



OFFICE OF INSPECTOR GENERAL
EXPORT-IMPORT BANK
of the **UNITED STATES**

**STATEMENT OF OSVALDO LUIS GRATACÓS,
ACTING INSPECTOR GENERAL
BEFORE SUBCOMMITTEES
OF THE
U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON FINANCIAL SERVICES**

**SEPTEMBER 29, 2010
4:00 PM**

Statement of
Mr. Osvaldo Luis Gratacós
Acting Inspector General
Export-Import Bank of the United States
Before the
United States House of Representatives
Committee on Financial Services
Subcommittee on Oversight and Investigations
& Subcommittee on International Monetary Policy and Trade

September 29, 2010 at 4:00 p.m.

Good afternoon, Chairman Moore, Chairman Meeks, Ranking Member Biggert, Ranking Member Miller, and distinguished members of these honorable Subcommittees.

Thank you for the invitation and opportunity to testify before you about the activities of the Office of Inspector General (OIG) and the programs and operations of the Export-Import Bank (Ex-Im Bank). Before I continue, I would like to thank the Almighty for this opportunity, my family, and the members of the Ex-Im OIG staff, a group of career public servants who make the work possible and are committed to the OIG mission of preventing and detecting fraud, waste, and abuse.

I. Background

The Ex-Im Bank is the official export credit agency (“ECA”) of the United States. Ex-Im Bank supports the financing of U.S. goods and services in international markets, turning export opportunities into actual sales that help U.S. companies of all sizes to create and maintain jobs in the United States. Ex-Im Bank has programs to address short, medium, and long-term needs of exporters; assuming the credit and country risks that the private sector is unable or unwilling to accept. Ex-Im Bank also helps U.S. exporters remain competitive by countering the export financing provided by foreign governments on behalf of foreign companies. At the same time, Ex-Im Bank

must safeguard taxpayer resources by determining that there is a reasonable likelihood of repayment with respect to each of its transactions.

Ex-Im OIG was statutorily created in 2002¹ but the Inspector General (IG) did not officially take office until August 2007.² By the time the IG was sworn in, Ex-Im Bank had experienced two significant and high profile fraud cases, related to its Medium-Term (MT) loan program, totaling over \$200 million. The MT program provides insurance and guarantees (up to 85% of loan amount) to businesses, including small businesses, with repayment terms to up to five years (seven years in certain cases). Due to limited market capacity for this product, Ex-Im Bank aggressively marketed, utilized, and enhanced its MT program in hopes of increasing participation and expanding Ex-Im Bank's business. Improper implementation of due diligence and underwriting practices, inadequate monitoring tools, and lack of compliance functions contributed to losses attributable to the MT program.

Acting upon the above referenced exposure and recommendations from Ex-Im Bank's management, Ex-Im OIG focused its initial efforts on auditing the MT program and its information technology support, as well as investigating fraud-related matters referred to our office or uncovered by our staff. Our initial audits of the MT program's business processes and its IT support reported, in relevant part, the following findings:³

- Finding 1: Insufficient Credit Underwriting, Due-Diligence Requirements, and Processes
- Finding 2: Lack of Early Warning/Delinquency and Performance Reporting Capabilities
- Finding 3: Insufficient Lender Oversight and Quality Assurance Control Activities

¹ Export-Import Bank Reauthorization Act of 2002, P.L. 107-189, Sec 22 (June 14, 2002).

² I had the privilege of joining Ex-Im OIG in 2008, as the first person hired by then IG, Michael W. Tankersley, and worked closely with the IG in establishing the organization. Since October 2009, I have had the honor of serving the American people as the Ex-Im Bank Acting Inspector General.

³ Report can be found at http://www.exim.gov/oig/documents/MT_Program_Business_Process_Final_Audit_Report.pdf

- Finding 4: Insufficient Exposure Fee Pricing Structure for Non-Sovereign Transactions
- Finding 5: Consequences of 100% Guarantee for Non-Sovereign Transactions
- Finding 6: Processing Time Inefficiencies; Definition of a Complete Application
- Finding 7: Lack of Strategy and Vision for the MT Program
- Finding 8: Management, Oversight, and Accountability of IT Support for the MT Program Needs Strengthening⁴

I am glad to report that Ex-Im Bank has addressed some of the findings and recommendations listed and referenced above. Ex-Im Bank continues to make progress towards completion of some of the open recommendations made by this office and listed in Appendix B herein and our follow-up report issued this year.⁵

