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~~REPORT ON A LETTER WHICH RAISED CERTAIN QUESTIONS  
REGARDING THE INVESTIGATION OF THE SMALL BUSINESS  
ADMINISTRATION~~

B-162307  
7-28-79

**RESTRICTED**

Report to Congressman John R. Dellenback pursuant to his request regarding a letter from Mrs. Jeannette Marshall who questioned certain statements in our report dated February 6, 1970 (B-162307), concerning the Small Business Administration's (SBA) foreclosure action on a loan to Mr. and Mrs. Stanley D. Nutesa for the Rose Motel, Phoenix, Oregon.

We advised the congressman that after evaluating Mrs. Marshall's comments, we continued to believe that the available evidence does not support a conclusion that there was any improper conduct by SBA representatives in their administration of the foreclosure action on the loan or a conclusion that SBA's investigation of the matter was biased.

[Comments on Questions Concerning a Report to a Congressman]

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**FOLLOW-UP EXAMINATION OF THE  
ADMINISTRATIVE ACTION ON A LOAN  
TO THE ROYAL HOTEL, PHOENIX,  
ARIZONA - SMALL BUSINESS  
ADMINISTRATION**

B-168307  
7-28-70

**RESTRICTED**

In response to a request dated May 11, 1970, we reported to the Honorable John R. Dellenback on questions raised by a constituent on our previous report to him dated February 6, 1970. We reported that after evaluating the constituent's comments, we continued to believe that the available evidence did not support a conclusion that there was any improper conduct by SBA representatives in their administration of the foreclosure action on the loan or a conclusion that SBA's investigation of the matter was biased.

Revised

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**FOLLOW-UP EXAMINATION OF THE  
FORECLOSURE ACTION ON A LOAN  
TO THE ROSE MODEL, FROBICK,  
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B-168307

7-28-70

**LOANS**

Follow-up review of allegations of improper conduct in connection with foreclosure action

**SMALL BUSINESS ACTIVITIES**

Follow-up review of allegations of improper conduct in connection with foreclosure action

Revised



**RESTRICTED** — Not to be released outside the General Accounting Office without specific written approval by the Office of Management and Organization. A record of which is kept by the Office of Management and Organization, Definitions Branch, OAS

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*Small Business  
Administration*

JUL 28 1970

Dear Mr. Dellenback:

Your letter of May 11, 1970, requested our [comments on a letter] dated May 1, 1970, that you had received from Mrs. Jeannette Marshall. Mrs. Marshall [questioned] certain statements in our report to you dated February 6, 1970 (B-168307), [concerning the Small Business Administration's (SBA) foreclosure action] on a loan to Mr. and Mrs. Stanley D. Mustoe for the Rose Motel, Phoenix, Oregon. After evaluating Mrs. Marshall's comments, we continue to believe that the available evidence does not support a conclusion that there was any improper conduct by SBA representatives in their administration of the foreclosure action on the loan or a conclusion that SBA's investigation of the matter was biased.

Mrs. Marshall stated:

"Please refer to the letter to you dated October 29, 1969, from Hilary Sandoval, Jr., Administrator of S.B.A., in which he stated (paragraph 2): 'There has been discovered no arrangement between the vendors of the note. (Mr. and Mrs. John Scupien), SBA, any potential buyer and Dean Vincent, Inc. (or any of its employees) whereby the Rose Motel would be sold at a sacrifice price.' But the documents you sent me were already six months old at the time he denied their existence!"

We cannot conclude that Mr. Sandoval's statement, referred to by Mrs. Marshall, denied the existence of the mentioned documents (the earnest money agreement and a letter from the realtor transmitting the agreement to the Scupiens' attorney). Actually, the Administrator indirectly referred to the agreement in his letter to you of October 29, 1969, when he stated that:

"One potential purchaser was located through the efforts of the realtor, and he was willing to offer what we felt was a premium price for the motel because of the availability of existing financing, however, he was never able to present an offer acceptable to the Mustoes."

Mrs. Marshall stated:

"\*\*\*in fact no offer was ever presented to the Mustoes for consideration, and both the broker and SBA refused to give them any information concerning it."

