Office of the Special Inspector General for Pandemic Recovery

March 8, 2023

TO: JACOB D. LEIBENLUFT
CHIEF RECOVERY OFFICER
U.S. DEPARTMENT OF THE TREASURY

FROM: THEODORE R. STEHNEY
ASSISTANT INSPECTOR GENERAL FOR AUDITING
SPECIAL INSPECTOR GENERAL FOR PANDEMIC RECOVERY (SIGPR)

SUBJECT: Roll-up of the Independent Review of 4003(b) Loan Recipients' Validation Memos
Audit Memorandum Number SIGPR-A-22-003-17

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) became law on March 27, 2020. Section 4003 of the CARES Act authorized the U.S. Department of Treasury (Treasury) to make loans, loan guarantees, and other investments to provide liquidity to eligible businesses related to losses incurred as a result of the coronavirus pandemic. Sections 4003(b)(1)-(3) appropriated $46 billion to help stabilize the airline industry and businesses critical to maintaining national security. The breakdown of available funding was as follows:

1. Up to $25 billion for passenger air carriers; businesses certified to perform inspection, repair, replace, or overhaul services; and ticket agents;
2. Up to $4 billion for cargo air carriers; and
3. Up to $17 billion for businesses critical to maintaining national security.

Treasury created two programs to facilitate the issuance of these loans – the Air Carrier Loan Program (ALP) and the National Security Loan Program (NSLP). Both programs followed Treasury's guidance as issued in the Underwriting Guide L1 Review Chapter and Underwriting Guide L2 Review Chapter. The L1 guidance covered the initial intake of applicant information through to the recommendation of sending applicants to the underwriting, credit analysis and approval process, which is covered in the L2 Underwriting Guide. The recommendation to send an applicant forward in the process is documented by Treasury in a Validation Memo.

During the initial loan application process, applicants were required to submit documents through a Treasury web portal. For each applicant to move forward in the loan process, applicants had to provide certain documentation, such as financial statements, an Internal Revenue Service (IRS) form 941, a financial plan, etc. Treasury

also performed internal queries to ensure the applicant wasn't debarred or suspended from conducting business with the federal government and had no government liens or bankruptcies, among others checks. This information was compiled in the Validation Memo.

Treasury made 35 loans totaling $21.9, with actual disbursements of $2.68 billion.* The loans are broken down as follows:

Type	No. of Loans	Authorized Loan Amounts	Loan Disbursements
Air Carriers	15	$ 21,113,399,648	$ 1,900,399,648
Cargo Air Carriers	2	2,111,656	2,111,656
Ticket Agents	2	20,549,651	20,549,651
Repair Stations	5	18,988,205	18,988,205
National Security	11	735,934,400	735,934,400
Totals	35	21,890,983,560	2,677,983,560

* Disbursements are less than the Authorized Loan Amounts because not all borrowers took the full amount authorized.

As part of our oversight of Section 4003, SIGPR performed 16 independent attestation reviews of 4003(b) loan recipients' Validation Memos. Our objective was to evaluate whether Treasury's Validation Memo for direct loan recipients was completed according to Treasury's L1 Underwriting Guide and other applicable criteria, and fairly presented the supporting documentation provided by each loan recipient in all material respects. Treasury's efforts culminated in the completion of a Validation Memo for 34 of 35 borrowers. We also performed a limited analysis of the remaining 18 loan recipients' Validation Memos.[1]

We selected our judgmental sample of 16 Validation Memos by first looking at the largest borrowers. We then selected companies from various segments of the program, e.g., ticket agents, businesses critical to national security, etc. Our sample consisted of authorized loan amounts totaling $21.1 billion with actual loan disbursements of $1.9 billion. After the initial 16 companies were reviewed, we then performed a limited analysis of the remaining borrowers that did not result in the issuance of a separate report. The results of our limited analysis of the remaining borrowers are also included in this memorandum.

[1] We did not perform a review of Yellow Corporation as a Validation Memo was not completed. We are assessing Yellow's loan approval process under separate cover.

