

**SEMIANNUAL REPORT OF THE INSPECTOR
GENERAL**

FOR THE PERIOD

April 1, 1996, To September 30, 1996

PREFACE

Pursuant to Public Law 95-452, the Office of Inspector General (OIG) is required to prepare a Semiannual Report of its activities for the Congress of the United States. This Semiannual Report, transmitted to the Congress by the Administrator of the Small Business Administration (SBA), covers the full range of OIG activities from April 1, 1996, to September 30, 1996.

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Executive Summary

This report on the activities of the Office of Inspector General (OIG) of the Small Business Administration (SBA) is submitted pursuant to Section 5(b) of P.L. 95-452, the Inspector General Act of 1978, as amended. It summarizes OIG activities for the 6-month period from April 1, 1996, to September 30, 1996.

Summary of Accomplishments

OIG audits, inspections, and investigations over the last 6 months achieved \$15,133,398 in potential dollar results, 36 indictments, and 44 convictions. The dollar results consist of (1) \$2,041,896 in potential recoveries, including judicially-awarded fines and restitution; (2) \$10,857,466 in management avoidances; (3) \$1,313,113 in disallowed costs agreed to by SBA's management; and (4) \$1,437,923 in management commitments to use funds more efficiently. This brings the OIG's FY 1996 accomplishments to almost \$70 million.

The OIG alone could not have achieved the accomplishments set forth in this report to the Congress. The results for this reporting period reflect the cooperation and support of other Federal audit, inspection, and investigative organizations such as the Federal Bureau of Investigation (FBI); U.S. Secret Service; Bureau of Alcohol, Tobacco and Firearms (BATF); Internal Revenue

Service (IRS); Air Force Office of Special Investigations; Federal Protective Service; other Federal OIGs; Department of Justice (DOJ) prosecutors; and, most importantly, the actions of SBA program managers and employees. Indeed, much of our success is due to referrals made by conscientious SBA employees.

OIG Mission for FY 1997

In FY 1997, the OIG will continue to focus its attention on SBA's two largest programs--Business Loans and Disaster Assistance. The continuing growth of these two programs, as discussed throughout this report, has been substantial over the last several years. While the number of dollars at risk in these two programs continues to grow, both the Agency and the OIG have undergone reductions in resources for their respective management and oversight activities. The Agency's total portfolio, which includes its loan and disaster programs, now exceeds \$35.3 billion. This represents a 7 percent growth over last

year's portfolio of \$32.8 billion. The burgeoning size of the oversight universe is clearly outpacing the OIG's ability to provide responsible levels of monitoring, and this is a major concern of the Inspector General.

Using \$3 million made available to the OIG by the President and the Congress in FY 1994 for the purpose of disaster-related oversight, the OIG subsequently developed a strategy to guide disaster-related oversight activity and to make optimal use of these funds. Increased temporary staffing, located near disaster sites, now provides needed personnel to meet the oversight goals of the OIG's disaster plan. The Congress again demonstrated its concern in the FY 1997 budget by appropriating an additional \$500,000 to the OIG for its the disaster-oversight effort.

The OIG continues to build greater awareness of its mission with SBA employees, program participants, and the Agency's resource partners. We believe the OIG's information dissemination activities are deterring some level of fraud, but equally important, these activities are also raising SBA program managers' interest in management and systems improvement. The office continues to pursue this dual goal through attendance at SBA-sponsored events, the development and use of educational presentations, more creative use of key OIG reports and activities, and staff involvement in other initiatives designed to make the OIG more visible within the Agency and its client groups. One such example is the OIG's use of IGnet, an Internet-based forum for the inspector general community and the public at large.

