Office of Inspector General
U.S. Small Business Administration

March-April, 2012 Update

Business Loans

Guaranty Purchase Review Needs Improvement
On March 23, the OIG issued Report 12-11R, *High-Dollar Early-Defaulted Loans Require an Increased Degree of Scrutiny and Improved Quality Control at the National Guaranty Purchase Center*. This was the last in a series of reports issued that related to the OIG's audit of 25 purchased 7(a) Recovery Act loans. Overall, material deficiencies were identified in 14 of the 25 early-defaulted loans selected for review. These deficiencies resulted in questioned costs or recoverable guaranty payments totaling approximately $10.7 million. The audit found that the National Guaranty Purchase Center (NGPC) either made a purchase error or did not identify the deficiencies during its guaranty purchase reviews on six of the nine loans. This resulted in improper payments totaling approximately $3.3 million. Due to the high number of deficiencies identified and the resulting improper payments, we recommended that the SBA establish a specialized early-default purchase review unit at the NGPC.

Missouri Woman Pleads Guilty
On March 8, 2012, a Missouri woman pled guilty to a superseding information, filed on the same date, charging her with one count of making a false statement to the SBA and aiding and abetting. The woman was the registered agent for a corporation organized by her father. She had no ownership interest in, or control of the corporation; however, she obtained two SBA-guaranteed loans, totaling $350,000, for the business. In connection with her application for these SBA loans, the woman knowingly made false statements to the SBA. She purported to have never been charged, arrested, or convicted of any criminal offense, when, in fact, she had been charged with illegally signing a petition, passing a bad check, and possession of a controlled substance. This is a joint investigation with the Federal Bureau of Investigation (FBI).

Texas Sales Manager Sentenced
On March 26, 2012, a Texas sales manager was sentenced to 24 months in prison, 5 years supervised release, and restitution of $409,143. The manager had previously pled guilty to bank fraud for knowingly executing a scheme to defraud and to obtain money from a bank by means of false and fraudulent pretenses. This investigation was initiated based on a referral from the FBI and a bank. The referral alleged that the manager received loan applications from potential borrowers and then inflated the income information provided by the applicants before submitting the fraudulent loan applications to various banks. The investigation determined there were 26 loans or lines of credit where the income information provided to the banks was not the same as what the applicants provided to the manager. Of these 26, at least 14 were delinquent or defaulted, with a cumulative outstanding balance of $530,512. The SBA guaranteed five of the 14 delinquent loans or lines of credit.

Former Utah Mortgage Loan Officer Pleads Guilty
On April 4, 2012, a business owner and former mortgage loan officer pled guilty to one count of money laundering. The investigation disclosed that he and his business partner recruited "straw borrowers" and used the borrowers' names and good credit to obtain, fraudulently, $335,000 in loans. The pair caused the straw borrowers, on the promise of future rewards, to submit documents indicating they owned thriving businesses, when, in fact, the majority of the businesses only existed on paper. Both subjects fraudulently obtained a total of four SBA loans and two regular bank loans. This case was initiated based on a referral from the SBA Utah District Office. This is a joint investigation with the Internal Revenue Service, Criminal Investigations (IRS CI).

Former President of Michigan Firm Found Guilty
On April 9, 2012, the president of a real estate investment firm was found guilty in a bench trial in Wayne County Circuit Court, Detroit, Michigan. Pursuant to a criminal information filed on September 9, 2011, the subject was found guilty of multiple felony counts, including seven counts of false pretenses with intent to defraud. These convictions resulted from his participation in multiple fraud schemes, including two loan-fraud schemes against the SBA. The first loan-fraud scheme involved a $98,000 SBA-guaranteed loan to a company purportedly owned by the subject's wife. The investigation, however, corroborated state corporate records showing that he was the true owner of the company. The second loan-fraud scheme involved a $100,000 SBA-guaranteed loan made to his business. The investigation revealed that the subject overstated the company's annual revenues as $890,000, when the actual revenues were only $35,240. In addition, proceeds from both SBA loans were processed, laundered, and diverted into his personal bank accounts instead of being used as

working capital for the respective businesses. At the trial, the subject was also convicted for his involvement in a residential property “flipping” scheme, a Housing and Urban Development (HUD) rent-subsidy scheme, and a vehicle code violation. This was a joint investigation with the Michigan State Police, the U.S. Secret Service (USSS), and the Wayne County Prosecutor’s Office.

