



Office of Inspector General U.S. Small Business Administration

July 2011 Update

Business Loan Programs

Review of Lender Practices in Originating Huntington Learning Center Franchise Loans

On July 13, 2011, the OIG issued a [report](#) on the results of an audit of Banco Popular's assessment of borrower repayment ability when originating Huntington Learning Center (HLC) franchise loans. The audit was conducted in response to a complaint alleging, in part, that lenders originated SBA-guaranteed loans made to HLCs based on inflated gross revenue projections submitted by loan brokers. The objective of the audit was to determine whether the complainant's lender, Banco Popular, adequately assessed borrower repayment ability when originating HLC franchise loans.

We reviewed all 12 HLC loans approved by Banco Popular during fiscal year 2007 using Preferred Lender Program (PLP) procedures and found that it did not adequately assess repayment ability when approving the loans. Specifically, the lender accepted unrealistic projected annual revenue figures that ranged from \$483,000 to \$650,025 as a basis for demonstrating the ability of the HLC franchises to repay their debts. The lender disregarded relevant and available data, which indicated that the franchises' revenue projections were unreasonable, which was partly due to the lender's perception that franchise loans required a lesser degree of due diligence. Had the lender complied with SBA's requirements, the 12 loans should have been declined. As of December 2010, there were 10 loans, with an aggregated outstanding SBA balance of \$2.1 million, which had been transferred to liquidation.

During the course of the audit, we also noted that SBA's Loan Accounting System did not accurately reflect or track franchise loans guaranteed by the agency, with the number of loans for these franchises inaccurately reported by an average of 17 percent. This data reliability issue could also negatively impact decisions made by lenders for loan approval and prospective borrowers that are considering franchise opportunities, as well as the ability of franchisors to attract new investors.

We recommend that the SBA: (1) seek recovery of the loan guaranties, less any recoveries, paid in connection with the 10 defaulted loans; (2) flag all Banco Popular HLC loans in SBA's Loan Accounting System to ensure the identified underwriting deficiencies are considered in the event of future default; and (3) implement a plan to ensure the completeness and accuracy of data pertaining to existing franchise loans and those made in the future.

Maine Businessman Convicted on False Statements

On July 11, 2011, the owner of a Kittery, Maine business was convicted in a jury trial in U.S. District Court, District of Maine, on one count of false statements. The subject had applied for a \$1.3 million SBA-guaranteed loan and submitted an SBA Form 912, Personal History, indicating that he had no prior criminal convictions. In truth, he had four previous convictions on criminal violations. The U.S. Attorney's Office in Portland, Maine referred this case to the OIG in the course of a health care fraud investigation in which they learned that the subject had falsified SBA documents.

Georgia Learning Center Owner Pleads Guilty

On July 12, 2011, in U.S. District Court for the Northern District of Georgia, a business owner pled guilty to a Criminal Information, filed on the same date, charging her with one count of conspiracy to defraud the United States. The subject was the owner of an educational academy in McDonough Georgia. In June 2008, the academy was sold via a 504 loan package worth \$3,175,000. The investigation disclosed that the owner orchestrated this deal as a "straw" transaction involving an unindicted co-conspirator. She never intended to relinquish possession of the academy and used the proceeds of the loan to continue to operate the business. Further, she caused the unindicted co-conspirator to falsely state that the sale would be supported by an equity injection of \$296,200 from the borrower when, in fact, no equity would be provided by the borrower. This is a joint investigation with the Federal Bureau of Investigation (FBI).

Three Indicted in Texas on Conspiracy and Bank Fraud

Three subjects were indicted on July 19, 2011, in the Northern District of Texas. Each was charged with one count of conspiracy to commit bank fraud and two substantive counts of bank fraud. In addition, one defendant, an attorney, was charged with one count of witness tampering. The indictment alleges that the defendants conspired to deceive a Prosper, Texas, bank and another bank in Garland, Texas, by fraudulently inducing them to make loans to one of the co-defendants. The conspiracy involved one SBA-guaranteed loan to purchase a laundromat and two commercial loans, totaling over \$1.3 million, to purchase land. Both purchases involved companies affiliated with a co-defendant. The indictment alleges that the defendants misrepresented assets and the source of the equity injection and down payment funds. The witness tampering count alleges that the attorney made several statements to another defendant to persuade her to lie and withhold information if she were to be interviewed by the FBI at a later date. This is a joint investigation with the FBI.

