



# Office of Inspector General

March 2013



## Business Loans

### *Virginia Man Pleads Guilty*

On March 6, 2013, the owner of a Virginia business pled guilty 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 following an April 2012 indictment. The indictment contained forfeiture allegations, which notified the defendant that the United States sought a \$17.7 million money judgment against him. To satisfy this judgment, he will forfeit a number of assets including bank accounts and real property. The investigation revealed that he had engaged in a multi-million dollar treasury check scheme involving bogus treasury checks and tax returns. The man also misrepresented his citizenship status on SBA-guaranteed 504 loan documents. This is a joint investigation with the Federal Bureau of Investigation (FBI).

### *NJ Man Pleads Guilty to Conspiracy*

On March 6, 2013, a New Jersey man pled guilty to a Criminal Information charging him with one count of conspiracy to commit bank fraud. The investigation revealed that members of a criminal organization were obtaining credit cards and loans from various lending institutions using false identities, documents, and business names. Many of the loans were SBA-guaranteed, and the majority are in default. The man, using fictitious business names, obtained three SBA-guaranteed 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. This is a joint investigation with the

Internal Revenue Service - Criminal Investigations (IRS-CI), the Englewood New Jersey Police Department, and the Bergen County Prosecutor's Office.

### *Additional Charges in Loan Scheme*

On March 12, 2013, a multiple-count second superseding indictment was filed in Maryland charging an SBA loan brokerage company and several other individuals identified in the investigation, in connection with a scheme to fraudulently obtain business loans. The fraudulently obtained loans, which were guaranteed by the SBA, resulted in losses of over \$100 million.

- ◆ The loan brokerage company and several other defendants were each charged with conspiracy to commit bank fraud, bank fraud, money laundering, aiding and abetting, and criminal forfeiture.
- ◆ Two new defendants, working as title agents and/or title attorneys, one located in Maryland and the other in Virginia, were each charged with conspiracy to commit bank fraud, bank fraud, money laundering, aiding and abetting, and criminal forfeiture.
- ◆ On March 19, 2013, the main co-defendant pled guilty to conspiracy to commit bank fraud; while the remaining co-defendant is an international fugitive. The two main defendants owned a loan brokerage company specializing in securing loans for individuals interested in purchasing or refinancing small businesses in the Mid-Atlantic area. They encouraged prospective borrowers to use the services of

their loan brokerage company to apply for business loans through the SBA's Section 7(a) program. The investigation revealed that the main defendants and others submitted SBA loan applications and supporting documentation to loan originators and underwriters on behalf of their clients that contained fraudulent personal financial statements and/or monthly bank statements. The fraudulent documentation overstated the net worth and equity injection amounts of the borrowers to falsely enhance their creditworthiness. This is a joint investigation with the FBI and the United States Postal Inspection Service.

## Disaster Loans

### *Arkansas Man Enters into \$200,000 Civil Settlement*

On March 8, 2013, an Arkansas man entered into a \$200,000 civil settlement with the U.S. government. The settlement resolves issues relating to an \$180,400 SBA disaster loan the man obtained for property damage caused by the 2008 Arkansas flooding. The investigation determined that he made false claims to the SBA by stating that the damages were to his Arkansas property when his primary residence was Illinois at the time of the disaster. The settlement stipulated that the SBA would receive \$167,680.26 for the loan balance and the US Attorney's Office would receive \$32,319.74 in civil penalties.

### **Retired Judge Pleads Guilty to Theft of Public Money**

On March 13, 2013, a retired Texas judge pled guilty to a superseding Information charging him with one count of theft of public money. The investigation disclosed the retired judge provided false statements in order to obtain a Hurricane Ike SBA disaster loan. Specifically, he made false statements about the location of his primary residence, the address for his homestead exemption, and the payment of the required personal equity injection. At the time of Hurricane Ike, his primary residence was in Conroe, Texas. However, in applications submitted to the SBA and the Federal Emergency Management Agency (FEMA), he claimed it was in Crystal Beach, Texas. The retired judge obtained a \$125,000 SBA loan to reconstruct his Crystal Beach property and approximately \$10,000 in FEMA disaster assistance for emergency housing needs. Prior to his guilty plea, the retired judge paid back the remaining \$100,000 SBA loan balance. This is a joint investigation with the DHS OIG.

### **Former Bowling Center Owner Indicted in \$1.88 Million Scheme**

On March 27, 2013, the former owner of a Texas bowling center was indicted on one count of conspiracy to commit offenses against and to defraud the United States, one count of fraud in connection with a major disaster, and six counts of false statements.

The man was approved for a \$998,500 disaster loan for Hurricane Humberto and an \$885,600 disaster loan for Hurricane Ike, which were fully disbursed for a total loan amount of \$1,884,100. The indictment alleged that he submitted inflated invoices for repair costs to the SBA in order to receive additional loan disbursements. This is a joint investigation with the FBI.

