-Im officials to evaluate any additional supporting documentation not originally included in the loan files. Additionally, we interviewed Ex-Im loan officers, directors, and other officials to obtain further perspective on the underwriting process of loan guarantee transactions.

To evaluate whether Ex-Im adequately designed procedures to prevent, detect, and investigate potential fraud in loan guarantee transactions, we identified key procedures by reviewing Ex-Im's established procedures and interviewing officials from the Ex-Im IG. We also interviewed lenders and Ex-Im officials to identify steps Ex-Im has taken to strengthen lender fraud procedures. We evaluated the federal standards and, as appropriate, industry standards and best practices for preventing, detecting, and investigating fraud. We reviewed Ex-Im's practices for verifying that debarred lenders and borrowers have not been authorized to receive loan guarantees. To assess Ex-Im's implementation of procedures to prevent fraudulent applications from being approved, we reviewed the same sample of loan guarantee transactions described above to determine whether Ex-Im effectively implemented its procedures, such as reviewing and evaluating documentation and implementing its Character, Reputational, and Transaction Integrity check, to detect and prevent fraudulent applications from being approved during the underwriting process. To identify and evaluate Ex-Im's processes for detecting potential fraud among active loan guarantee transactions, we interviewed officials about current practices and reviewed documentation of cases showing how Ex-Im detected potential fraud under a variety of circumstances.

We conducted this performance audit from March 2013 to September 2014 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for

our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Comments from the Export-Import Bank of the United States



EXPORT-IMPORT BANK
OF THE UNITED STATES

August 27, 2014

Gary Engel
Director Financial Management and Assurance
U.S. Government Accountability Office
Washington, D.C. 20584

Dear Mr. Engel:

Thank you for providing the Export-Import Bank of the United States ("Ex-Im Bank" or "the Bank") with the Government Accountability Office (GAO) report, "Enhancements Needed in Loan Guarantee Underwriting Procedures and for Documenting Fraud Processes" (August 2014). The Bank supports the GAO's work and audits which complement the Bank's efforts to continually improve its practices and procedures. Ex-Im Bank is proud of its cooperative relationship with GAO.

We are pleased that GAO recognized that Ex-Im Bank has implemented many key aspects of the underwriting process as required by the Bank's Loan, Guarantee, and Insurance Manual. We appreciate that GAO noted the Bank's low amount of claims paid which is due in part to the Bank's underwriting efforts. In FY 2013, the Bank paid \$28.4 million in claims on all guarantee programs, which represents 0.04% percent of the entire \$70.3 billion portfolio.

GAO has made six recommendations in this report regarding loan guarantee underwriting due diligence and documentation of fraud processes. These recommendations deal primarily with enhancing documentation and providing detailed instructions to Bank staff in the Loan, Guarantee, and Insurance Manual.

Recommendation 1: Develop and implement procedures, prior to loan guarantee approval, for (1) verifying the transaction applicants are not delinquent on federal debt, including using credit reports to make such a determination and (2) performing assessments of collateral for non-aircraft medium and long-term loan guarantee transactions.

Management response: Management concurs with this recommendation.

811 VERMONT AVENUE, N.W. WASHINGTON, D.C. 20571

The Bank will develop and implement procedures, including the use of credit reports as applicable, for verifying the transaction applicants are not delinquent on federal debt. Currently all relevant transaction parties must certify they are not delinquent on any amounts due and owing to the U.S., they have not been suspended or debarred by the U.S. government, and that they have paid all federal, state and local taxes and material judgments. These certifications are subject to penalties for false or misleading statements to the U.S. government (18 U.S.C. 1001, et seq.).

Management is currently reviewing and evaluating its current Character, Reputational, and Transaction Integrity (CRTI) process, and expects to have this completed by the end of this calendar year. The review includes an assessment of the Do Not Pay List database and consideration of its inclusion into the database check currently conducted by the Bank for all transactions. The Bank's current Know Your Customer standards, implemented in May 2014, include independent credit reports under due diligence documents, and provide for loan officers to "obtain and review tax records" as additional due diligence when applicable. In addition, the Bank will instruct loan officers on the use of credit reports, and documenting when a credit report is not required for the transaction.

The Bank also agrees with the second part of the recommendation. It is important to note that the Bank does perform assessments of collateral for non-aircraft medium and long term guarantee transactions. The GAO recommendation is to document current practices in the Manual for performing assessments of collateral for non-aircraft medium and long term guarantee transactions. Ex-Im Bank currently evaluates each medium and long term export contract which is used as an appropriate assessment of collateral for non-aircraft transactions. The Bank will update the Manual to include current practices as well as potential enhancements.

