Office of Inspector General

August-September 2013

Business Loans

Texas Couple Pleads Guilty to Conspiracy

On August 9, 2013, a Texas husband and wife each pled guilty to one count of conspiracy. An Order for Presentence Restitution was signed, and the defendants paid $150,000. The investigation revealed that the couple applied for and received a $420,000 SBA-guaranteed loan to purchase a convenience store. The husband purported to the lender that most of the cash injection was coming from the sale of a previously owned convenience store. In reality, the couple had depleted the majority of those funds prior to closing on the loan. Further, the wife secured lines of credit (LOC) from two banks using different company names, and at least $91,269 of the $146,359 cash injection was derived directly from the LOC. In their dealings with the SBA lender, the couple did not disclose these additional debts, and they certified the accuracy of false personal and business financial statements. The couple later filed for bankruptcy and listed the above referenced LOC as part of their $456,806 in unsecured debts.

North Dakota Man Sentenced for Bank Fraud

On August 13, 2013, a North Dakota man was sentenced to 15 months in prison, 60 months supervised release, and ordered to pay $2,781,392 in restitution and a $200 special assessment fee. The man previously pled guilty to one count of bank fraud and one count of making a false entry in bank records. The man, a former loan officer at a bank, provided inaccurate and misleading information in order to secure a $2 million SBA-guaranteed loan for a business. The investigation also determined that he failed to properly verify the cash injection and to provide the required proof that the loan proceeds were used according to the agreed upon terms. This case was initiated based on a referral from the SBA National Liquidation & Guaranty Purchase Center in Herndon, VA. This is a joint investigation with the U.S. Secret Service; the Federal Deposit Insurance Corporation OIG; the Federal Bureau of Investigation (FBI); the U.S. Immigration and Customs Enforcement, Office of Investigations; and the Tampa Police Department.

Alabama Man Pleads Guilty in Case Referred by the IRS-Criminal Investigations

On August 15, 2013, an Alabama man pled guilty to five counts of wire fraud, four counts of false statements to the SBA, three counts of false statements on loan and credit applications, and one count of money laundering. This case was based on a referral from the Internal Revenue Service-Criminal Investigations (IRS-CI). According to the referral, a business, wholly owned by the man, failed to file corporate or personal tax returns from 2002 through 2009. The investigation revealed that the man provided false and unfiled tax returns to a bank to secure a $300,000 SBA-guaranteed LOC for his business. The LOC had an outstanding balance of $80,876.42 when it was "charged off." Additionally, the man provided false corporate and personal tax returns to the SBA to qualify his business for initial 8(a) certification in June 2003 through September 2008. This is a joint investigation with the U.S. Army, Criminal Investigation Command, IRS-CI, and the Defense Criminal Investigative Service.

Virginia Man Sentenced in 504 Loan Program Fraud

On August 27, 2013, a Virginia business owner was sentenced to 57 months incarceration, 36 months supervised release, and ordered to pay a $400 special assessment fee and $1,820,195 in restitution, to be paid jointly and severally with his two co-defendants. The man previously pled guilty on March 6, 2013, to one count of conspiracy to defraud the United States, one count of conspiracy to commit money laundering, and one count of structuring currency transactions. The investigation revealed that he had participated in a multi-million dollar scheme involving bogus treasury checks and tax returns. In addition, he misrepresented his citizenship status in the course of obtaining a $149,000 SBA 504 loan and a $203,000 bank loan. This is a joint investigation with the FBI.

Two Texas Men Plead Guilty to Fraud

On September 9, 2013, one Texas man pled guilty to one count of conspiracy to commit wire fraud, while a second man pled guilty to one count each of wire fraud and conspiracy to commit wire fraud. The men were indicted on May 8, 2013. The indictment alleged that the first man provided fraudulent bank statements to a bank when securing a $990,000 SBA-guaranteed loan to purchase a hotel. Some statements were altered to show a significantly higher account balance and others showed the man as the account holder when the account actually belonged to the second man who was the seller of the hotel. Further, the indictment alleged that the seller secretly funded the buyer's full cash injection, attempting to disguise money loaned to the buyer as consulting fees and sales commissions. In July 2009, the buyer received a second SBA-guaranteed loan for $510,000 to make improvements and additions to the hotel. Again, the seller allegedly supplied the funds for the buyer's cash injection. Records in the loan file also identified the seller as the general contractor handling the construction project, in spite of his claim that he was planning to leave the United States.