Mr. Cliff W. Brower, the attorney for the Mustoes, in a letter dated April 19, 1969, to Mr. Peter A. Plumridge, SDA Regional Counsel, stated that the realtor had advised Mr. Mustoe that he had not accepted the offer of \$41,000 for the motel in view of Mr. Mustoe's earlier statement that \$57,000 would be needed to pay all of Mr. Mustoe's debts. Mr. Mustoe, on December 11, 1969, also informed us that he had advised the realtor that the offer of \$41,000 was not enough because he had much more than that amount invested in the motel.

Mrs. Marshall further stated:

"\*\*\*It comes from the Dean Vincent documents of April 15 and 16, 1969 that the reason for withholding information was that the Scupiens and the brokers were the only ones who would benefit, and Mustoes were only being asked to release their interest."

From our review of this transaction, we cannot conclude that the Scupiens would "benefit" as contended by Mrs. Marshall since they would have received about \$18,700 for their \$21,000 interest in the motel. (See p. 5.) Also, although it may be termed a benefit, a brokerage commission for such a sale would be customary. In any event, since both the Mustoes and the Scupiens had an interest in the property, it could not have been sold without the approval of both parties.

Mrs. Marshall stated:

"Mr. Irons flatly stated that Mustoes' default would be the best thing that could happen to Scupiens."

This statement refers to the letter dated April 16, 1969, from Mr. Claude Irons, a representative of the realty firm of Dean Vincent, Inc., transmitting to the Scupiens' attorney the earnest money agreement setting forth the offer of about \$41,000 for the motel. The potential purchaser was interested in converting the motel into apartment units. In the concluding paragraph to that letter, Mr. Irons stated:

"I feel this is a good arrangement for all concerned. There is no money changing hands today, the loan has been committed for the construction and the Scupien's worries will be over under this arrangement. In fact, the best thing that could happen to them would be to have the purchaser go into default because they would be a lot better off with 11 apartments then (sic) they would with 10 empty motel rooms."

We view Mr. Irons' statement as referring to the potential purchaser's default since it was the purchaser, not the Mustoes, who was planning to convert the motel into apartment units.

Mrs. Marshall stated:

"One also wonders why SBA did not invite any other brokers to try to obtain a sale."

Mr. O. Russell Stoddard, the SBA Liquidation and Disposal Officer, advised us that he had not considered the motel marketable and had not called in any realtors to help locate a buyer. We were advised that Mr. Irons, a friend and former associate of Mr. Stoddard, had asked Mr. Stoddard whether he knew of any property in the area that would be desirable for conversion into efficiency apartments. Mr. Stoddard informed us that he advised Mr. Irons about the Ross Motel. In our opinion, it would have been preferable to have invited several realtors to try to locate a buyer for the motel although there is no assurance that such action would have resulted in the sale of the motel.

Mrs. Marshall stated:

"The GAO report to you states (p. 2, par. 3) 'SBA officials considered the feasibility of purchasing the Scupiens' interest in the motel, but, on the basis of an SBA appraisal, they concluded that the motel was not an economically viable entity ...' The striking fact is that SBA officials reached this conclusion only 7 months after approval of the loan and only 4 months after the first payment on Mustone's 10-year note. If the January 1969 conclusion was correct, the loan should not have been made in the first place!"

We did not review in depth the SBA evaluation of the loan application because we considered such a review beyond the scope of your original request that we investigate charges of possible improper conduct by SBA in the administration of the foreclosure action. We agree, however, that the statement that the motel was not economically viable raises questions as to whether SBA should have approved the loan.

Mrs. Marshall stated:

"To proceed to hasty foreclosure of the SBA mortgage does not seem to me to be the way for SBA to 'place special emphasis on aid to small business concerns located in ... areas of high unemployment or ... owned by individuals with low income.' (Quoting from GAO report, bottom of p. 1).\*\*\*

"As an alternative to the action taken SBA might well have used 15 USC 636(c), which gives SBA authority to extend the maturity of or renew any loan for additional periods up to 10 years beyond the original period to aid in

orderly liquidation of the loan. The alternative considered and rejected would seem to have shown more promise, in the light of the Phoenix bank appraisal I sent you showing a valuation of the Ross Motel of \$52,500."