Furthermore, since reaching current staffing levels in April 2009, the OIG has had remarkable success as will be shown by the Semiannual Report to Congress to be issued next month. Specifically, the OIG has issued fifteen (15) audit and special reports containing over fifty (50) recommendations and suggestions for improving Ex-Im Bank programs and operations, including the ones contained in MT program related audits. Our investigative efforts have resulted in a number of law enforcement actions, including: fifty-one (51) indictments and arrests relating to over \$45 million in claims paid by Ex-Im Bank; one conviction; over eighty (80) management referrals for actions; and over \$26 million in program savings due to policy cancelations arising of our investigative efforts. Moreover, the OIG is currently investigating forty-eight (48) open matters representing approximately \$327 million in claims paid by Ex-Im Bank (or around 13% of all Ex-Im Bank claims paid as of the end of FY 2009). All of this has been accomplished with a very modest annual budget of \$2.5 million (for FY 2009) and a staff of ten professionals.

⁴ See Appendix B for open and closed recommendations as reported in Audit report *Medium-Term Export Credit Program—Information Technology (IT) Systems, Support and Governance*, OIG-AR-09-05 (June 12, 2009). Follow up audit, OIG-EV-10-01 (June 30, 2010). Reports can be found at <http://www.exim.gov/oig/index.cfm>.

⁵ See Appendix A for open and closed recommendations as reported on *Follow-Up of Audit Recommendations Reported in Medium Term Export Credit Program—Credit & Fraud Risk Management Business Process Improvement*, OIG-EV-10-02 (July 7, 2010). Report can be found at http://www.exim.gov/oig/documents/Follow_Up_of_Audit_Recommendations_10_02.pdf

II. Ex-Im Bank and Small Business

In 2002, Congress mandated Ex-Im Bank to increase the financing made available to small businesses from 10% to 20%.⁶ The 20% requirement was maintained in the current Ex-Im Bank reauthorization.⁷ The General Accountability Office (GAO) reported that Ex-Im Bank met its small business mandate in 2006 and 2007.⁸ In FY 2009, Ex-Im Bank reported 2,540 small business transactions exceeding its 20% mandate totaling \$4.4 billion (or 21% of all authorizations).⁹

In 2008, GAO took a further look at Ex-Im Bank's effectiveness in measuring compliance with small business Congressional mandates.¹⁰ GAO found that Ex-Im Bank had generally addressed most, but not all, of the legislative functions stated in the 2006 Reauthorization Act by developing 28 performance standards "ranging from providing excellent customer service to increasing outreach to small business".¹¹ Of particular interest was the lack of performance standards to address rural recruitment, outreach efforts to reach small businesses employing fewer than 100 employees, and promoting small business exports in cooperation with Small Business Administration.¹² Moreover, GAO stated that even though Ex-Im Bank has developed some performance standards in furtherance of its assistance to small businesses, 27 in total, almost half of them *lacked measurable targets and time frames*¹³ (emphasis added). Of particular interest was the lack of performance measures to "monitor progress" for financing socially and economically

⁶ Export-Import Bank Reauthorization Act of 2002, P.L. 107-189, Sec 7(a) (June 14, 2002).

⁷ Export-Import Bank Reauthorization Act of 2006, P.L. 109-438(December 20, 2006).

⁸ GAO-08-419T

⁹ Export-Import Bank 2009 Annual Report.

¹⁰ *Export-Import Bank Performance Standards for Small Assistance are in Place but Ex-Im is in the Early Stages of Measuring Their Effectiveness*, GAO-08-915 (July 2008)

¹¹ Id. at 3.

¹² Id.

¹³ Id.

disadvantaged businesses.¹⁴ The lack of targets to measure progress and the lack of time frames prevent Ex-Im Bank management from accurately monitoring progress in achieving its standards.

The OIG, through its statutory mission, is committed to supporting Ex-Im Bank's actions in meeting its mission of assisting in the financing of exports of U.S. goods and services in international markets, protecting and creating American jobs, and increasing the participation of small businesses in Ex-Im Bank programs. Ex-Im Bank plays a key role in financing the export of these goods and services. That role has increased in recent years. Today, the opportunity for increasing American exports is an important element to our nation's economic recovery. In FY 2009, Ex-Im Bank announced record authorization levels reaching \$21 billion and has reported authorization levels surpassing last year's levels for current FY 2010. Ex-Im Bank's role coupled with these growth levels present a valuable opportunity for the OIG to partner with Ex-Im Bank in support of its mission while exercising OIG's statutory independence.

