Office of Inspector General
U.S. Small Business Administration

June 2011 Update

Business Loan Programs

Alabama Man Convicted on False Statements
On June 9, 2011, an Alabama man was sentenced in the U.S. District Court for the Northern District of Alabama to 2 weekends in jail, 12 months home detention, 5 years probation, and 100 hours of community service. He was also ordered to pay restitution of $120,486.66 and a special assessment fee of $100. The subject, who was the owner of a gas station in Cullman, Alabama, had pled guilty to one count of making false statements after selling his business to another person utilizing an SBA loan of $76,000. The investigation disclosed that the seller presented false tax information to the SBA and the purchaser to artificially inflate the annual sales revenues of the gas station.

Kansas Construction Company and Others Indicted
On June 15, 2011, in the District of Kansas, a construction company and four individuals were indicted for their alleged participation in a scheme to falsely obtain contracts through the SBA's Service-Disabled Veteran-Owned Small Business (SDVOSB) set aside program. The indictment charges each defendant with multiple counts relating to conspiracy, major program fraud, wire fraud, money laundering, and making false statements. The indictment alleges that the individuals engaged in a series of acts in order to misrepresent the relationship between the construction company and a second firm and to falsely represent the construction company to be a certified SDVOSB. This is a joint investigation with the Defense Criminal Investigative Service (DCIS), the General Services Administration OIG, and the Department of Veterans Affairs OIG.

Maryland Restaurant Owner Convicted
On June 17, 2011, in the U.S. District Court for the District of Maryland, the president and owner of a Korean restaurant in Lusby, Maryland, was sentenced to 30 months in prison, 3 years supervised release, restitution of $150,000, and a $100 special assessment fee. The subject was previously found guilty in a jury trial of one count of conspiracy, one count of making false statements and aiding and abetting. The owner had obtained an SBA-guaranteed loan in the amount of $417,000 through a finance company to perform construction and renovation work for leased space and to purchase equipment and inventory for his new restaurant business. On his loan application, the subject certified the cost of the construction work to be $295,000 even though he had already entered into an agreement with a construction company for the work to be performed for $145,000. The subject conspired with the construction company to falsely represent the total cost of the project as $295,000 in order to receive additional funds for his personal use.

Material Deficiencies Identified in Four 7(a) Recovery Act Loans Resulted in $3.2 Million of Questioned Costs
On June 29, 2011, the OIG issued a report on the results of a review of purchased 7(a) Recovery Act loans. The objective of the audit was to determine whether purchased 7(a) Recovery Act loans were originated, closed, and purchased in accordance with SBA's rules and regulations, and commercially prudent lending standards. The four loans were part of a judgmental sample of Recovery Act loans, approved for $500,000 or more, that had been purchased as of September 30, 2010. The audit found that the lenders did not originate and close the four 7(a) Recovery Act loans in accordance with established guidelines. Further, SBA loan officers did not identify deficiencies in three of the loans during their purchase reviews. The OIG recommended that the SBA seek recovery of approximately $3.2 million.

Disaster Loans

Louisiana Couple Pleads Guilty
On June 9, 2011, a husband and wife pled guilty in the Western District of Louisiana to one count of conspiracy to commit wire fraud. The charges involve an SBA loan of $126,300 that another couple received in order to rebuild and repair their residence, which had been damaged by Hurricane Ike. The couple gave power of

attorney to a financial group, owned by the wife, for the purpose of negotiating and finalizing their SBA loan. The husband was the manager of the company responsible for the repairs to the borrowers' residence. A review of invoices, cancelled checks, and paid receipts submitted to the SBA by the wife in support of loan disbursement determined that the items listed on the invoices had never been purchased and the cancelled checks were fraudulent.

Mississippi Man Pleads to Theft of Public Funds

On June 14, 2011, a Mississippi man pled guilty in U.S. District Court, Southern District of Mississippi to one count of theft of public funds. The investigation disclosed that on his SBA loan application he misrepresented the location of his primary residence, which he claimed had been damaged by Hurricane Katrina. He was approved for a $144,900 SBA disaster home loan, of which $121,300 was disbursed. As a result of this investigation, the subject repaid the remaining balance of his SBA loan. The subject had also made the same claims when completing applications for Federal Emergency Management Agency (FEMA) and Mississippi Development Authority grant benefits. This is a joint investigation with the U.S. Housing and Urban Development (HUD) OIG, U.S. Department of Homeland Security (DHS) OIG, and the Mississippi State Auditor's Office.

Woman Sentenced for False Statements

On June 15, 2011, a Louisiana woman was sentenced in U.S. District Court for the Middle District of Louisiana to 36 months probation, immediate restitution to the SBA of $46,300, and a $100 special assessment fee. She previously pled guilty to one count of false statements. Following Hurricane Katrina, the subject applied for and received an SBA loan to rebuild her home in Baton Rouge, Louisiana. She also applied for and received emergency assistance from FEMA and the Louisiana Road Home Program. The investigation revealed that the woman created fraudulent receipts and documents that reflected repair expenses she had supposedly sustained as a result of the storm, but which she had not actually incurred. Based on the fraudulent documents, the SBA increased her loan from $85,400 to $108,000. This was a joint investigation with the HUD OIG, DHS OIG, and the U.S. Postal Service OIG.