## **Government Contracting**

### **TX Man Indicted on Wire Fraud and Aggravated Identity theft**

On March 6, 2013, a Texas businessman was indicted on six counts of wire fraud and two counts of aggravated identity theft. This case was predicated on a referral from the Government Accountability Office (GAO), which alleged that man's firm was falsifying documents to establish its status as a Service-Disabled, Veteran-Owned, Small Business (SDVOSB). Specifically, the referral alleged that owner falsified the credentials of his company's engineers, as well as his company's office locations, number of employees, and past projects. The owner was awarded a Department of Veterans Affairs (VA) SDVOSB set-aside contract and ten task orders under that contract, with a cumulative value of \$1,587,952. This is a joint investigation with the VA OIG.

### **Continued Actions in \$31 Million 8(a) Scheme**

Five individuals were charged by criminal information and pled guilty in connection with fraudulently obtaining over \$31 million dollars in 8(a) and small business set-aside contracts. The investigation disclosed a scheme in which the principals of two Virginia firms falsified their eligibility for the 8(a) program. This is a joint investigation with National Aeronautics and Space Administration – OIG, the Defense Criminal Investigative Service, and the DHS – OIG. The five individuals were charged as follows:

- ◆ On March 13, 2013, the former owner of one of the Virginia firms pled guilty to one count of major fraud against the Government and one count of conspiracy to commit bribery. He also agreed to forfeit \$6.3 million in criminal proceeds. The man had also paid a DHS employee \$50,000 to help his firm obtain DHS contracts.
- ◆ On March 13, 2013, the former president of the second firm pled guilty to one count of major fraud against the Government.
- ◆ On March 14, 2013, the former vice president of the second firm pled guilty to one count of conspiracy to commit major fraud against the Government.
- ◆ On March 18, 2013, the former chief financial officer of the second firm

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*Five individuals pled guilty in connection with fraudulently obtaining over \$31 million dollars in 8(a) and small business set-aside contracts*

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pled guilty to one count of conspiracy to commit major fraud against the Government.

- ◆ On March 15, 2013, the former owner of the second firm pled guilty to one count of major fraud against the Government, and agreed to forfeit \$1.2 million in criminal proceeds.

On March 14, 2013, four individuals were charged by criminal information in connection with a major scheme in which bribe payments were made to U.S. Army Corps of Engineers (USACOE) officials in return for preferential treatment on 8(a) contracts. The charges were as follows:

- ◆ The representative of a firm was charged with bribery of a public official, conspiracy to commit bank fraud, and aiding and abetting and causing an act to be done. In addition to the bribery scheme, the man was charged for defrauding lenders by obtaining mortgage loans on properties using false loan applications, forged documents and fraudulent settlements in order to generate large cash proceeds. He pled guilty on March 29, 2013.
- ◆ An SBA certified 8(a) program participant firm was charged with conspiracy and bribery of a public official.
- ◆ The president of the 8(a) program participant firm was charged with conspiracy to commit bribery of a public official.
- ◆ The representative of a second firm was charged with conspiracy to commit wire fraud and pled guilty on March 29, 2013.

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*“four charged in connection with a major scheme in which bribe payments were made to U.S. Army Corps of Engineers (USACOE) officials in return for preferential treatment on 8(a) contracts”*

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## Agency Management

### ***Evaluation of SBA’s Progress in Reducing Improper Payments in FY 2012***

On March 14, 2013, the OIG issued [Audit Report 13-13](#), *Evaluation of SBA’s Progress in Reducing Improper Payments in FY 2012*. The objective of this audit was to determine the adequacy of SBA’s compliance with IPERA and OMB’s implementing guidance. To achieve the audit objective, the OIG determined whether the SBA addressed required provisions, and performed limited testing of compliance with these provisions. The OIG also reviewed the completeness of improper payments disclosures in the SBA’s Agency Financial Report for fiscal year (FY) 2012, and assessed the Agency’s efforts to prevent and reduce improper payments.

The OIG found that the SBA was generally compliant in meeting the minimum requirements, in accordance with OMB guidance. Further, the OIG found that the SBA’s efforts to prevent and reduce improper payments have resulted in significant progress since the FY 2011 assessment. Specifically, the Disaster Assistance Loan Program made progress through the deployment of improved controls and process improvements, which reduced their improper payments rate from 28.4 percent in FY 2011 to 17.9 percent in FY 2012. In addition, the 7(a) and 504 programs improved their testing procedures for loan guaranty approvals. The revised procedures were more robust and led to the identification of more improper payments during the testing process. As a result, the improper payments estimate increased from \$0 in FY 2011 to \$233 million and \$105 million, respectively, in FY 2012. Notwithstanding these accomplishments, further improve-

ment is still needed in the effectiveness and development of SBA improper payment controls and processes for all of the programs or activities.

The OIG also assessed whether the SBA complied with IPERA reporting requirements, as specified in OMB guidance. This evaluation found that the SBA generally met all the IPERA reporting requirements. However, the Disaster Assistance Loan program was not compliant because their improper payment rate exceeded the 10 percent threshold. In addition, three of the five programs or activities did not achieve their annual reduction targets. The OIG was unable to evaluate the accuracy and completeness of the improper payments rate reported for the Acquisition Program.