OIG maintains a close monitoring and oversight perspective of Ex-Im Bank operational strategies, including small business strategies and goals. As Ex-Im Bank addresses the recommendations presented by GAO, Ex-Im Bank is also in the process of developing and implementing new strategies and processes geared to accomplish President Barack Obama's goal of doubling exports in the next five years.¹⁵ A significant component in achieving that goal is the focus on attracting more small businesses to participate in export programs. Of importance to this office are the export-credit programs offered by the Ex-Im Bank.

¹⁴ Id.

¹⁵ President Barack Obama launched this goal during the State of the Union address on January 26, 2010.

Currently, Ex-Im Bank is taking steps to attract more small business participation. Some of the more visible steps are:

- A). created a Small Business Committee (as required by Export-Import Bank Reauthorization Act of 2006);¹⁶
- B). established a Senior Vice-President for Small Business reporting to Ex-Im Bank President & Chairman;
- C). expanded short-term content eligibility provisions (covering U.S. content on transactions even if the U.S. content is less than 50% of transaction value);¹⁷
- D). Export Live events nationwide (educational conferences involving other federal agencies);
- E). introduced new products (re-insurance and supply-chain financing);
- F). increasing Delegation of Authority approval thresholds in order to expedite transactions;
- G). reorganization to create cell groups to increase approval cycle time for medium and short term applications;
- H). “express” application approval policies (for small business transactions under \$500,000);
- I). increase small business staffing under the Senior Vice-President for Small Business¹⁸;
- J). increasing regional offices’ staffing to recruit more businesses;¹⁸
- K). opening of additional regional offices¹⁸.

Ex-Im Bank has made significant progress in its effort to increase small business participation, although it is premature to audit the steps discussed above to determine their effectiveness. However, it is the OIG opinion that Ex-Im Bank has taken numerous steps in addressing some of the findings reported in the GAO audits, but has not fully developed all the performance standards, performance measures, and targeted time frames highlighted by GAO.¹⁹ Being able to accurately report and measure small business participation and exports would only enhance Ex-Im Bank’s ability to achieve the National Export Initiative’s goal.

¹⁶ Export-Import Bank Reauthorization Act of 2006, P.L. 109-438(December 20, 2006).

¹⁷ The policy was in effect since the late 1960’s.

¹⁸ Pending budget increase authority under FY 2011 OMB submission.

¹⁹ Ex-Im Bank still uses the 2009-2011 Small Business Plan audited by GAO. Ex-Im Bank is currently preparing the 2011-2013 Small Business Plan which will address some of the strategies arising out of the National Export Initiative.

III. Challenges

It is our opinion that Ex-Im Bank is facing a number of challenges in its efforts to increase small business participation as part of the Congressional mandate and the National Export Initiative. Some of these challenges are:

- *Inefficient and Ineffective Information Technology (IT) platform.* Ex-Im Bank currently uses a fragmented IT platform composed of several databases. These databases do not interface with each other, making data mining burdensome and time consuming. Ex-Im Bank would benefit from a comprehensive IT platform that interfaces with other Ex-Im Bank's systems.²⁰
- *Compliance and Oversight Procedures for Delegated Authority.* Ex-Im Bank is in the process of developing processes and procedures to address the monitoring of the delegated authority efforts. Compliance factors should be developed to effectively monitor uniform consistency of transaction approvals.
- *Enhancement of Due Diligence and Credit Underwriting Practices and Training Efforts to Address Surge in Application and Potential Decentralized Application Approval Process.* Given the lessons learned from the MT program, the surge in the number of transactions, and insufficient credit information and history from borrowers, it is vital that Ex-Im Bank enhances due diligence practices in order to identify fraudulent and incomplete transactions. With individual Delegated Authority as high as \$10 million, Ex-Im Bank needs to develop effective policies, procedures, and compliance practices to assess effectiveness of the delegations.
- *Limited Staff Resources.* In order to accomplish some of the actions stated herein, Ex-Im Bank is relying on the President's FY 2011 Budget request which provides Ex-Im Bank with a budget increase as part of the National Export Initiative.
- *Developing Performance Standards and Metrics.* In order to properly quantify the effect and success of the Small Business Strategy, Ex-Im Bank should develop these metrics, including those for socially and economically disadvantaged businesses, as recommended by GAO.
- *Properly Develop Simplified Application Processes, Training and Educational Materials for First-Time Exporters.* Conveying the export financing message in simpler terms may allow small businesses to consider exporting their goods for the first time. Also, it would encourage future participation.