Louisiana Woman Forfeits Home at Sentencing

On June 16, 2011, a Louisiana woman appeared in U.S. District Court for the Eastern District of Louisiana and was sentenced to 60 months probation, restitution of $351,098.69, and a $300 special assessment fee. The court also ordered the immediate forfeiture of a single-family residence owned by the subject. The sentencing was a result of her guilty plea to three counts of theft of government funds. The investigation disclosed that she provided false statements on her applications for disaster assistance related to damage to her primary residence from Hurricane Katrina. Although she owned the property that she claimed as her primary residence, the house was considered unlivable prior to the storm. As a result of her representations, she received $219,000 in disaster loan funds from the SBA, a $150,000 grant from the HUD Road Home Program, and approximately $26,676 from FEMA. This was a joint investigation with HUD OIG, DHS OIG, and the Federal Bureau of Investigation (FBI).

Louisiana Man Charged with Theft of Funds

On June 21, 2011, a Louisiana man was charged in a criminal information with one count of theft of government funds in U.S. District Court for the Eastern District of Louisiana. The information alleges he submitted fraudulent documents to the SBA for repairs to his rental properties damaged by Hurricane Katrina. As a result of his misrepresentations, he received multiple loan disbursements totaling $103,100 from the SBA. This is a joint investigation with the HUD OIG.

Texas Property Manager Indicted

On June 29, 2011, in the Southern District of Texas, a property manager was indicted on one count of conspiracy and two counts of fraud in connection with a major disaster. The charges relate to the property manager's claim that Hurricane Ike damaged a rental property, which the investigation alleges had been damaged by an intentional fire prior to Hurricane Ike. The owner of the property and the owner's brother were previously indicted for their alleged participation in a false invoice scheme. The owner of the property, a real estate broker and Houston area bank director, was approved for $999,700 in home and business disaster loans. The business loan was approved to repair or replace more than 40 rental properties allegedly damaged by Hurricane Ike. The investigation alleges that the owner submitted to the SBA inflated and false invoices for repairs to his residence and rental properties. The second brother's charges relate to his verifying to the SBA $680,000 in fictitious repairs that he claimed were completed by his company. This case was referred to the OIG by the SBA Processing and Disbursement Center, Fort Worth, TX and is a joint investigation with the DHS OIG.

Release of Collateral by the Disaster Loan Servicing Centers

On June 3, 2011, the OIG issued a report on the results of a review of the release of collateral by SBA Disaster Loan Servicing Centers in Birmingham, Alabama and El

Paso, Texas. The objective of the audit was to determine whether the servicing centers were appropriately and timely releasing collateral on disaster loans.

An OIG review of a statistical sample of 120 collateral release decisions made on active loans showed that the servicing centers did not consistently make appropriate decisions to release collateral on these loans. The review found that 55, or approximately 46 percent, of the collateral release decisions, for collective property values of at least $3.1 million, were inappropriate. As a result, the remaining collateral for some loans was not sufficient to protect the Agency's interests because the loan balance exceeded the value of the property. The inappropriate collateral release decisions occurred because the Agency did not perform a full collateral analysis. A full analysis would have included obtaining an appraisal or other acceptable property valuation, and evaluating whether the retained collateral value was sufficient in relation to the outstanding loan balance. As a result of these inappropriate collateral releases, the OIG projects that at least $3.9 million of loan balances could be insufficiently protected, exposing the Agency to a higher risk of loss.

To assess the timeliness of collateral releases, the OIG reviewed a statistical sample of paid-in-full loans. The OIG found that collateral releases for paid-in-full loans was not always timely; however, the impact to the Agency was not significant.

The audit also disclosed five other matters which merit attention. For some collateral releases, the SBA did not receive the net proceeds from the sale of damaged properties, proceeds from these sales were not always applied to the correct loan, some damaged properties were sold for less than fair market value, justifications for some collateral releases were misleading, and insurance coverage on the remaining collateral was not always verified as required.

The OIG made six recommendations to improve the collateral release process. During the audit, the servicing centers began implementing procedures to correct some of the deficiencies identified.

Government Contracting & Business Development

Florida Men Indicted on $100 Million Contract Scheme
On June 21, 2011, two men were indicted in U.S. District Court for the Middle District of Florida on one count of conspiracy and five counts of wire fraud. The indictment also contains forfeiture allegations that notified the defendants that the United States intends to seek a $100 million monetary judgment and to call for forfeiture, as proceeds of the alleged fraud, a number of assets including $8.1 million previously seized from bank accounts and real property. The indictment alleges that the subjects devised a scheme whereby they created a company for the purpose of obtaining a $100 million small business set-aside contract with the Department of Defense (DoD). The subjects used a nominee owner to create the appearance that their company was not affiliated with a consultant firm that they controlled. Their firm had been the incumbent contractor on a previous DoD contract. The subjects allegedly submitted false and misleading information concerning the relationship between the two companies after the affiliation was challenged in the course of a size protest submitted to the SBA Office of Government Contracting. This is a joint investigation with the DCIS.