Results of Independent Attestation Reviews

We identified minor discrepancies in 10 of the 16 Validation Memos reviewed and a material deficiency for one Validation Memo.[2] The following chart below summarizes the results:

Borrower	Material Deficiencies Identified
Ovation Travel Group	1. The entire Ticket Agent Section of the Validation Memo was incomplete. 2. There was a discrepancy in the number of employees on the application and the IRS-941 form. 3. There were other portions of the Validation Memo that were left blank.

Borrower	Minor Discrepancies Identified
Alaska Airlines	1. The Validation Memo indicates that the applicant is publicly traded. It is not. 2. The Validation Memo indicates that the borrower was not a Payroll Support Program (PSP) applicant. Borrower received Payroll Support Payments. 3. The Salesforce Application had incomplete fields.
Hawaiian Airlines	1. The Validation Memo indicates that the borrower was not a PSP applicant. It was. 2. The Validation Memo indicates that no other CARES Act funding was received. Borrower received Payroll Support Payments.
Mesa Airlines	1. The Validation Memo indicates that the borrower was not a PSP applicant. It was. 2. There was no supervisory review of the Validation Memo.
American Airlines	1. The Validation Memo indicates that the borrower was not a PSP applicant. It was.
United Airlines	1. The Validation Memo indicates that the borrower was not a PSP applicant. It was.
SkyWest Airlines	1. The Validation Memo indicates that the borrower was not a PSP applicant. It was.
Caribbean Sun Airlines	1. The Validation Memo indicates that the borrower was not a PSP applicant. It was.
SpinLaunch	1. Loan amount indicates borrower was allocated $20 million, however was only allocated $2.5 million. 2. The Validation Memo indicates the borrower received $1.05 million in Payroll Protection Program (PPP); however, the PPP was cancelled, and the amount was $0.
Meridian Rapid Defense Group	1. The Validation Memo did not have a Lead Reviewer signature.
TIMCO Engine Center	1. The Validation Memo did not have a supervisory review.

[2] The 16 independent reports are posted on our website and can be accessed at www.sigpr.gov/reports.

Material Deficiencies

We identified material deficiencies with Ovation Travel Group (Ovation), and the loan application should not have advanced to the next step in the loan process. Ovation was the only ticket agent reviewed.

Ovation's Validation Memo included a separate section with distinct questions for ticket agents. However, this section of Ovation's Validation Memo was left blank. While it is not known if the responses to the questions would have prevented Ovation from being approved or eligible for a loan, this section should have been completed prior to advancing Ovations application to underwriting.

There was also an unexplained discrepancy in the number of employees on Ovation's application and its submitted IRS form 941. This is relevant because the CARES Act required borrowers to retain, within 10 percent, the number of employees between March 24,2020 and September 30, 2020. Without a confirmed number of employees in the documents provided, this requirement of the CARES Act could not be verified.

Ovation, like several other borrowers, lacked documented evidence of a supervisory review. Had the supervisor reviewed the completed Validation Memo, these deficiencies may have been detected and corrected.

Minor Discrepancies

We identified 10 of 16 Validation Memos with minor discrepancies. However, the fact that many of these same minor discrepancies were repeatedly found in multiple Validation Memos points to a systemic issue with Treasury's review process as it relates to following its L1 Underwriting Guide procedures.

The most common discrepancy was that the Validation Memos stated that the borrower did not receive or apply for, or expect to apply for, loans provided or guaranteed pursuant to other programs under the CARES Act. We noted this for eight Validation Memos, where the borrower did either apply for or receive Payroll Support Payments PSP. While PSP is not a loan program, Treasury explained that PSP was considered "other assistance". Treasury further goes on to say that the reviewer relied on the applicant's self-reporting and certification.

Other issues we identified were:

- Four Validation Memos lacked a Supervisory or Lead Reviewer review and signature;
- Two instances where there were blanks on the Validation Memo or application;
- A Validation Memo had an incorrect amount for the allocated loan amount and indicated that the borrower received a PPP loan when it did not; and
- A Validation Memo that indicates the company is publicly traded when it is a private company.

Results of Our Limited Analysis

We performed a limited analysis of the remaining 18 borrowers, primarily looking for discrepancies that we found with the original 16 borrowers we reviewed. We identified four borrowers that appeared to have minor discrepancies; however, Treasury was able to explain or provide documents resolving the discrepancies for two of those borrowers. The remaining two borrowers showed that there was no supervisory review or signature.