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### ***The SBA's Loan Management and Accounting System- Incremental Improvement Projects***

On March 19, 2013, the OIG issued [Audit Briefing Report 13-11: The SBA's Loan Management and Accounting System- Incremental Improvement Projects](#). This report presents the results of the OIG's review of the Small Business Administration's efforts to modernize its loan management system and migrate off the mainframe environment. Since 2004, a significant management challenge facing the SBA is the modernization of the loan accounting process. Specifically, this report addresses issues identified in the planning, management, and oversight of SBA's ongoing migration efforts.

The OIG found that the SBA successfully migrated the data-entry of over 44% of its loan and lending transactions from mainframe data entry to web-based data entry. This was the first step in fully migrating off SBA's legacy mainframe and utilizing updated technology. During the review, the OIG also found that the:

- ◆ SBA did not have an incremental improvement project to migrate its newly created COBOL code into production.
- ◆ Root Cause Analysis Project was altered from its initially approved project.
- ◆ User Interface Migration Project screens were not security tested and validated.
- ◆ Quality Assurance and Independent Verification and Validations programs did not exist.

The OIG identified five findings that put the development of this project at risk for not meeting the needs and expectations of the SBA, the Office of Management and Budget (OMB), and Congress. The OIG also issued six recommendations.

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### ***The SBA Used Inappropriate Contracting Practices to Reconfigure Space for the Office of International Trade***

On March 26, 2013, the OIG issued [Audit Report 13-12: The SBA Used Inappropriate Contracting Practices to Reconfigure Space for the Office of International Trade](#). This is the second of two audit reports related to the reconfiguration of OIT's office space. The OIG found that the Contracting Officer's Representative (COR) inappropriately authorized the use of an existing contract to complete the OIT reconfiguration, and in doing so exceeded his authority. Additionally, the COR failed to develop a Statement of Work to ensure the requested work was completed in accordance with SBA's requirements. Further, the COR and Contracting Officer (CO) did

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*"the SBA's efforts to prevent and reduce improper payments have resulted in significant progress since the FY 2011 assessment"*

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**Office of Inspector General**  
**Peggy E. Gustafson**  
**Inspector General**

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If you are aware of suspected waste, fraud, or abuse in any SBA program, please report it online at <http://www.sba.gov/office-of-inspector-general/2662>

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

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not review and approve the OIT invoice for the reconfiguration work in accordance with federal and SBA's policy.

The OIG recommended that the SBA (1) implement procedures to ensure that COs and CORs properly review invoices for compliance with the terms of the contract and the scope of work; (2) direct the CO, for purchase order SBA-HQ-11-M-0018, to review all invoices and make a determination of whether all work that was billed to the SBA was actually performed. If not, the CO should take appropriate action; (3) implement procedures to ensure the COs and CORs maintain supporting documentation of contract actions in the contract files as required by the Federal Acquisition Regulations; and (4) perform a review of the purchase order discussed in this report, focusing on the authority of the COR. If appropriate, initiate appropriate administrative action against the COR assigned to the purchase order.

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***The SBA's 417 Unauthorized Commitments Impacted Mission-Related Services and Increased Costs***

On March 28, 2013, the OIG issued [Audit Report 13-14: The SBA's 417 Unauthorized Commitments Impacted Mission-Related Services and Increased Costs](#). The audit objective was to determine the extent and reasons unauthorized commitments occurred at the SBA. The OIG determined that the SBA received invoices associated with 417 unauthorized commitments, valuing more than \$1.4 million between November 2010 and May 2012. The OIG found that the total number of unauthorized commitments at the SBA in the last two fiscal years greatly exceeded the total number of unauthorized commitments at six other federal agencies of a similar size. Further, the OIG believes that the 417 unauthorized commitments directly affected the ability of the Agency to procure goods and services for its daily operations legally and efficiently, and limited its ability to provide needed support to small businesses.

The SBA continues to improve its acquisition process and preventing unauthorized commitments. The OIG recommended seven actions to improve contract management at the SBA and significantly decrease the total number of future unauthorized commitments.

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***Briefing Report for the FY 2012 Federal Information Security Management Act Review.***

On March 29, 2013, the OIG issued [Audit Briefing Report 13-15: Briefing Report for the FY 2012 Federal Information Security Management Act Review](#). This report presents the results of the OIG's Federal Information Security Management Act (FISMA) review of the SBA. Under FISMA, agencies report their compliance with information security requirements. The OIG reports on the effectiveness of the agency's information security program in accordance with OMB criteria. For Fiscal Year (FY) 2012, the OIG was required to report on the following 11 areas: 1) continuous monitoring management; 2) configuration management; 3) identity and access management; 4) incident and response reporting; 5) risk management; 6) security training; 7) plan of actions and milestones; 8) remote access management; 9) contingency planning; 10) contractor systems, and 11) security capital planning.

The OIG found that the SBA continues to demonstrate improvement in its IT Security Program. Specifically, the SBA showed improvement in the areas of Incident Response and Risk Management, continues to meet requirements in the area of Security Capital Planning, and needs to make significant improvement in the area of Configuration Management. The OIG also recommended the SBA update its Telework SOP, which contained outdated technical procedures.