Office of Inspector General

March 2015

Business Loans

California Man Sentenced to 6 Months of Home Detention and 3 Years of Supervised Release

On March 9, 2015, a California man was sentenced to 6 months of home detention and 3 years of supervised release for his involvement in fraudulently obtaining Section 7(a) business loans from the Small Business Administration (SBA). He was also ordered to pay restitution of $210,000 and to participate in mental health treatment. The man had previously pled guilty to mail fraud in July 2014.

In May 2012, a grand jury had indicted a husband, his wife, their daughter, and the above man for fraud. The first three individuals owned a gas station and car wash in California. The indictment alleged that the defendants executed a scheme to defraud a financing corporation, a bank, and SBA by making false statements to obtain loans for that business.

As part of the scheme, the husband and a co-conspirator included false information in the loan application regarding the straw buyer's experience and assets. In addition, the husband and a co-conspirator falsely advised the bank that a $600,000 equity down payment had been used for the purchase of the business, when in fact no down payment was made. Consequently, the man and another individual entered into a series of transactions designed to create the false appearance that the family had invested $600,000 of its own funds into purchasing the business. SBA, which partially guaranteed the bank loan, lost nearly $1 million. The SBA Office of Inspector General (OIG) initiated this investigation, which was later joined by the Federal Bureau of Investigation (FBI).

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Maryland Man Sentenced to 51 Months in Prison for Conspiracy to Commit Bank Fraud

On March 11, 2015, a Maryland man was sentenced to 51 months in prison, to be followed by 3 years of supervised release, and was ordered to pay restitution of $950,000. He had previously pled guilty to conspiracy to commit bank fraud.

The man had created a real estate investment firm to buy a liquor store and was the majority owner of that firm. In May 2006, he and an individual with a minority ownership interest in the firm signed agreements to buy the liquor store for $899,000 and the related real estate for $400,000.

The man sought a principal of a capital investment company to broker a loan for the store's purchase. The pair discussed obtaining an SBA-guaranteed loan from a bank. The man disclosed to the broker that he could use a straw buyer for the loan. Together, they agreed to falsely represent to the bank that another individual would be the owner and operator of the liquor store. At the September 2006 settlement for the sale of the liquor store to the real estate investment firm, the straw purchaser falsely represented to the bank that he was the president of the real estate investment firm. The funds needed to close the transaction were provided by the Maryland man, and not the straw purchaser. The bank funded a loan of $950,000.

After the closing, the Maryland man operated the liquor store. In January 2007, he sold a 50 percent stake in the store to another individual for $380,000 and claimed that he owned 100 percent of the store. In 2007, he stopped making loan payments to the bank, and the loan went into default.

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Former Vice President of Iowa Bank Charged for Submitting False Documents and Identity Theft

On March 18, 2015, the former senior vice president of an Iowa bank was charged in a superseding indictment with submitting false documents to a bank and aggravated identity theft. From March 2003 until March 2010, the man allegedly assisted other schemers in acquiring fraudulent loans by filling out loan documents without the knowledge or consent of the purported borrowers. They subsequently used the loan proceeds for personal expenses, business operating expenses, and payments for delinquent loans held by the schemers and others at the bank. When these fraudulent loans matured, the former senior vice president allegedly used false signatures of the unwitting borrowers to extend the loan maturities to further conceal the debt.

Four defendants have pled guilty thus far. The bank executive is the remaining defendant. This joint investigation is being conducted in conjunction with the Federal Deposit Insurance Corporation (FDIC) OIG, the Iowa Department of Criminal Investigation, and FBI.

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Government Contracting

Florida Building Company Agrees to Pay $1.1 Million for Fraudulently Obtaining Government Contracts

On March 10, 2015, a settlement was executed in a civil case between a large Florida building company and the U.S. Attorney's Office. The company agreed to pay the U.S. Government $1.1 million. The civil suit was based on an allegation that a firm acted as a "front" for another large company owned by the Florida building company. The "front" firm allegedly obtained Government contracts set aside for service-disabled veteran-owned small businesses (SDVOSB) for which it was not eligible. Moreover, the two large companies were found to have conducted the majority of the contract work. This investigation was conducted jointly with the Department of Justice and DHS OIG.

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Nebraska Man Sentenced to 2 Years of Probation and Forfeiture of $3.35 Million

On March 12, 2015, a Nebraska man was sentenced in a U.S. District Court in Iowa to 2 years of probation, 180 days in a residential reentry program (halfway house), and forfeiture of all interest in over $3.35 million seized by the U.S. Government and determined by the court to be profits from a fraud scheme. In addition, his paving corporation was sentenced to 2 years of probation after having previously pled guilty to money laundering. His business partner's contracting firm was also sentenced to 2 years of probation. Per a plea agreement, the Government agreed to dismiss all charges against the partner, a service-disabled veteran (SDV) utilized by the Nebraska man to perpetrate the scheme. The Nebraska man had previously pled guilty to major program fraud, and his corporation had pled guilty to money laundering to further a contracting fraud scheme. His admissions of guilt followed a guilty plea entered by his business partner's contracting firm to major program fraud and wire fraud. In May 2013, a Federal grand jury in Iowa had indicted the two men and their companies in connection with a $23.5 million SDVOSB fraud scheme.