Conclusion

Our reviews showed that 11 of 16, or nearly 69 percent, of the Validation Memos we reviewed had either major or minor discrepancies. Including the results of our limited analysis, we identified that 38 percent of all Validation Memos had discrepancies. The high instance of discrepancies identified points to a systemic issue with the initial step in the lending process.

While no formal recommendations are being proposed,[3] we strongly suggest that the systemic issues identified in this memorandum be addressed and corrected before Treasury uses the L1 Underwriting Guide in the future. Treasury's Validation Memo was the end result of the first step of the loan approval process, where Treasury performed its due diligence to determine if applicants warranted being moved to the next phase of the loan approval process; an integral part in the overall loan approval process. Attention to detail and understanding and following policies and procedures could aid in eliminating the types of discrepancies identified in our reviews in future initiatives.

We do not require a written response to this memorandum, however, if you wish to respond, we will incorporate the entire response as an addendum to this memorandum.

If you have any questions regarding this memorandum, please contact me or any member of the audit team at the following:

Michael Sinclair	Audit Manager	Michael.Sinclair@sigpr.gov	(202) 923-8021
Reynaldo Gonzales	Auditor-in-Charge	Reynaldo.Gonzales@sigpr.gov	(202) 941-6828

I would like to thank you and your staff for your assistance during the attestation reviews.

[3] Attestation review engagements only provide limited assurance, and as a result, auditors do not perform sufficient work to be able to develop elements of a finding or provide recommendations.

APPENDIX A – AUDIT MEMORANDUM DISTRIBUTION

Chief Recovery Officer – U.S. Department of the Treasury

Office of General Counsel – U.S. Department of the Treasury

Inspector General – Special Inspector General for Pandemic Recovery

Asst. Inspector General for Auditing – Special Inspector General for Pandemic Recovery

Office of General Counsel – Special Inspector General for Pandemic Recovery

APPENDIX B – BORROWER RESPONSE IN ACCORDANCE WITH PUBLIC LAW 117-263

April 4, 2023

Via email: michael.sinclair@sigpr.gov

Mr. Michael Sinclair
U.S. Department of the Treasury
Special Inspector General for Pandemic Recovery
Office of Audits
2051 Jamieson Ave., Suite 600
Alexandria, VA 22314

Ref. (*i*) Letter of March 9, 2023, from Assistant Inspector General T.R. Stehney, SIGPR, to Alaska Airlines;

(*ii*) Letter of March 8, 2023, from Assistant Inspector General T.R. Stehney, SIGPR, to J.D. Leibenluft, Chief Recovery Officer, U.S. Department of the Treasury

Dear Mr. Sinclair,

Thank you for forwarding Assistant Inspector General Stehney's two letters, referenced above. We read both, and are appreciative of the opportunity to respond, which we now do.

From our understanding of the March 8th letter to the Chief Recovery Officer, the minor discrepancy which references Alaska Airlines appeared in a validation memo written by the U.S. Dep't. of the Treasury. We reviewed our submissions to U.S. Treasury, and do not have a sense of where the discrepancies may have originated.

To the three issues noted in I.G. Stehney's March 8th letter:

1. "The Validation Memo indicates that [Alaska Airlines] is publicly traded. It is not."

   Alaska Airlines, Inc., is indeed not publicly traded. It is a wholly-owned subsidiary of Alaska Air Group, Inc., a Delaware corporation that is publicly traded (NYSE ticker symbol ALK).

2. "The Validation Memo indicates that [Alaska Airlines] was not a Payroll Support Program (PSP) applicant. [Alaska Airlines] received Payroll Support Payments."

   Alaska Airlines did in fact submit an application to the PSP Program, and received payroll support payments.

3. "The Salesforce Application had incomplete fields."

   Alaska Airlines did not have any affiliation with Salesforce with regard to CARES Act relief.

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We hope this confirmation is of use. Should there be any other questions, please feel free to contact my colleagues copied below.

Sincerely,

ALASKA AIRLINES, INC.

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