Maine Business Owner Sentenced

On April 18, 2012, a Maine business owner was sentenced to 24 months incarceration, one year supervised release, and a $100 special assessment fee. The sentence is the result of a conviction on one count of false statements. When the subject applied for a $1.3 million SBA-guaranteed loan, he submitted an SBA Form 912, Personal History Form, indicating that he had no prior criminal convictions. In fact, he had been convicted of criminal violations on four previous occasions. This case was referred to the OIG by the U.S. Attorney’s Office, Portland, Maine, when, in the course of a health care fraud investigation, it was discovered that the subject had made false statements to the SBA. He was ordered to serve this sentence concurrently with the 30-month prison term resulting from his health care fraud conviction. The SBA loan was paid in full; therefore, no restitution was ordered. This is a joint investigation with the FBI.

Louisiana Man Pleads Guilty

On April 25, 2012, a Louisiana man plead guilty to five counts of wire fraud, one count of making false statements to a financial institution, and one count of making a false tax return. The subject and another individual applied for a $916,000 SBA-guaranteed loan to finance the purchase of a business. The investigation revealed that he constructed a fraudulent commission agreement used at loan closing, which circumvented the equity injection requirement. This is a joint investigation with the FBI, the Louisiana State Attorney General’s Office (LSAGO), and IRS CI.

Plea and Judgments Unsealed in California

On April 23, 2012, the OIG confirmed that plea agreements for one individual and two corporations, and judgments for the individual and one corporation had been unsealed. The individual pled guilty to one count of conspiracy to make false statements to influence banks. One corporation pled guilty to one count of money laundering, and one count of aiding and abetting. The second corporation pled guilty to one count of conspiracy to make false statements to influence banks. The primary subject, an authorized representative of the companies who had previously pled guilty, entered the plea agreements for the two companies. The primary subject, along with his wife, owned or controlled about 60 convenience stores in northern California. They used straw borrowers to obtain SBA-guaranteed loans, which allowed them and their associates to hide their financial interests in the individual businesses, conceal the true sources of cash injections for the loans, and launder the proceeds of the loans. This is a joint investigation with the FBI; IRS CI; Department of Homeland Security, Immigration and Customs Enforcement; the U.S. Department of Agriculture (USDA) OIG , and the California Department of Alcoholic Beverage Control.

Disaster Loans

Texas Man Indicted on Five Counts of Forgery

On March 28, 2012, a Texas man was indicted on five counts of forgery of contracts, deeds, or powers of attorney. The indictment alleges that he forged signatures of his estranged wife and others on SBA loan documents in order to obtain two SBA disaster loans in connection with Hurricane Katrina. The SBA approved a $95,600 home loan to repair his alleged residence and a $71,800 business loan to repair the other half of the same duplex, which he claimed as a rental property. He then used the loan proceeds for personal living expenses (i.e. hotel rooms, dining, a vehicle purchase, and gas). None of the money was used to repair the real property, which actually belonged to his estranged wife. The SBA suffered a loss of approximately $54,000.

Government Contracting & Business Development

Illinois Couple and their Business Sentenced

On March 7, 2012, an Illinois couple and their business were sentenced as a result of their guilty pleas to conspiracy to commit wire fraud. The husband, a former associate director of a U.S. Department of Veterans Affairs (VA), Consolidated Mail Outpatient Pharmacy (CMOP), was sentenced to 60 months in prison. The wife was sentenced to 24 months probation; and the couple and their company were ordered to pay $400,000 in restitution, jointly and severally. The couple created their business in order to provide temporary pharmacists, fraudulently, to the CMOP where the husband worked. The business later sought SBA certification as a woman-owned, minority-owned small disadvantaged business and SBA 8(a) Program participant. As part of the conspiracy, the couple agreed to allow another company to fraudulently masquerade as their business to qualify for contracts set aside for SBA 8(a) participants. In addition, the husband claimed that the business was managed solely by his wife in order to avoid conflict of interest laws governing federal employees. During the course of the scheme, the husband, working with others, secretly agreed that the billing rates charged to the VA should increase for certain pharmacists their company provided. Between 2000 and 2007, the couple and other unindicted co-conspirators used the company to bill the VA for more than $8 million in services. This is a joint investigation with the U.S. Department of Justice, Antitrust