New Jersey Man Sentenced for Conspiracy to Commit Bank Fraud

On September 9, 2013, a New Jersey man was sentenced to 24 months in prison and 36 months probation. The man was also ordered to pay restitution of $154,623 and a special assessment fee of $100. The man previously pled guilty on March 6, 2013, to a criminal information charging him with one count of conspiracy to commit bank fraud. The investigation revealed that an organized group of criminals was obtaining credit cards and loans from various lending institutions using false identities, documents, and business names. Loan officers at various banks were also involved in the scheme. Many of the loans were SBA-guaranteed under the Express Loan program and are in default. The man, as a member of this group, obtained three SBA-guaranteed Express loans totaling $130,000, as well as a $25,000 non-SBA loan. Each loan was from a different lending institution and all the loans have been charged-off. The man obtained these loans in the names of two fictitious companies. This is a joint investigation with the IRS-CI, the Englewood New Jersey Police Department, and the Bergen County Prosecutor's Office.

New Jersey Man Sentenced for Bank Fraud

Man Sentenced for Theft Related to SBIC Program

On September 23, 2013, a Kentucky man was sentenced to time previously served and three years of supervised probation. He was also ordered to pay $59,567.11 in restitution to the SBA. On June 26, 2013, the man pled guilty to three counts of theft and one count of false statements on a loan application. He was indicted on these charges on December 4, 2012. The investigation revealed that the SBA appointed the man and his company to liquidate a portfolio of small business concerns of an investment firm, pursuant to the Small Business Investment Company Program. From 2008 to 2010, the man diverted the proceeds of sales from the investment firm's small business concerns into a fraudulently opened bank account and converted those proceeds for his personal use. The diverted funds exceeded $59,000.

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Recovery Act

California Woman Sentenced on False Statements

On September 3, 2013, a California woman was sentenced to three months imprisonment and one year of supervised release. The woman was also ordered to serve 200 hours of community service and to pay $1,179,525.22 in restitution and a $100 special assessment fee. The woman pled guilty to one count of making false statements to a federally insured bank. The investigation revealed that that the woman failed to disclose liabilities owed to friends and family and past-due tax debt in her application for a $1,750,000 bank loan to consolidate business debt and acquire working capital. The SBA guaranteed this loan using American Reinvestment and Recovery Act funds.

California Man Sentenced for Falsifying Loan Application

On September 30, 2013, a California man was sentenced to three months in prison, three months home confinement, and two years of supervised release. He was also ordered to pay restitution of $47,747. The man pled guilty to knowingly falsifying material facts in a loan application with the SBA. In March 2009, the man, doing business as a cabinet company, applied for a $50,000 SBA-guaranteed small business loan under the

American Recovery and Reinvestment Act of 2009. The man signed the SBA forms to certify that the information contained in his application was true and complete. However, the man misrepresented his criminal history by certifying that he never been involved in bankruptcy proceedings when in fact, he had.

Government Contracting

North Carolina Men Plead Guilty to False Statements

On September 4, 2013, the chief financial officer and the president of a North Carolina masonry firm pled guilty to a criminal information, filed on July 17, 2013, charging each of them with a one count of false statements. The defendants, representing a subcontracting firm, caused the prime contractor of a federal contract at Camp Lejeune, North Carolina, to make a false statement to the Department of the Navy. Specifically, the prime contractor claimed to have successfully met its small business subcontracting goals when it had not. The investigation revealed that in early 2011, the Naval Facilities Engineering Command Mid-Atlantic (NAVFAC) in Norfolk, Virginia, issued a "Solicitation, Offer and Award" for a series of construction projects at Camp Lejeune. This contract, valued at over $67 million, was awarded to a prime contractor in August 2011. The sub-contractor submitted a $9.4 million bid to do masonry work for the prime contractor. An employee of the prime contractor subsequently told the chief financial officer of the masonry firm that his company would receive the subcontract if it used a minority-owned company. The CFO agreed to use an affiliated company, one that he controlled, to receive the subcontract. All of the work on the subcontract passed through the affiliated firm to the masonry company. This is a joint investigation with the DCIS and the Naval Criminal Investigative Service.