Summaries of OIG audit and inspection reports are being made available over IGnet, a communications system coordinated for the federal inspector general community by the SBA/OIG. **IGnet can be reached through the Internet at <http://www.sbaonline.sba.gov/ignet>.** These are relatively economical methods of reporting our work, and they are having a substantial impact on the accomplishment of our mission goals. The OIG is also becoming progressively more visible to SBA's resource partners through attendance of key OIG officials at the National Association of Guaranteed Government Lenders (NAGGL) conference, active leadership and participation in the activities of the National Intergovernmental Audit Forum, and professional presentations at the annual meeting of the American Institute of Certified Public Accountants and other professional and trade organizations. The OIG's visibility is also enhanced through the Inspector General's (IG) leadership role in the President's Council on Integrity and Efficiency (PCIE).

Highlights of the Past Six Months

Efforts to Improve SBA Program Management

Annual Audit of SBA's Financial Statements Yields Qualified Opinion.

Three material weaknesses caused a qualified opinion to be issued for the FY 1995 independent audit of SBA's financial statements, required by the Chief Financial Officers Act of 1990. SBA did not (1) maintain comprehensive inventory records of acquired property, (2) consistently value

the acquired property at its net realizable value, and (3) reconcile certain fund balances with the U.S. Department of Treasury. The first two exceptions were repeated from the 1994 audit. Because of the lack of an automated inventory system with unit detail, SBA cannot reconcile the estimated \$140 million of collateral purchased property to its general ledger. The SBA's CFO has indicated, however, that field office records fully document this general ledger balance. The fund balance problem refers to loan accounting balances, which were reported to be \$32 million higher on SBA's books than on those of the Department of Treasury. The CFO has been reconciling these balances over the past year, working with the audit staff. The FY 1996 audit is underway, and the CFO has been correcting the problems reported in previous years working toward an unqualified opinion for FY 1996.

Two Audits Call for Procedural Changes To Prevent Abuse in the Section 8(a) Program. One OIG audit report addressed a procurement method called basic ordering agreements (BOA). Such agreements can result in unlimited sole source awards to single companies, thereby undermining statutory competitive thresholds. The OIG auditors recommended (1) limiting the dollar amount of sole source BOA delivery orders to regulatory competitive thresholds, i.e., \$5 million for manufacturing and \$3 million for other SIC codes; and (2) limiting Standard Industrial Classification (SIC) codes in a BOA to one major group.

A second audit report called for SBA to require firms to be established wholesalers or retailers in the products they sell to the

Government. Section 8(a) contractors would also have to supply the products of a small business, if available. These requirements would aid the firms in developing their businesses while reducing the pass-through of contracts to large businesses.

OIG Audits SBA's New Low Documentation (LowDoc) Loan Program.

An audit of the LowDoc program found that, as of July 1996, only 2 of 70 loans examined were past due or in liquidation, indicating a relatively low failure rate due to LowDoc credit procedures. The audit did, however, find that 5 loans out of the sample of 70 were approved for borrowers with questionable repayment ability and 2 were approved for ineligible borrowers. The auditors also found that 54 loans, including 6 of the 7 with approval errors, had at least one other processing or disbursement deficiency compared to Section 7(a) loan program guidelines.

Inspector General Community Supports OIG Involvement in the GPRA Process.

Under the auspices of the President's Council on Integrity and Efficiency (PCIE), the SBA and Treasury Department Inspectors General recently directed a survey of all IGs. The survey's goals were to determine current and planned OIG involvement in the implementation of the Government Performance and Results Act (GPRA) within host agencies and to solicit IG perceptions as to the appropriate role of the IGs in that process. The majority of IG respondents believed OIGs should act in an advisory/consultative capacity in the Act's implementation stages, but they should also perform independent audits and reviews of results once the host department or Agency

has had an opportunity to implement both its strategic and performance plans.

SBA Should Discontinue Using the Section 7(a) Loan Program Commercial Loss Rate. An OIG inspection report, requested by the SBA Administrator, found that the methodology for determining the Section 7(a) general business loan program's commercial loss rate is valid. The rate is not, however, comparable with banking industry loss rates because of significant differences in the loan portfolios. SBA's loan-making objectives also vary considerably from those of the for-profit banking industry, and differing charge-off policies affect the timing of charge-offs and, therefore, loss rates. The commercial loss rate is further misleading as an indicator of the Agency's Section 7(a) loan program performance because of the rapidly expanding portfolio and the 3-to-4 year lag between loan disbursements and charge-offs. For these reasons, the IG recommended that SBA discontinue using the Section 7(a) commercial loss rate to compare Section 7(a) program performance with that of the banking industry.