Division and the VA OIG, with assistance from the Defense Criminal Investigative Service (DCIS) and the USSS.

D.C. Company Owner Charged with Conspiracy

On March 12, 2012, a construction company owner was charged by criminal information with conspiracy to commit money laundering and criminal forfeiture. The charges allege that he conspired to conduct financial transactions to conceal the proceeds of a bribery scheme from authorities and to use such proceeds to obtain real property, vehicles, and luxury items for his personal benefit. The owner allegedly caused his company to submit fictitious purchase orders and invoices to a prime contractor to obtain payments from the U.S. Army Corps of Engineers for government contracts. This is a joint investigation with the FBI; the IRS CI; the Army CID, and DCIS.

Director of Contracts Pleads Guilty to Bribery in D.C.

On March 13, 2012, the director of contracts for a technology firm pled guilty to one count of bribery and one count of unlawful kickbacks. Additionally, the director agreed to the forfeiture of money to the United States for $689,342. The investigation revealed that the director gave, offered, and promised over $7 million, directly and indirectly, to a public official, in return for the official's approval of U.S. Army Corps of Engineers contracts and subcontracts. Additionally, the director, a prime contractor employee, solicited, accepted, and attempted to accept kickbacks in excess of $1 million from subcontractors in exchange for awarding contracts and providing favorable treatment. This is a joint investigation with the FBI, IRS CI, Army CID, and DCIS.

Two More Indicted for Bribery Scheme in D.C.

During the month of April, two additional subjects were indicted for their alleged participation the previously described scheme involving more than $20 million in bribe and kickback payments. On April 18, 2012, the owner of a home building company was charged with one count of conspiracy to commit interstate transportation of stolen money and one count of criminal forfeiture. On April 20, 2012, in the same court, the president of another firm was charged with bribery of a public official and aiding and abetting and causing an act to be done. The charges relate to allegations that these men and others were involved in a multi-million dollar bribery and kickback scheme, in which payments were made to U.S. Army Corps of Engineers officials in return for preferential treatment on 8(a) contracts. This is a joint investigation with the FBI, IRS CI, Army CID, and DCIS.

Veterans Affairs Project Director Pleads Guilty

On March 15, 2012, a Missouri man pled guilty in U.S. District Court, Eastern District of Missouri, to a criminal information filed on the same day. The information charged that the man with acceptance of gratuities to influence decisions in an official capacity as a federal employee. The subject, while serving as a director of projects for the VA Medical Center in St. Louis, accepted illegal gratuities in the form of tickets to sporting events, meals and entertainment, and interest-free loans from the owners of a contracting firm among others, in exchange for steering work to the contracting firm. The contracting firm was awarded $3.4 million in government 8(a) set-aside contracts from January 2007 to late 2010, the time during which he recommended the company to personnel at the VA. This is a joint investigation with the GSA OIG and VA OIG.

Two Boise Firms Plead Guilty to HubZone Fraud

Two Boise companies pled guilty to fraud relating to the HUBZone program. On March 15, 2012, the president of a roofing company pled guilty on behalf of his company, to one count of wire fraud. On March 28, 2012, the president of a construction company pled guilty on behalf of the construction firm, to one count of wire fraud and one count of false statements pertaining to the GSA's Surplus Property Program through which SBA 8(a) companies can obtain surplus property. Both companies submitted fraudulent HUBZone applications to the SBA that stated their principal places of business were located in HUBZones and that each had two employees who resided in HUBZones.
The investigation revealed that neither of the companies was located in a HUBZone and none of the employees resided in a HUBZone. The companies received a combined total of over $1.6 million in contracts based on the false HUBZone certifications. The investigation also found that one of the firms obtained property as an SBA certified 8(a) company under the GSA's Surplus Property Program and immediately sold or transferred that property to a non-8(a) entity. This is a joint investigation with the IRS CI, VA OIG, GSA OIG, USDA OIG, Department of Interior OIG, Air Force Office of Special Investigations, Army CID, and DCIS.