Florida Firm Enters Civil Settlement in SDVOSB Case

On September 11, 2013, a civil settlement was reached between a Florida business and the U.S. Attorney's Office. In the settlement, the company agreed to pay the United States $50,000 plus 1% of its total annual revenues from 2014 through 2018. The civil suit was based on the allegation that the company obtained government contracts for which it was not eligible. These contracts had been "set aside" for award to service-disabled, veteran-owned small businesses (SDVOSB). The firm was determined to be ineligible for these contracts based on its affiliation with two other firms, which were both large companies. The investigation revealed that the two other firms conducted the majority of the work on these contracts. The settlement amount was based on an ability to pay analysis conducted by the Department of Justice and is in lieu of a potential claim amount of $18,145,659. This is a joint investigation with the Department of Justice and the Department of Homeland Security (DHS) OIG.

Trial Nets Convictions for President and Shareholder of Idaho Firm

On September 19, 2013, after a 26-day trial, the president and majority stockholder of an Idaho construction firm and a minority shareholder in the firm were each found guilty on all counts charged in a Superseding Indictment filed on May 17, 2013. The president's convictions included four counts of filing false individual and corporate tax returns, two counts of conspiracy to defraud the United States, five counts of wire fraud, five counts of mail fraud, one count of false statements, three counts of interstate transportation of property taken by fraud, one count of conspiracy to obstruct justice, and one count of obstruction of justice. The minority shareholder was found guilty of two counts of obstruction of justice and one count of conspiracy to obstruct justice.

The investigation disclosed that president took steps to lower, artificially, her personal net worth, such as acquiring, holding, and transferring assets into the names of

26-Day Trial Ends in Conviction of Two

nominees in order to appear to be economically disadvantaged. This allowed her construction company to qualify for the Department of Transportation's (DOT) Disadvantaged Business Enterprises (DBE) and SBA's 8(a) programs. The president also filed false and fraudulent tax returns that did not report all income she or the business received. The false returns and financial statements were submitted in support of the business' applications to the SBA 8(a) Program and the DBE Programs for Idaho and Utah. The business received more than $2.5 million in federal government contracts based on the company's fraudulently obtained SBA 8 (a) status, and more than $15 million in state government contracts based on the company's fraudulently obtained DBE status in the states of Idaho and Utah. The government is seeking $9,237,722.10 in forfeiture from the woman, which represents the proceeds obtained as a result of her criminal conduct. This is a joint investigation with the IRS-CI, DOT OIG, and the FBI.

Missouri Man Enters Pre-Trial Agreement in SDVOSB Fraud

On September 20, 2013, the president of a Missouri contracting firm entered into a pre-trial diversion agreement with the U.S. Attorney's Office. The agreement reflects that the president accepted responsibility for participating in false, fraudulent, and deceptive practices with respect to government contracting. The man, a service-disabled veteran, was hired to serve as the figurehead president of the contracting firm to qualify the company as an SDVOSB. As an SDVOSB, the firm obtained government contracts and served as a pass through for another construction company. The man, however, was not involved in the daily operations nor did he control the company. He was paid a small percentage of the income from the contracts for his services. The pre-trial diversion agreement calls for the deferment of prosecution for a period of 18 months during which time the man must abide by certain conditions. One condition, which the man has already met, was to make restitution payments totaling $21,610.20, to cover the cost of investigative activities, to the three federal agencies involved in the investigation. This is a joint investigation with the General Services Administration OIG and the Veteran's Administration (VA) OIG.