Activities to Enhance Fraud Detection and Deterrence

California Loan Broker and Nine Others Charged With Making False Statements. A loan broker from La Canada, California, and nine other southern Californians involved with SBA-guaranteed business loans he brokered, were charged with making false statements. The broker and seven of the nine others have pled guilty.

The loan broker pled guilty to five counts of

making false statements in a loan application to a Federally-insured financial institution. He also pled guilty to a **criminal forfeiture** count allowing the Government to recapture the illegal proceeds of his crimes. Between 1987 and 1992, the man brokered more than two dozen fraudulent loans totaling more than \$9 million. His scheme involved the submission of falsified financial information, including Federal tax returns, financial statements, invoices, etc., to induce the banks and SBA to grant the loans. When the banks and SBA approved the loan applications, the broker would launder part of the proceeds through a business which he fraudulently represented had sold equipment to various applicants.

Results of False Tax Return Cases Increase. Over the last 6 years, the OIG has received 284 allegations that false tax returns were submitted in support of SBA business or disaster loan applications. These fraud referrals now involve loan applications submitted to 44 SBA district offices, totaling \$115 million and involving 1,039 individual subjects. To date, 82 individuals have been **indicted on criminal charges:** 72 have been **adjudicated guilty**, 2 indictments were dismissed, and 8 others have not yet gone to trial.

Affirmative Civil Enforcement Program. The OIG continues to expand the scope of its efforts to make optimal use of the Department of Justice's Affirmative Civil Enforcement (ACE) program. This U.S. Attorney program targets cases which might not be prosecuted criminally because of the minimal dollar amounts involved, absence of financial loss to the Government, or because

other facts of the case might not support a criminal prosecution. Heretofore, our success with the ACE program was focused in only ten states; however, during this reporting period, the OIG realized its first ACE results in Iowa, Kansas, and Utah.

During the approximately 39 months the OIG has been involved with the ACE program, we have had a total of **52 successful cases**, resulting in **\$2,372,917 in civil penalties** and **\$1,656,218 in recoveries** by SBA. Individual ACE outcomes are reported in the program area chapters, as appropriate.

Business Loan Program

SBA's small business loan programs serve one of the most important missions of the Agency: to ensure that Federal funds and resources are used to help finance qualified small enterprises. Under the **Section 7(a) Guaranteed Loan Program**, SBA guarantees loans to small businesses that are unable to obtain private financing. These loans must be of such merit, or be so secured, as to reasonably ensure repayment to the lending institution. No loan may be made unless the financial assistance is not otherwise available on reasonable terms from elsewhere in the credit market. Under the guarantee plan, SBA agrees to purchase the guaranteed portion of the loan upon default by the small business. SBA's guarantee share of loans by private lenders averages about 77 percent.

More than 8,000 lenders have made at least one Section 7(a) loan in the past 5 years. Currently, approximately 38 percent of these loans are being made by participants in the Agency's **Certified Lender Program (CLP)** or its **Preferred Lender Program (PLP)**.

Lenders who are heavily involved in the SBA guarantee program and meet the Agency's criteria can participate through the **CLP**. Over 900 participating lenders, approved for the **CLP** program, are permitted to assume greater authorities and responsibilities in processing, closing, servicing, and liquidating loans. As a result, SBA can process loan guarantee applications in 3 days, rather than the 2 weeks that it may take for a thorough analysis by Agency staff. About 9 percent of all business loan guarantees are made through the **CLP** process.

As permitted by Section 7(a)(2) of the Small Business Act, SBA delegates even wider authority to preferred lenders, i.e., lenders who can commit the Agency to guarantee eligible business loans and decide the level of SBA participation. This program, with over 350 participants, reduces processing time on strong credit applications and uses the resources of SBA's best lenders to the maximum. About 29 percent of all business loan guarantees are made through the **PLP** process.