As stated in our February report to you, SBA's foreclosure actions were prompted by the institution of the foreclosure suit by the seller of the motel, the Scupiens, on their 1963 contract with the Mustoes. It does not appear that extending the maturity of the SBA loan would have alleviated the situation since the foreclosure suit was initiated by the Scupiens and would still have to be resolved. SBA concluded that there was insufficient equity in the property over and above the Scupiens' interest to justify SBA's purchase of the Scupiens' interest. This decision was based on SBA's appraisal in January 1969 which showed that the market value of the property was about \$30,000. The bank appraisal referred to by Mrs. Marshall was made in March 1966, almost 3 years prior to the SBA appraisal.

Mrs. Marshall stated:

"The GAO report is in error in stating (p. 3, par. 4) that 'Scupiens' attorney offered the Mustoes \$1,000 net of all obligations for their full interest in the motel.' The fact is Mr. Peter A. Plunridge, attorney for SPA, on April 24, 1969 wrote to Cliff Brower, Mustoes' attorney, that the \$1,000 would have to be applied on the SBA loan and would not go to Mustoes."

Mrs. Marshall's comments concerning the application of the \$1,000 are correct. Our further review of the SBA loan file showed that, after the \$1,000 offer had been declined by the Mustoes' attorney, Mr. Plunridge advised the attorney that the \$1,000 would have had to be applied to the SBA loan.

Mrs. Marshall stated:

"Another interesting fact that is glossed over by the investigators is that the sale price of the motel apparently available was \$41,436, while the contract and mortgage debt against it were around \$30,000. This still leaves a difference of over \$11,000, no part of which was offered to Mustoe but all of which was evidently to go to Scupiens and the broker."

Under the terms of the earnest money agreement, the purchaser would have assumed the SBA loan of \$11,863. The Scupiens would have received the balance of the sale price of \$41,436, or \$29,573, in monthly payments of \$350. The Scupiens would have had to pay a fee of \$4,000 to

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the realtor and the motel's outstanding obligations. The financial statements for the motel as of December 31, 1968, showed outstanding obligations of \$6,860, exclusive of the amounts due the Scupiens and SBA. Therefore, the Scupiens would have received about \$18,700 for their \$21,000 interest, as follows:

Sale price		\$41,426
Less amount of SBA loan to be assumed by purchaser		<u>11,863</u>
Amount due Scupiens on proposed sale		\$29,573
Less realtor's fee	\$4,000	
Less outstanding obligations as of December 31, 1968	<u>6,860</u>	<u>10,860</u>
Balance		\$18,713
Unpaid balance on 1963 purchase contract with the Mustoes		<u>21,000</u>
Deficit		<u>\$2,287</u>

As shown above, no balance was available which could have been offered to the Mustoes. In any event, the Scupiens chose not to accept the terms of the earnest money agreement and the sale was not accomplished.

SBA officials advised us that the sheriff's sale of the real property was held on May 18, 1970, that the Scupiens were the only bidders, and that the property was purchased for \$24,636. The personal property was not included in the sheriff's sale because of a conflict over lien rights to the property. We were further advised that, for consideration of \$600 paid by the Scupiens, SBA released its lien on all personal property and waived its right of redemption on the real property. Mr. Plumridge, SBA Regional Counsel, explained that the right of redemption was waived because, in the opinion of the SBA personnel, it was worthless--the market value of the motel was less than the \$24,636 paid by the Scupiens and the costs that would be incurred by SBA in exercising its right of redemption.

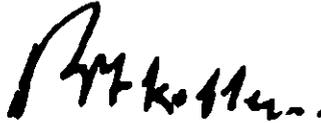
#### CONCLUSIONS

We continue to believe that the available evidence does not support a conclusion that there was any improper conduct by SBA representatives or that SBA's investigation of your constituent's complaint was biased. As discussed in our report of February 6, 1970, we believe that the Mustoes' misunderstanding might have been avoided if SBA representatives had fully explained the actions they were taking and why they were being taken.

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We trust that the above comments will serve the purposes of your request. Members of my staff will be available to discuss this matter with you further if you desire.

Sincerely yours,



Assistant Comptroller General  
of the United States

The Honorable John R. Dellenback  
House of Representatives