²⁰ Ex-Im Online was launched with the purpose of reducing application approval time. Ex-Im Online is a "front-end" data gathering system.

-
- *Continued Collaboration and Cooperation with Other Agencies, including Small Business Administration and Department of Commerce in order to Reach Out to Small Businesses.* Enhancing export opportunities require the participation, training, and collaboration of other federal agencies. The National Export Initiative addresses and encourages collaboration between agencies.

IV. Conclusion

In only three years since its inception (and just over one year since reaching current staff levels), the OIG efforts are having a noticeable impact on Ex-Im Bank's operations. While Ex-Im Bank continues to provide export credit and financing as part of its export credit agency functions and the recently unveiled National Export Initiative, it faces foreseeable challenges in its quests of achieving the National Export Initiative's goal. I have highlighted some of the relevant work performed by the OIG, specifically as it relates to the MT program, in order to illustrate the importance of proper planning, implementation and oversight of strategies and products and to incorporate lessons learned from prior Ex-Im Bank's activities. The OIG will continue enhancing its independent oversight role by closely focusing on Ex-Im Bank operations in order to improve its efficiency, meet Congressional requirements, as well as strengthen its efforts in preventing and detecting fraud, waste, and abuse.

Chairman Moore, Chairman Meeks, Ranking Members Biggert and Miller and members of these honorable Subcommittees, thank you once again for the opportunity to testify before you today. I would be pleased to respond to any questions you may have. Thank you!

APPENDIX A

**Findings and Recommendations: Medium-Term Export Credit Program –
Credit and Fraud Risk Management and Business Process Improvement
(March 30, 2009, OIG-AR-09-04) &
Follow-Up Review (July 7, 2010, OIG-EV-10-02)**

The OIG determined that Ex-Im Bank adequately addressed and closed four of eight recommendations noted below.

Finding – Insufficient Credit Underwriting Due-Diligence Requirements and Processes	
Recommendation 1. <ul style="list-style-type: none"> ○ Require as part of credit underwriting due-diligence on-site inspections and appraisals of the equipment being exported as well as bank/brokerage statements of obligors and guarantors for MT transactions. ○ Develop a process to manage the quality of appraisers and appraisals received. 	Closed
Finding – Lack of Early Warning/Delinquency and Performance Reporting Capabilities	
Recommendation 2. <ul style="list-style-type: none"> ○ Institute a defined and standardized process for lenders to report payment history. ○ As enhancements are made to Ex-Im Bank’s technology infrastructure, significant priority should be given to the end-to-end build out of performance reporting capabilities. ○ Strong consideration should be given to hiring a quantitative analyst with experience in the design and implementation of pricing, risk management and credit analysis tools and models to lead that effort. ○ Payment frequency for MT transactions should be consistent with local country norms. 	Closed
Finding – Insufficient Lender Oversight and Quality Assurance Control Activities	
Recommendation 3A. <ul style="list-style-type: none"> ○ Institute a formal lender oversight function to actively manage and monitor performance of transactions on a lender-by-lender basis and to assess the quality of lender due-diligence performed on a periodic basis, quarterly at a minimum. ○ The lender oversight function should report into a division independent of front-office originations such as Credit Review and Compliance. 	Open
Recommendation 3B. <ul style="list-style-type: none"> ○ Establish a quality assurance function for the MT program responsible for managing and monitoring performance of transaction participants. ○ Manage the process of performing periodic MT export credit transaction file reviews on a sub-sample of transactions. 	Closed