The **504 Loan Program** provides long-term, fixed-rate financing through certified development companies (CDCs) to small businesses to acquire real estate, machinery, and equipment for expansion of business or modernizing facilities. Typically, 504 loan proceeds

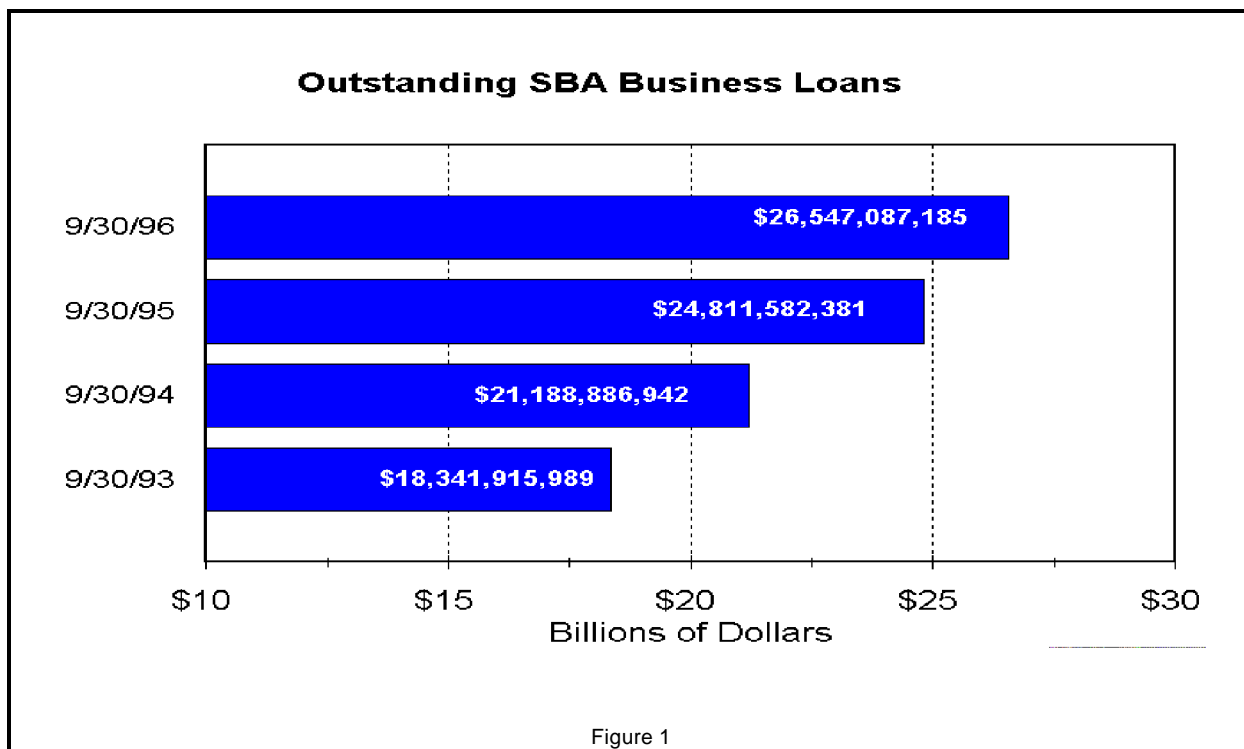
are provided as follows: 50 percent by an unguaranteed first mortgage bank loan, 40 percent by an SBA-guaranteed debenture, and 10 percent by the small business customer. The maximum SBA debenture is \$1 million.