The investigation showed that, from May 2007 through August 2010, the contracting firm unlawfully received 45 set-aside and sole-source SDVOSB contracts from the U.S. Department of Veterans Affairs (VA) and the Department of Defense, including contracts involving American Recovery and Reinvestment Act funds. The contracting firm was a pass-through and front company for the Nebraska man's other businesses, such as the paving corporation. His business partner was simply a figurehead used for his SDV status. This was a joint investigation with the General Services Administration (GSA) OIG, VA OIG, FDIC OIG, and the Defense Criminal Investigative Service (DCIS).

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President of Colorado Firm Pleads Guilty to Conspiracy

On March 16, 2015, the owner and president of a Colorado firm pled guilty to conspiracy. The plea was based on his August 2014 indictment for making false statements to SBA, conspiracy, and filing false tax returns. The investigation discovered that he had directed his accountant and the company's controller to conceal millions of dollars in assets, including a condominium in Vail, Colorado. He also diverted millions of dollars in unreported income, mostly through overseas accounts. This action was omitted from SBA annual updates and financial statements. In doing so, he maintained the firm's certification as a Section 8(a) disadvantaged business. Finally, he concealed the assets and income from the Internal Revenue Service (IRS) by filing false tax returns. The misrepresentations led to the wrongful award of over $17 million in 8(a) set-aside contracts to the firm from 2006 to 2010.

This is a joint investigation with DCIS, IRS Criminal Investigation, GSA OIG, and U.S. Army Criminal Investigation Command. This matter was referred by GSA OIG.

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Massachusetts HUBZone Firm and Owner Suspended

On March 27, 2015, SBA suspended a Massachusetts HUBZone firm and its sole owner. This action prohibits the company from being awarded any new Government procurements. SBA's decision was based on information previously provided by OIG, which disclosed that the firm operated primarily from its non-HUBZone office location. The suspension barred the company from receiving two GSA indefinite delivery/indefinite quantity (IDIQ) procurements scheduled to be awarded in April 2015. The firm had been the leading bidder and was expected to win both awards. The first IDIQ procurement had a maximum value of $20 million and the second had a maximum value of $15 million. Consequently, the firm's suspension resulted in a cost avoidance of $35 million. This investigation is being worked jointly with GSA OIG and is based on its referral alleging fraudulent behavior by the company.

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Disaster Loans

New Jersey Man Pleads Guilty to Theft by Deception

On March 20, 2015, a New Jersey man pled guilty to theft by deception based on previous charges for filing false applications to collect Federal relief funds after Hurricane Sandy. He also made $116,900 in full restitution, of which $31,900 was paid to the Federal Emergency Management Agency (FEMA) and $85,000 to the State of New Jersey. The man had received $31,900 in FEMA grants, a $10,000 grant under the Homeowner Resettlement Program (RSP), and a $75,000 grant under the Reconstruction, Rehabilitation, Elevation and Mitigation Program. The last two grants were funded by the U.S. Department of Housing and Urban Development (HUD) and administered by the New Jersey State Department of Community Affairs (DCA). The man had claimed that his primary residence was damaged by the hurricane. However, that house allegedly is a vacation property, and his primary residence is elsewhere. He had applied for an SBA Disaster Home Loan and was declined in December 2013 because he had indicated that the relevant property was not his primary residence. This investigation was worked jointly with a task force comprised of the New Jersey DCA, the U.S. Department of Homeland Security (DHS) OIG, and HUD OIG, under the direction of the New Jersey Office of the Attorney General.

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Homeowner Couple Allegedly Filed False Applications for Sandy Relief Funds

On March 24, 2014, the New Jersey Office of the Attorney General filed two separate complaints against a homeowner couple who allegedly filed false applications to collect Federal relief funds after Hurricane Sandy. The man, a Florida resident, was charged by a complaint-summons with theft by deception, and his wife, also a Florida resident, was charged by a complaint-summons with theft by deception and unsworn falsification. They allegedly received $91,900 by filing fraudulent applications. The couple received $31,900 in grants from FEMA and a $10,000 RSP grant. Moreover, they were approved for a $129,600 SBA Disaster Home Loan, from which they received $50,000 in proceeds. The couple had claimed that their primary residence in New Jersey was damaged by the hurricane. That house allegedly is a vacation property, and the primary residence is actually in Florida. This investigation was worked jointly with a task force comprised of the New Jersey DCA, DHS OIG, and HUD OIG, under the direction of the New Jersey Office of the Attorney General.