Missouri Firm Pleads Guilty to Conspiracy to Defraud the Government

On September 27, 2013, a Missouri contracting firm was charged and pled guilty to one count of conspiracy to defraud the U.S. Government. The investigation showed that the firm, which was not a legitimate SDVOSB, received approximately $3.4 million in SDVOSB set-aside contracts from the U.S. Department of Veteran Affairs. The investigation also revealed that the firm was not controlled by a service-disabled veteran but acted as a shell company in order for second firm to receive SDVOSB set-aside contracts, which it was not qualified to receive. The vast majority of work awarded to the contracting firm was passed through to the second firm. This is a joint investigation with the GSA OIG and the VA OIG.

Disaster

Texas Woman Sentenced for Theft of Government Funds

On September 13, 2013, a Texas woman was sentenced to 18 months imprisonment and 3 years supervised release. She was also ordered to pay $96,900 in restitution as a result of her February 20, 2013, guilty plea to one count of theft of government funds. The investigation disclosed that the woman altered repair invoices and filed them with the SBA in support of a $97,385 disaster loan she received for her Violet, Louisiana residence, which was damaged by Hurricane Katrina. In addition, in November 2012, the woman was convicted in Texas for misprision of a felony. She was sentenced to three years supervised release for participating in a similar scheme involving SBA disaster loans obtained by her family members. This is a joint investigation with DHS OIG.

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Ineligible Firm Pleads Guilty to Conspiracy to Defraud the Government After Receiving $3.4 Million in Set-Aside Contracts

Agency Management

Audit Report 13-18

On September 27, 2013, the OIG issued Audit Report 13-18, *The SBA Did Not Effectively Manage Defaulted Disaster Loans to Maximize Recovery from 2006 to 2011.* The objective of this audit was to determine whether the Small Business Administration National Disaster Loan Resolution Center: (1) effectively managed delinquent disaster loans to maximize recovery and minimize losses, (2) complied with applicable laws and regulations, and (3) had a mission aligned with Federal debt collection objectives.

The OIG determined that the SBA National Disaster Loan resolution Center (NDLRC) did not effectively manage delinquent disaster loans to maximize recovery and minimize losses. During the five-year period from June 2006 through June 2011, the NDLRC charged off approximately 9,035 defaulted disaster loans. The OIG estimates that at least 7,198 of these loans, totaling $752.6 million, were charged off without using all appropriate collection tools to maximize recovery.

The OIG concluded that the SBA was not successful in maximizing recovery because management did not: (1) align the NDLRC mission with Federal debt collection objectives; (2) adhere to existing controls, including Standard Operating Procedures (SOPs); (3) include requirements of the DCIA in the SOP; (4) provide oversight of loan collateral, or have an effective Management Information System to monitor and track the collateral, (5) ensure that staff were properly trained; or, (6) ensure that management and staff performance goals emphasized effective debt recovery.

Audit Report 13-19

On September 27, 2013, the OIG issued Audit Report 13-19, *Evaluation of SBA's Implementation of the GPRA Modernization Act of 2010.* The objective of this evaluation was to determine if the SBA met statutory reporting requirements of the Modernization Act in its 2014 Agency Performance Plan and 2012 Agency Performance Report.

The OIG evaluated the SBA's Performance Management reporting, to include its 2013 and 2014 Agency Performance Plans, 2011 and 2012 Agency Performance Reports, and Agency Quarterly Performance Update presentations. The OIG also evaluated a limited sample of program performance indicators to understand how performance information is reported to the SBA Performance Management Office. The OIG performed this review in accordance with *Quality Standards for Inspection and Evaluations* issue by the Council of the Inspectors General on Integrity and Efficiency. The OIG found the SBA to be generally compliant with the GPRA Modernization Act's reporting requirements; however, the OIG identified omissions in a few areas. The OIG made one recommendation to help improve the SBA's GPRA Modernization Act Reporting.

Audit Report 13-20

On September 30, 2013, the OIG issued Audit Report 13-20*, The Small Business Administration's Controls Over Cash Gifts*. The SBA has gift authority under sections 4(g), 8(b)(1)(G), 5(b)(9) and 7(k)(2) of the Small Business Act (the Act). The objective of this review was to assess whether the SBA was following established procedures for soliciting, accepting, holding, and utilizing cash gifts in fiscal year 2012. Section 4(g)(2) of the Act provides that any gift, devise, or bequest of cash accepted by the Administrator shall be held in a separate account and shall be subject to semi-annual audits by the Inspector General who shall report his or her findings to Congress.