With the creation of the Agency's Low Documentation (**LowDoc**) application process, lenders are now able to use their own internal loan application documents, plus a single, two-sided SBA form to apply for an SBA guarantee on a loan of \$100,000 or less. The demand for this program is unprecedented; **36 percent of all SBA loan guarantee applications are now submitted through the LowDoc application process.**

Summary of OIG Activity

The following summarizes OIG activities relating to SBA's business loan programs over the reporting period:

- Three audit reports were issued and eight audits were underway.
- One inspection report was issued and two others were underway.
- Business loan investigations resulted in 29 indictments and 29 convictions, not necessarily the same cases, however.
- Business loan investigations produced \$395,427 in court-ordered restitution, \$500,000 in other recoveries by SBA, \$986,797 in reductions to the Agency's financial risk, and \$52,540 in civil penalties and fines.
- Office of Security Operations name check activity resulted in the declination of 37 business loans, totaling \$7,826,617.
- Twenty-six business loan investigations were closed, leaving an inventory of 153 active cases involving 730 subjects. Due to other workload demands, another 12 business loan cases were referred to another law enforcement agency for investigation, giving the OIG a total of 78 business loan referrals to monitor.
- One proposed piece of legislation and one Standard Operating Procedure were reviewed.



Efforts to Improve SBA Program Management

SBA's 7(a) Loan Program Loss Rate Methodology Deemed Valid, But Rate Not Comparable to Banking Industry Loss Rates

The Office of Inspector General (OIG) issued an inspection report requested by the SBA Administrator on the Agency's 7(a) loan program loss rate. The report focuses on the methodology used to compute the commercial loss rate for the 7(a) general business loan program and on the use of this rate by Small Business Administration (SBA) officials.

While there are minor differences in how the SBA and the banking industry compute the

commercial, or one-year, loss rate, the OIG found that the methodology used by SBA to calculate the rate is fundamentally valid and consistent with that used by the banking industry. **The OIG also found, however, that SBA's commercial loss rate is not comparable with banking industry's loss rates** because of the significant differences in their loan portfolios--SBA's portfolio includes only small businesses, whereas the industry rate reflects losses on loans to businesses of all sizes; SBA's loans are concentrated primarily in retail trade and services, while private lender loans cut across all industrial sectors; and SBA's portfolio includes real estate loans, which are excluded from the industry loss rates. SBA's loan-making objectives also vary considerably from those of the for-profit banking industry, and differing charge-off policies affect the timing of charge-offs and,

therefore, the loss rates. Finally, the commercial loss rate is misleading as an indicator of current 7(a) loan program performance because of the rapidly expanding portfolio and the 3-to-4 year lag between loan disbursements and charge-offs. It should also be noted that SBA program officials do not use the commercial loss rate for internal management purposes; instead, they focus on cohort performance and other indicators such as purchase, currency, and subsidy rates. These indicators appear to be more useful measures of loan performance.

For these reasons, the Inspector General recommended that SBA discontinue the use of the commercial loss rate for the 7(a) general business loan program. While conceding the validity of the report's arguments, SBA officials believe that the Agency should continue using the commercial loss rate. They assert that it is useful for comparisons with the commercial lending industry because the methodology is similar and the rate is easily understood--whereas the subsidy rate and its derivatives are not.

The inspection also found that loss and default rates are sometimes used interchangeably and not always properly identified, providing the potential for an inadvertent misrepresentation of 7(a) loan program performance. The inspectors recommended that information on loss and default rates be more clearly defined and labeled. Because of changes resulting from credit reform, the OIG also recommended that the Office of the Chief Financial Officer (OCFO) determine whether revisions can be made in the format of the

Agency's Annual Loss Study. The OCFO is addressing these issues.