Alabama Man Sentenced on Misrepresentation Charges

On April 4, 2012, an Alabama man was sentenced to 12 months and one day imprisonment, 12 months of supervised release, and restitution of $130,000. He previously pled guilty to two counts of misrepresentation after the investigation disclosed that he falsely obtained HUBZone certification for his business. Specifically, it was determined that his firm's principal office was not located within a HUBZone, and 35 percent of its employees did not reside within a HUBZone, as required by program regulations. As a result, his firm was awarded 28 federal contracts from 2006 to 2009, valued at $2,565,692, which it would not have been eligible to receive without HUBZone status. This is a joint investigation with the Army CID and DCIS.

Kansas Construction Company Owner Pleads Guilty

On April 9, 2012, the owner of a construction company pled guilty to single counts of conspiracy, major program fraud, wire fraud, money laundering, and false statements.

In addition, he agreed to the imposition of a forfeiture judgment against him for $6,836,277.94. The investigation revealed that the subject and his company fraudulently claimed Service-Disabled, Veteran-Owned (SDVO) small business status to obtain 11 federal government contracts valued at $6,836,277.94, which his company would not otherwise be entitled to receive. He also admitted providing the VA contracting officer a fraudulent resume in which he claimed to have served three tours in Southeast Asia as a highly decorated officer in the U.S. Army. Government records show that subject never left the state of Missouri during his service in the Army and Missouri National Guard. This is a joint investigation with the GSA OIG, the Department of VA OIG, and DCIS.

Construction Management Firm Owner Pleads Guilty

On April 18, 2012, the owner of a construction management firm pled guilty to one-count information charging him with conspiracy to commit money laundering. Additionally, the owner agreed to a money judgment in favor of the United States of $4,055,063. The investigation revealed a conspiracy to launder proceeds of a bribery scheme and to use the proceeds to obtain real property, vehicles, and luxury personal goods for personal benefit. The subject and others caused his firm to submit fictitious purchase orders and invoices to a prime contractor, in order to obtain payments from the U.S. Army Corps of Engineers for government contracts. This is a joint investigation with the FBI, IRS CI, Army CID, and DCIS.

Agency Management

Annual Review of the SBA's Accounting of Drug Control Funds

On March 1, 2012, the OIG issued Report 12-9 *Independent Review of the SBAs Accounting of FY 2011Drug Control Funds and Performance Summary*. As directed by the Office of National Drug Control Policy (ONDCP) Circular, *Drug Control Accounting*, agencies are required annually to provide a detailed accounting of all funds expended on National Drug Control Program activities and the results associated with those activities. Nothing came to our attention that caused us to believe that the SBA's alternative report for the year ended September 30, 2011 is not presented, in all material respects, in conformity with ONDCP's Circular, or that management's assertions are not fairly stated, in all material respects, based on the criteria set forth in ONDCP's Circular, *Drug Control Accounting.*

Contracting Activities not Complying with IPERA

On March 8, 2012, the OIG issued Advisory Memorandum 12-7, *The SBA's Improper Payment Review and Reporting for its Contracting Activities did not comply with IPERA and IPIA Requirements during FY 2011*. This memorandum addressed significant issues related to the agency's contracting activities that the OIG identified during its review, the *Small Business Administration's* (SBA) *Compliance with the Improper Payments Elimination and Recovery Act of 2010* (IPERA). During the IPERA review, the OIG determined that the SBA did not comply with IPERA and Improper Payments Information Act (IPIA) requirements, particularly, the SBA's planning, execution, and reporting of the improper payments for its contracting activities during Fiscal Year (FY) 2011.