Recommendation 2: Establish mechanisms to oversee compliance with Ex-Im's existing procedures, prior to loan guarantee approval, for (1) obtaining credit reports for transaction applicants or documenting why they were not applicable; (2) documenting certain eligibility procedures, including the Character, Reputational, and Transaction Integrity reviews for medium and long-term loan guarantee transactions, export item eligibility, and country eligibility; and (3) documenting the analysis of country exposure.

Management response: The Bank concurs with this recommendation.

As stated in the report, the Bank believes credit reports are not usually the most reliable and current sources of information, and as a result the Loan Officer's due diligence is much more extensive than what a credit report may be able to provide. Ex-Im requires in long term transactions, at a minimum, three years of audited financial statements and significant business operation and management information. To the extent possible, Ex-Im also uses credit rating reports such as Moody's and Standard and Poor's, initial public offering (IPO) or bond

prospectuses, industry information, project and export information, financial projections, and supporting underlying contracts and memoranda. This is in addition to all the contractually required certifications which may be subject to penalties for false or misleading statements to the U.S. government (18 U.S.C. 1001, et seq.). The Bank will assess the existing procedures and requirements for obtaining credit reports, and will update the Manual on the use of credit reports, and documenting when a credit report is not required for the transaction.

Ex-Im will develop mechanisms to oversee compliance with Ex-Im Bank's existing procedures, prior to loan guarantee approval, for documenting certain eligibility procedures, including the Character, Reputational, and Transaction Integrity reviews for medium and long-term loan guarantee transactions, export item eligibility, country eligibility, and the analysis of country exposure. The Bank also plans to review the Loan, Guarantee, and Insurance Manual to determine if certain elements in the current eligibility procedures and requirements need to be updated. Ex-Im Bank has also created a Business Compliance Group to work with Bank staff to develop procedures to ensure transactional compliance with requirements.

Recommendation 3: Develop and implement detailed instructions, prior to loan guarantee approval, for (1) preparing and including all required documents or analyses in the loan file and (2) using credit reports in the risk assessment and due diligence process.

Management response: The Bank concurs with this recommendation.

The Bank will develop and implement instructions for loan officers regarding the preparation and inclusion of all required documents in the loan file. As mentioned above, the Bank has created a new Business Compliance Group to work with Bank staff to develop procedures to ensure transactional compliance with requirements. The group will work with loan officers to develop processes for documentation and ensure the required documentation is contained in each loan file.

The Bank will assess the existing procedures and requirements for obtaining credit reports, and update the Manual on the use of credit reports as applicable in risk assessment and due diligence processes, and documenting when a credit report is not required for the transaction.

Recommendation 4: Update the Character, Reputational, and Transaction Integrity review process to include the search of databases to help identify transaction applicants with delinquent federal debt that would then not be eligible for loan guarantees.

Management response: The Bank concurs with this recommendation.

Management is currently reviewing and evaluating its current Character, Reputational, and Transaction Integrity (CRTI) process, and expects to have this completed by the end of this

calendar year. The review includes an assessment of the Do Not Pay List database and consideration of its inclusion into the database check currently conducted by the Bank for all transactions. The Bank's current Know Your Customer standards, implemented in May 2014, include independent credit reports under due diligence documents, and "obtain and review tax records" as additional due diligence when applicable.

Recommendation 5: Document Ex-Im's current risk-based approach for scheduling delegated authority lender field exams.

Management response: The Bank concurs with this recommendation.

Ex-Im Bank will update the Manual to include a current risk-based approach for scheduling delegated authority lender field exams. This update will be completed by December 31, 2014.

Recommendation 6: Document Ex-Im's overall fraud process, including describing the roles and responsibilities of Ex-Im divisions and officials that are key participants in Ex-Im's fraud processes.

Management response: The Bank concurs with this recommendation.

The Bank appreciates the GAO report acknowledging that the Bank has taken steps to "prevent, detect, and investigate fraud" including training for staff by the OIG, the Bank's Credit Review and Compliance Division, and an external vendor contracted to provide formalized training. The Bank will develop a document which encompasses the Bank's comprehensive fraud process, describing the roles and responsibilities of Ex-Im divisions and officials that are key participants in Ex-Im's fraud processes.

We thank the GAO for your efforts to ensure the Bank's policies and procedures continue to improve, as well as protect the U.S. Taxpayer from fraud, waste, and abuse.

Sincerely,



Charles J. Hall
Executive Vice President and Chief Risk Officer
Export-Import Bank of the United States

Appendix III: GAO Contacts and Staff Acknowledgments

GAO Contacts

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Staff Acknowledgments

In addition to the contacts named above, Marcia Carlsen (Assistant Director), Joah Iannotta (Assistant Director), Jeanette Brahame, Michael Bird, Katy Crosby, Dennis Fauber, Natasha Guerra, Cole Haase, Debra Hoffman, Dragan Matic, and Carroll Warfield Jr. made key contributions to this report.

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