OIG Conducts Audit of SBA's LowDoc Loan Program

An audit of SBA's Low Documentation Loan Program (LowDoc)¹ found that 5 loans out of an audit sample of 70 were approved for borrowers with questionable repayment ability and 2 were approved for ineligible borrowers. As of July 1996, only 2 of the 70 loans were past due or in liquidation, indicating a relatively low failure rate due to LowDoc credit procedures. The auditors also found that 54 loans, including 6 of the 7 with approval errors, had at least one other processing or disbursement deficiency compared to Section 7(a) loan program guidelines. **The most prevalent deficiencies involved inadequate verification of equity injections, use of proceeds, and Federal tax returns.**

The auditors examined a random sample of 70 loans totaling \$3.7 million out of the 27,045 loans totaling \$1.5 billion approved from inception of LowDoc in December 1993 until May 1995. Based on a statistical projection of the sample results, it was estimated that loans totaling \$115.9 million

¹ LowDoc is a new 7(a) loan program that minimizes paperwork for loans under \$100,000. After a pilot phase in Texas, the program was expanded nationwide in June 1994. For loans of less than \$50,000, participating lenders need send only an application form to SBA for approval. For loans from \$50,000 to \$100,000, lenders provide SBA with business tax returns, financial statements, and a credit analysis. SBA guarantees 80 percent of approved LowDoc loans. Banks are expected to apply credit criteria in the same manner as they would for their own non-guaranteed loans.

were approved for borrowers who had questionable repayment ability, and loans totaling \$34.8 million were approved for borrowers not meeting eligibility requirements. Limited SBA guidance at the start of the LowDoc program and limited monitoring of both lenders and District Offices may have caused the processing deficiencies. LowDoc procedures were clarified in April 1996 after 11 months of operation. The audit report recommended that the Associate Administrator for Financial Assistance (AA/FA) develop performance standards for LowDoc loans and conduct periodic reviews to identify unacceptable performance by either lenders or District Offices. The report also recommended that the SBA guarantee be denied or withdrawn for five specific loans cited in the audit and whenever there are significant lender deficiencies. It further recommended that SBA establish criteria for evaluating other sources of income that are used to supplement an applicant's repayment ability. The AA/FA agreed with the findings and recommendations.

Houston Management Consultant Secretly Reorganizes, Defaults on Loan, and Improperly Causes \$117,518 SBA Writeoff

Shortly after obtaining a \$200,000 Section 7(a) loan, a management consulting firm in Houston, Texas, **reorganized and transferred its assets to Dallas without SBA's knowledge or consent.** When the loan later defaulted, SBA thought the borrower had gone out of business and, consequently, charged off \$117,518 in a negotiated settlement of the loan balance. SBA's Management and Technical

Assistance Program, unaware of the 7(a) loan default, awarded a \$353,000 contract to the Dallas firm a year later. SBA's Houston District Office agreed with the audit recommendation that SBA withdraw the settlement agreement and pursue collection of the amount that had been written off. This audit was one of a series of reviews of early defaulting loans. An overall report on the audits' systemic findings will be issued at a later date.

New York Small Business Lending Company Sustains Losses Attributable to Procedural Weaknesses

An OIG audit found that a **Small Business Lending Company (SBLC) needed significantly improved procedures in loan origination and servicing, monitoring delinquent debt, and internal controls.** At the request of the responsible SBA program office, the OIG audited the New York City SBLC licensed by SBA because one-third of its loan guarantees had been repurchased between 1986 and 1995. A review of 18 repurchased loans identified \$627,039 in recoverable losses to SBA. The losses involved loan origination and servicing errors including: (1) failure to secure collateral, (2) disbursement of loan proceeds for inventory already purchased, and (3) acceptance of low real estate appraisals. The audit also indicated that the SBLC charged borrowers inappropriate fees for application processing and for lender overhead costs (such as photocopying and office supplies).

The Associate Administrator for Financial Assistance (AA/FA) concurred in the audit findings and took corrective actions. The officials for the SBLC generally agreed with

the findings, except for the finding that fees charged to borrowers were inappropriate. The SBLC also asserted that it should not be held accountable for actions prior to 1991, when the present ownership was established. The AA/FA disagreed with the SBLC's position on these two points.