The OIG determined the SBA adequately complied with the Act regarding the acceptance, holding, and utilization of cash gifts. The responsible SBA officials determined the gifts were something the Agency could use and that its use would further the mission of the Agency. The non-federal organizations that gifted cash donations were properly vetted through the SBA's program offices to ensure no business relationships existed that would cause a conflict of interest in accordance with the Act.

During the 2011 review, the OIG noted that the SBA had not had permanent procedures on gift acceptance in place since 2007. The OIG also noted that the procedural notice that prescribes SBA's control over the B Assistance Trust (BAT) Fund expired in 2005. The OIG previously recommended that the SBA's Office of General Counsel collaborate with the Offices of the Chief Financial Officer and Strategic Alliances to issue SOP 90 53 to include procedures for soliciting, accepting, depositing, expending, and tracking expenditures, as well as documentation retention requirements for cash gifts. During the FY 2012 review, the OIG found that the SBA still had not issued this SOP.

Audit Report 13-21

On September 30, 2013, the OIG issued Audit Report 13-21, *The Small Business Administration's Enterprise-wide Controls Over its Cosponsored Activities.* The objective of this limited scope audit was to determine the adequacy of controls over the SBA's cosponsored activities in accordance with federal laws, regulations, and policies. The OIG did not assess the validity and eligibility of individual expenses for the cosponsored activities.

The OIG determined that for its cosponsored activities, the SBA did not fully implement effective controls to comply with the requirements stipulated in Title 13, Part 106 of the Code of Federal Regulations (CFR) and SOP 90 75 3, Outreach Activities. Specifically, the SBA did not (1) consistently vet and perform conflicts of interest determinations, (2) report on the results of its activities within established timeframes, and (3) control excess funds that remained at the conclusion of those activities.

The OIG concluded that opportunities exist to strengthen SBA's controls over cosponsored activities that include:

- Fully implementing additional controls over cosponsorship approval and closeout procedures;
- Strengthening controls over the maintenance of official cosponsorship files to ensure that all required documentation is obtained; and
- Performing effective Quality Service Reviews on all cosponsored activities to ensure that laws, regulations, and SBA policy were followed.

To help implement stronger controls and oversight of cosponsored activities, the OIG made eight recommendations to several SBA officials.

Audit Report 13-22

On September 30, 2013, the OIG issued Audit Report 13-22, *Improved Examination Quality Can Strengthen SBA's Oversight of Small Business Investment Companies.* During survey work, the OIG identified deficiencies in the management of the SBIC examination process and as a result, the OIG developed a reporting objective to identify key challenges the Office of Investments and Innovation (OII) faced in executing its SBIC examination function.

The OIG found that improvements to SBA processes could enhance the extent to which the Office of SBIC Examinations identifies business conditions and practices prohibited by the Small Business Act and Agency policy. Specifically, the OIG found that the SBA's focus on the frequency of examinations as a strategy for reducing risk did not include a compensating control to ensure that examinations conducted would result in accurate assessments of regulatory compliance. With a greater emphasis on quantity, the OSE runs the risk that the review of an SBIC may be inaccurate or incomplete. To this point, the significant decrease in examination reports with findings could indicate that the quality of these assessments has suffered. Outdated guidance and incomplete examination checklists also affected the quality of the SBIC examination process. The examiners were impacted by challenges in the areas of strategic planning, training, technology, communication and funding. These challenges, coupled with an emphasis on quantity resulted in examiners not identifying all findings. The OIG made three recommendations.

Office of Inspector General

Peggy E. Gustafson

Inspector General

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To promote integrity, economy, and efficiency, we encourage you to report suspected instances of fraud, waste, abuse, or mismanagement in any SBA program to the OIG Hotline* at
http://www.sba.gov/office-of-inspector-general/2662

Or call the OIG Hotline toll-free, at (800) 767-0385

**In accordance with Sections 7 and 8L(b)(2)(B) of the Inspector General's Act, confidentiality of a complainant's personally identifying information is mandatory, absent express consent by the complainant authorizing the release of such information.*

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