The OIG found that the: (1) personnel responsible for developing the test plan and performing the improper payments review did not have training in contracting practices; (2) test plan was inadequate to detect improper payments;(3) IPERA review did not capture significant payment errors; (4) publishing of an 89 percent improper payment rate was incomplete; (5) improper payment rate was not reported in accordance with the Office of Management and Budget (OMB) guidance; and (6) SBA management did not develop or publish a *Corrective Action Plan* and a *Payment Recapture Audit Plan*.
Without addressing the root cause(s) of its improper payments, the agency remains at significant risk for future improper payments. The OIG made five recommendations.

SBA Generally Meets IPERA Reporting Guidance but Immediate Attention Is Needed to Prevent and Reduce Improper Payments

On March 15, 2012, the OIG issued Report 12-10, *SBA Generally Meets IPERA Reporting Guidance but Immediate Attention Is Needed to prevent and Reduce Improper Payments.* The purpose of this review was to address the adequacy of SBA's compliance with IPERA and OMB's implementing guidance. The OIG assessed whether the SBA addressed required provisions and performed limited testing of compliance with these provisions. We also reviewed the completeness of improper payments disclosures in the SBA's Agency Financial Report for FY 2011, and assessed the Agency's efforts to prevent and reduce improper payments. The OIG found that the SBA was generally compliant in meeting the minimal reporting requirements for IPERA in its FY 2011 AFR. The OIG's qualitative review of the Agency's efforts to prevent and reduce improper payments demonstrated that immediate management attention is needed in four of the six programs or activities to improve the accuracy and completeness of reporting; sufficiency of improper payments recapturing activities; and the quality of corrective action plans.

Issue in State Trade and Export Promotion Program

On March 30, the OIG issued Advisory Memorandum 12-12, *The SBA's Office of International Trade Inappropriately Awarded a One Million Dollar State Trade and Export Promotion (STEP) Program Grant to an Ineligible Recipient*. This memorandum presented an issue that the OIG identified during its ongoing *Audit of the Small*

Business Administration's (SBA's) State Trade and Export Promotion (STEP) Grant Program. The OIG's review determined that the Office of International Trade awarded a STEP program grant, valued at $1,022,781, to the Commonwealth of the Northern Mariana Islands, even though the Commonwealth was not identified in the authorizing statute as eligible to receive the grant. This resulted in eligible grant recipients receiving a lesser portion of the available $30 million for the FY 2011 STEP grant program. The OIG recommended that the SBA immediately terminate the grant before any grant money was disbursed, that fund disbursements be withheld, and that all previously disbursed funds be recovered. Additionally, the OIG recommended that the SBA redistribute the funds to other qualified STEP grant recipients or return the funds to the U.S. Department of the Treasury, and take precautions to ensure that an ineligible recipient does not receive a STEP grant in subsequent years. The SBA terminated the grant.

Cash Gifts Review

On March 30, 2012, the OIG issued Report 12-13, *Review of the SBA's Fiscal Year 2011 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 2011.

The OIG determined that the SBA obtained proper approvals to solicit and accept gifts to use for the payment of travel and per diem costs for the SBA's Start-up America events in 2011. The SBA recorded the cash donations in the BAT Fund and timely made the funds available to the Office of the Administrator for expenditure. In addition, the Massachusetts District Office used its prior year BAT Funds to pay for a Jobs Act "Listening Tour" event.

The OIG noted, however, that the SBA recorded the wrong accounting code in its accounting system. Consequently, guest speakers and participants' travel moreover, per diem expenses for the Start-Up America events, totaling $5,680.51, were reimbursed out of the SBA's salaries and expenses appropriation instead of the BAT Fund. While $5,680.81 of the original $10,000 gift should have been used to pay these travel expenses, the OIG noted that the SBA did not follow-up with Business Forward regarding the disposition of the unused $4,319.49. The OIG also found that the SBA did not have permanent procedures in place on gift acceptance since 2007, and recommended that the agency issue such procedures.

Peggy E. Gustafson, Inspector General

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

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:

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

Many OIG reports can be found on the OIG's website http://www.sba.gov/office-of-inspector-general