Program Vulnerability Memorandum Issued on Undisclosed Criminal Histories of Loan Applicants

During the reporting period, the OIG issued a program vulnerability memorandum (PVM) to the acting Associate Deputy Administrator for Economic Development (ADA/ED). The PVM cited the results of a recent OIG investigative project, conducted jointly with the U.S. Secret Service, to determine what percentage of borrowers within a sample concealed information regarding their criminal histories when applying for Section 7(a) loans. Of the more than 3,300 borrowers in the sample, 11.6% (representing more than \$33 million in SBA exposure) were found to have concealed their criminal records. Under current SBA procedures, the approximately 95% of loan applicants who answer "No" to the three criminal history questions are not subject to further criminal record checks to get their loan, i.e., their denials are accepted as fact. In the context of the potential negative impact of these loans on the Agency's subsidy rate, the IG made three suggestions to the ADA/ED for procedural changes to tighten this loophole.

❶ Conduct FBI Name Checks on All Applicants. The Federal Bureau of Investigation (FBI) Name Check provides a minimal level of capability to detect

undisclosed criminal records at a very reasonable price, with little or no effect on the loan application process. Name checks could be implemented with no extra paperwork on the part of the applicant. The process would only involve forwarding the SBA Form 912 (the applicant's Statement of Personal History) to the OIG's Office of Security Operations (OSO) and awaiting a response from the FBI. In the past year, the OIG has implemented a Machine Readable Data (MRD) system that will reduce the turnaround time at the FBI from 2 weeks to 48-72 hours. The cost of FBI Name Checks has also been reduced from \$12 for a manual check to \$1.40 for each MRD check which identifies no record and \$10.65 for each check which identifies a record.

❷ Incorporate Waiver Into Form 912. The Form 912 could be modified to include a statement that the applicant authorizes the OIG to verify the criminal-history representations on the form submitted. This waiver would supplement the existing warning against making false statements to the Government, and the signature of the applicant would overcome any Privacy Act concerns of the Department of Justice (DOJ). The inclusion of the waiver would provide a needed level of deterrence against many of those who would otherwise submit applications containing false statements as to the applicant's criminal record.

❸ Submit Copies of Every Form 912. A copy of the Form 912 for every applicant should be forwarded to the OIG's OSO, which will conduct random MRD checks and notify SBA's Office of Financial Assistance of any discrepant information. The OSO would attempt to conduct these

random checks quickly to preclude any disbursement of funds to ineligible applicants; the OIG normally would receive results from the FBI within 48-72 hours.

As of the end of this reporting period, the OIG, in consultation with the ADA/ED's staff, was selecting a sample of loans approved in FY 1994-96 to further test inferences drawn from the original study.

Review of Small Business Act Amendments of 1996

The OIG reviewed H.R. 3719 (a bill to amend the Small Business Act of 1953) and commented on several provisions. First, it was noted that one provision of the bill would give PLP lenders "complete authority" to service and liquidate loans without obtaining prior specific approval from SBA. The OIG expressed concern that this language could be interpreted as superseding the present requirement that PLPs submit liquidation plans for SBA approval. It is essential that PLPs continue to prepare liquidation plans, and that SBA review and approve such plans.

Second, the bill would require SBA to develop and implement a standard review program for PLPs. The OIG suggested that this program be expanded to include small business lending companies (SBLCs). This would relieve the OIG of the responsibility for providing mandatory and primary regular reviews of SBLCs, for which the OIG does not presently have sufficient resources. The OIG would continue to initiate audits of individual SBLCs where appropriate. Because some SBLCs are also PLPs, they would already be included in the standard

review program for PLPs.

Finally, the OIG proposed two technical amendments, one each to Title 12 and Title 18, to address an issue that recently surfaced in litigation involving false statements made to SBA. The amendments would make clear that SBA stands in the shoes of its predecessor, the Reconstruction Finance Corporation, and that a false statement made to SBA or an SBIC would be a criminal violation. The courts could then assess civil and criminal penalties for such violations.