Former Army Contracting Officials Indicted in Texas
On June 22, 2011, two former high-level contracting officials with the U.S. Army were indicted in San Antonio, Texas. The seven-count indictment charges the husband and wife with one count of conspiracy to defraud the U.S. and four counts of filing false tax returns and aiding and abetting. The wife is also charged with two additional counts of making false statements. These allegations relate to the couple's acceptance and concealment of payments totaling over $100,000, from an SBA 8(a) participant firm based in Chicago, Illinois, to which they awarded multiple construction contracts in their official capacities. The 8(a) firm was not revealed in this indictment, but according to the indictment, the couple conspired to evade administrative and criminal inquiry by directing the 8(a) firm to convey its payments through complex financial transactions involving their relatives and structured cash deposits below $10,000 into joint accounts held with relatives. These surreptitious transactions were specifically designed to conceal the true source and purpose of the funds and to circumvent the reporting requirements of financial institutions. The conspiracy scheme also included concealing the income from the Internal Revenue Service (IRS) on the couple's tax returns from 2002 to 2008, and from the Army's ethics officials on the wife's annual Confidential Financial Disclosure Reports (OGE Forms 450). This is a joint investigation with the Army Criminal Investigation Division (Army CID), the IRS Criminal Investigation Division (CID), the FBI, DCIS, and the Department of Justice Antirust and Tax Divisions.

Virginia 8(a) Owner Indicted on Conspiracy, Bribery, and Extortion Charges
On June 23, 2011, the owner of a system and information services corporation was indicted in the Eastern District of Virginia on one count of conspiracy, one count of

bribery, one count of procurement of citizenship or naturalization unlawfully, one count of fraud and misuse of Visas, permits, and other documents, one count of false statements, one count of extortion by blackmail, and three counts of aiding and abetting. The owner's company is an 8(a) certified firm and has received over $3 million in contracts set aside for 8(a) certified businesses. The indictment alleges that the owner obtained falsified U.S. citizenship documents from a DHS employee and used the documents as a basis for his claim that he was a U.S. citizen to obtain a Department of Defense security clearance. The subject also used the falsified U.S. citizenship documents as a basis for his claim that he was a U.S. citizen on his firm's 8(a) application. This is a joint investigation with the DHS OIG, Immigration and Customs Enforcement – Homeland Security Investigations, Department of State - Diplomatic Security Service, and the Department of Labor OIG.

Agency Management

SBA's Funding of Information Technology Contracts Awarded to Isika Technologies, Inc

On June 2, 2011, the OIG issued a report on the results from an audit of the SBA's procurement of information technology (IT) hardware and software through ISIKA Technologies, Inc. (iTechnologies). This was the second in a series of reports related to this ongoing audit.

The OIG found that SBA did not properly fund an Indefinite Delivery/Indefinite Quantity (IDIQ) contract because it obligated $3.151 million during FY 2009 and FY 2010 by issuing contract modifications without identifying specific requirements for IT hardware and software. Because SBA did not use these obligated annual funds to purchase IT hardware or software during FY 2009 and FY 2010, the agency inappropriately obligated annual funds that otherwise would not have been available for use in a subsequent fiscal year. According to SBA personnel, this occurred because contracting officers did not review contract modification details prior to issuance and cited fiscal year-end constraints as the rationale for not performing a review. As a result, the SBA: 1) violated the bona fide needs rule relating to its FY 2009 and FY 2010 annual appropriations; 2) risked violating the Anti-Deficiency Act (ADA) by obligating expired FY 2010 annual funds during FY 2011 with no assurance that the agency had funds available to cover these inappropriate expenditures; and 3) reported the inappropriate obligation of funds to the Federal Procurement Data System-Next Generation (FPDS-NG), which resulted in an overstatement of obligations to Small Disadvantaged Businesses (SDBs) in the FY 2009 Small Business Goaling Report, which could also result in incorrect SDB reporting in the FY 2010 Small Business Goaling Report.

The OIG recommended that the SBA establish procedures to discontinue the practice of inappropriately obligating funds on contracts in anticipation of future needs, de-obligate inappropriately obligated funds, and develop and provide training to agency personnel on the bona fide needs rule. We also recommended that the SBA determine whether it violated the ADA and take appropriate action if a violation exists, review all ongoing SBA IDIQ contracts to ensure that task orders are being issued in accordance with government regulations, and based on the IDIQ contracts review results, determine whether administrative actions are warranted against the contracting officers. Finally, we recommended that the SBA revise FPDS-NG data for the IDIQ contract to ensure that inappropriately obligated funds are not included in the FY 2010 Small Business Goaling Report.

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The OIG has established an e-mail address, oig@sba.gov that we encourage the public to use to communicate with our office. We welcome your comments concerning this update or other OIG publications. To obtain copies of these documents please contact:

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