Finding – Insufficient Exposure Fee Pricing Structure for Non-Sovereign Transactions	
Recommendation 4. <ul style="list-style-type: none"> ○ Revamp exposure fee pricing structure for non-sovereign MT program transactions to more effectively account for transaction-level risk. ○ Consider establishing minimum, base exposure fees for non-sovereign MT transactions that are at a premium to the OECD floor pricing that the Bank utilizes for its exposure fee pricing of sovereign transactions. 	Open
Finding – Consequences of 100% Guarantee for Non-Sovereign Transactions	
Recommendation 5. <ul style="list-style-type: none"> ○ Evaluate the impact of implementing a greater degree of risk sharing or other incentives for non-sovereign transactions to reduce the moral hazard currently associated with the MT program. 	Closed
Finding – Processing Time Inefficiencies: Definition of a Complete Application	
Recommendation 6. <ul style="list-style-type: none"> ○ Develop a definition of a complete application by defining documentation requirements at initial application. ○ Consider creating dedicated teams in Trade Finance Insurance and Credit Underwriting that would be responsible for processing transactions from first-time lenders as well as those transactions considered highly complex or risky. 	Open
Finding – Lack of Strategy and Vision for the Medium Term Program	
Recommendation 7. <ul style="list-style-type: none"> ○ Develop and document a strategic plan for the MT program (even if one is not documented for Ex-Im Bank as a whole) identifying the major goals of the MT program over the next 3 to 5 years and the strategies that management will deploy to achieve the goals, including the use of technology and targets for key performance measures. 	Open

Appendix B

Results of Follow-Up Testing of Audit Recommendations Reported in Medium-Term Export Credit Program – Information Technology (IT) Systems, Support and Governance (June 12, 2009, OIG-AR-09-05)

We determined that Ex-Im adequately addressed and closed four of five recommendations noted below.

Finding – Management, Oversight and Accountability of IT Support for the MT Program Needs Strengthening	
Recommendation 1A. <ul style="list-style-type: none"> ○ Develop an IT Strategic Plan that is aligned with the MT Program business plan and covers the same time period. 	Open
Recommendation 1B. <ul style="list-style-type: none"> ○ Designate a senior manager with responsibility and accountability for the management of the IT systems support for the MT Program throughout its life cycle. ○ Direct the designated senior manager to take a leadership role in the ongoing development of detailed business requirements in response to strategic objectives identified for IT support of the MT Program and requests for enhancements from system users and in the communication of those business requirements to the Office of the Chief Information Officer (OCIO). ○ Direct the designated senior manager to obtain a plan of action and milestone schedule from the OCIO that addresses all outstanding Change Requests/defects, which should include all system capabilities required to meet management’s objectives for the MT Program, and to take prompt action to ensure the OCIO has timely and appropriately prioritized and developed a well documented plan to address each Change Request/defect. 	Closed
Finding – IT Systems that Support the MT Program Need Improvement	
Recommendation 2A. <ul style="list-style-type: none"> ○ Define and document the key transactional data fields that must be stored across all Ex-Im Bank programs and the structures and relationships between them. This data model would address the problems related to multiple participant files and other common reference data. The data model would also highlight information needs that are not currently met by existing databases or applications. ○ Develop, document and implement a plan to enhance the functional capabilities and interoperability of Ex-Im On-Line (EOL) and the other systems supporting MT Program transactions, with a focus on design and implementation of embedded system controls, such as: <ul style="list-style-type: none"> ▪ automation of MT lender rating and credit scoring models; ▪ automated system alerts that warn of transaction participants with prior claims history as well as denied, withdrawn or fraudulent transactions across all Ex-Im Bank lending programs; and ○ automated monitoring of all MT Program transactions regardless of size. 	Closed

Recommendation 2B. <ul style="list-style-type: none">○ Develop data repositories that consolidate and organize the key transactional data fields.	Closed
Finding – Systems Development Process Needs Improvement	
Recommendation 3: Implement: <ul style="list-style-type: none">○ A user-friendly process for submitting and accepting new end user business requirements as it relates to requests for system enhancements. This process should also facilitate improved communication between the OCIO resources and end users to ensure that business requirements are accurately designed and that justification is provided for denied requests.○ A more robust testing program that a) includes the development of a comprehensive suite of test cases and test scripts that can be automatically rerun multiple times and b) requires formal involvement of MT users in the development of the test cases, the execution of the tests and the sign-off of test results.○ A more formal and comprehensive training program for EOL system users. The training should focus not only on the mechanics of the system but also on the policies and processes that the system is supporting. Details on the training program should be made available on Ex-Im Bank’s website	Closed



**Office of Inspector General
Export-Import Bank of the United States
811 Vermont Avenue, NW
Washington, DC 20571
202-565-3908
www.exim.gov/oig**