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Business Loans

SBA Needs to Improve its Oversight of Lender Service Providers

On March 12, 2015, OIG issued Report 15-06, *Improvement is Needed in SBA's Oversight of Lender Service Providers*, which presents the results of our audit of the Small Business Administration's oversight of lender service providers (LSPs) as loan agents.

LSPs are deeply involved in all phases of the loan life cycle, including originating, closing, servicing, and liquidating SBA business loans. Since the number of LSPs and their agreements with lenders have significantly increased in recent years, SBA will need to improve its internal controls to ensure LSPs' performance and conduct complies with SBA's requirements. OIG determined that SBA had not established a method to track LSP portfolio activities, and therefore could not adequately assess potential risks associated with LSP involvement in SBA loan programs. In addition, SBA did not adequately investigate a number of potential violations of SBA policy by lenders and LSPs, such as a lack of approved agreements. OIG recommended two actions that will help strengthen SBA's oversight of LSPs and their relationships with SBA lenders. The Agency agreed with OIG's findings and recommendations, and has already taken some steps to improve its oversight of LSPs.

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The OIG High Risk 7(a) Loan Review Program Recommends $1.8 Million in Recoveries

On March 20, 2015, OIG issued *Report* 15-09, *The OIG High Risk 7(a) Loan Review Program Recommends $1.8 Million in Recoveries*, which presents the results of OIG's ongoing High Risk 7(a) Loan Review Program from July 2014 to February 2015.

OIG's review of seven early-defaulted loans identified material lender origination and closing deficiencies that justified denial of the guaranty for three loans totaling $1.8 million. To facilitate SBA's timely review and recovery of these payments, OIG issued three notices of finding and recommendation (NFR) that included detailed descriptions of the identified material deficiencies.

Two of the three loans with material deficiencies financed change of ownership transactions. We have previously identified change of ownership transactions as high risk. We also identified material lender underwriting deficiencies (i.e. repayment ability) in all three loans. In a previous audit, we determined that SBA's limited reviews of lender underwriting resulted in improper payments. In addition, the National Guaranty Purchase Center quality control team reviewed one of the three loans during the purchase review process, but did not identify any material deficiencies with the loan. Further, this same loan was included in SBA's FY 2014 review of improper payments and was not identified as an improper payment.

OIG recommended that SBA require the lenders to bring the three loans into compliance and, if not possible, seek recovery of approximately $1.8 million from the lenders. The Agency agreed with the recommendations and is working with the lenders to either bring the loans into compliance or recover the improper payments.

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Agency Management

SBA Needs to take Actions to Close 32 Open Recommendations and Take Additional Measures to Ensure Information Technology is Secure

On March 13, 2015, SBA OIG published its Report 15-07, *Weaknesses Identified During the FY 2014 Federal Information Security Management Act Review*. The Federal Information Security Management Act (FISMA) requires that OIG review SBA's information technology security program. To determine SBA's compliance with FISMA, OIG contracted with an independent public accountant, KPMG, to perform review procedures relating to FISMA. OIG monitored KPMG's work and reported SBA's compliance with FISMA in the Agency FISMA filings in November 2014. OIG also assessed the Agency's progress in implementing open recommendations and compared our current year assessment with its fiscal year 2013 FISMA evaluation. In addition to the 32 open FISMA recommendations noted in Appendix II, OIG made 6 new recommendations to address FISMA-related vulnerabilities. SBA fully agreed with all six recommendations, and projected they would be implemented by February 2017.

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SBA Complied with the Small Business Act's Requirements Regarding Cash Gifts

On March 18, 2015, SBA OIG published Report 15-08, *SBA's 2014 and 2015 Cash Gifts*. 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). Employees may solicit and accept gifts on behalf of SBA after proper approvals, including a conflict of interest determination by SBA's Office of General Counsel. 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 semiannual audits by the Inspector General who shall report his or her findings to Congress.

The objective of the OIG evaluation was to determine whether SBA's controls were adequate over the solicitation, acceptance, holding, and utilization of cash gifts. To accomplish this objective, OIG interviewed key SBA employees and reviewed various management and financial records available for fiscal years 2014 and 2015. Overall, OIG's evaluation found that SBA complied with the Act regarding the solicitation, acceptance, holding, and utilization of cash gifts.

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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.*

We welcome your comments concerning this update or other OIG publications.

To obtain copies of these documents please contact us at:

SBA Office of Inspector General
409 Third Street SW, 7th Floor
Washington, DC 20416
E-mail: oig@sba.gov
Telephone: (202) 205-6586 FAX (202) 205-7382

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