Former Missouri Bank VP Guilty of Bank Fraud

On July 22, 2011, in the Western District of Missouri, the former vice president of a Richland, Missouri bank, was charged in a Criminal Information and pled guilty to one count of bank fraud. The investigation disclosed that he knowingly and intentionally engaged in approximately 15 fraudulent transactions, involving both SBA and non-SBA loans, in order to divert funds to his own personal accounts. His activity resulted in an approximate loss of \$451,763 to the bank. This is a joint investigation with the Federal Deposit Insurance Corporation OIG and the FBI.

Businessman Pleads Guilty to Mail Fraud

On July 26, 2011, in U.S. District Court, Western District of North Carolina, the president of a Warsaw, North Carolina business was charged via a Bill of Information with four counts of mail fraud. On July 27, 2011, he pled guilty to all four counts. According to the information, he aided and abetted others engaged in a scheme to defraud the SBA and financial institutions out of at least \$92,500 by fraudulently submitting loan applications and documentation for SBA-guaranteed loans and diverting the proceeds of such loans for unauthorized purposes. This case was initiated by the OIG based on a referral from the SBA lender. This is a joint investigation with the U.S. Postal Inspection Service.

Disaster Loans

Louisiana Contractor Pleads Guilty

On July 20, 2011, a contractor pled guilty in U.S. District Court for the Eastern District of Louisiana to a Bill of Information charging one count of theft of public funds. The defendant applied to the SBA for a low interest disaster loan to repair his New Orleans rental properties damaged by Hurricane Katrina. The investigation disclosed that he submitted fraudulent documents to the SBA in support of repairs to the rental properties. Because of his misrepresentations, he received multiple loan disbursements totaling \$103,100 from the SBA. This is a joint investigation with the Department of Housing and Urban Development (HUD) OIG.

Texas Property Manager Pleads Guilty to Conspiracy

On July 22, 2011, a property manager pled guilty in U.S. District Court for the Southern District of Texas to one count of conspiracy. Previously, on June 29, 2011, he and two brothers were each charged in a superseding indictment with conspiracy and fraud in connection with a major disaster. These charges involve a false invoice scheme relating to approximately \$1 million in SBA home and business disaster loans. The property manager falsely represented that Hurricane Ike had damaged a rental property. The investigation determined that the damage to the rental property had been caused by an intentional fire set prior to Hurricane Ike. This case was referred to the OIG by the SBA Processing and Disbursement Center, Fort Worth, Texas. This is a joint investigation with the Department of Homeland Security (DHS) OIG.

Homeowner Indicted for Theft of Government Funds

On Friday, July 29, 2011, a homeowner was indicted in U.S. District Court for the Eastern District of Louisiana on one count of theft of government funds. The indictment, based on an investigation by the SBA OIG and the HUD OIG, charges that the subject provided false statements to the affected agencies in an attempt to receive benefits to which he was not entitled. As a result of damage to his home by Hurricane Katrina, the SBA approved a disaster home loan of \$141,800. The indictment alleges that he submitted false receipts to the SBA indicating that he spent \$11,716 and \$51,688 on repairs to his primary residence. As a result of his misrepresentations, he received a loan disbursement from SBA totaling \$31,800. This is a joint investigation with the HUD OIG.

Government Contracting & Business Development

8(a) Business Owner Sentenced

On July 13, 2011, in U.S. District Court, District of Columbia, the owner of a design and remodeling business was sentenced to 18 months in prison, 36 months probation, \$389,738 in restitution and 360 hours of community service. The sentencing was the result of her guilty plea to one count of conspiracy and one count of false claims. The subject, the owner of an 8(a) certified design/remodeling business, conspired to submit falsified information to the U.S. General Services Administration (GSA) in the course of obtaining an 8(a) contract with DHS, Immigration and Customs Enforcement (ICE). As a result of the conspiracy, ICE suffered a loss of \$389,738. This is a joint investigation with the DHS ICE, the GSA OIG, and the Department of Justice Antitrust Division.

Agency Management

Former SBA Program Manager Pleads Guilty

On July 20, 2011, a former SBA program manager pled guilty to one count of theft of government property and one criminal forfeiture count. The former employee used a government travel card to rent automobiles for personal use and forged a supervisor's signature on travel authorizations and vouchers. As a result of the employee's false claims, the government paid fraudulent travel costs totaling \$7,919.68.

Peggy E. Gustafson, Inspector General

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