Activities to Enhance Fraud Detection and Deterrence

Latest Results from Affirmative Civil Enforcement (ACE) Program

Over this reporting period, the OIG's participation in DOJ's ACE program produced six successful business loan cases, resulting in \$500,000 in recoveries and \$23,500 in civil penalties. The five smallest cases, which produced the civil penalties, involved fraudulent representations in applications for loans that were stopped before funds were disbursed. Two of those cases produced the OIG's first ACE results in Kansas. The sixth case represents the OIG's largest business loan ACE recovery and its first ACE result in Utah. Fraudulent statements in the loan applications in these cases involved tax returns, a standby agreement, a previous charge-off and bankruptcy, and the applicant's repayment record on other loans.

OIG Briefs Members of Lender Community

During this reporting period, our investigations staff continued its practice of making presentations to groups of participating lenders. The Assistant Inspector General for Investigations addressed more than 60 bankers at an SBA Lenders Conference in Seattle, highlighting the benefits to be gained from cooperation between participants and the OIG in combating waste, fraud, and abuse in the guaranteed loan programs.

Washington Fundraiser Sentenced for Conversion of Collateral

The former president of a fund-raising service company in Bellevue, Washington, was sentenced to 3 years probation, a \$50 special assessment, and \$18,008 in restitution to SBA and a participating lender bank. He had pled guilty to **conversion of collateral** pledged for a \$750,000 SBA-guaranteed business loan. The investigation revealed that he sold more than \$360,000 of his firm's accounts receivable pledged as collateral on the loan. The OIG investigation was based on a referral from the Seattle District Office and was conducted jointly with the FBI.

Missouri Water Bottling Executive Sentenced for Mail Fraud

The secretary of a water bottling company in New Bloomfield, Missouri, was sentenced to 366 days imprisonment, 2 years supervised release, and a \$50 special assessment. He had pled guilty to one count of **mail fraud**. Both he and his wife, the company's president, had been indicted for using the U.S. mails in a scheme to defraud SBA. (The charges against

the wife were dismissed as a condition of her husband's plea agreement.) The investigation showed that the couple made false statements to obtain a \$150,000 SBA-guaranteed loan, diverted loan proceeds to their own use, and sold or traded collateral after the business failed. The company made only one payment before defaulting on the loan. The OIG initiated this investigation based on a referral from the St. Louis District Office.

Pennsylvania Business Owner Sentenced for Bank Fraud and Making False Statements

The owner of an Allentown, Pennsylvania, dog grooming business pled guilty to **bank fraud, making a false statement to SBA, and making a false statement to a Federally-insured lender**. She was sentenced to 1 day imprisonment, 3 years supervised release, a \$2,000 fine, and a \$150 special assessment for submitting false information to SBA and a Small Business Lending Corporation (SBLC). The charges relate to her scheme to defraud SBA, the SBLC, and a participating lender bank by submitting fictitious Federal income tax returns as part of her loan applications. The woman first applied to the SBLC for a \$107,000 SBA-guaranteed loan, which was subsequently canceled due to discrepancies between the tax returns she submitted and those on file with the Internal Revenue Service (IRS). While being interviewed by an SBA/OIG special agent, she also omitted that she then went to the bank in Emmaus, Pennsylvania, and, using the same fictitious tax returns, applied for and received two non-SBA loans totaling \$100,000. This matter was referred to the OIG by the Financing Division of SBA's Philadelphia District Office.

New York Computer Company Owner Pleads Guilty to Bank Fraud and Making False Statements

The former owner of a computer sales and service business in Binghamton, New York, pled guilty to five counts of **bank fraud** and one count of **making false statements to SBA**. A multi-agency investigation revealed that the owner had grossly overstated the value of assets in a listing he submitted, to forestall the participating lender and SBA from calling his delinquent \$450,000 SBA-guaranteed loan. He also admitted using personal and business credit cards to obtain approximately \$34,000 in fraudulent cash advances (establishing a false account receivable with his credit card and then withdrawing cash against the credit) and “kiting” approximately \$10,000 in checks drawn on his credit union account. The OIG and the FBI joined the investigation initiated by the Secret Service.

Minnesota Business Owner Indicted for Bank Fraud

The owner of a technology company dealing in graphics software in Bloomington, Minnesota, was indicted on one count of **bank fraud** and one count of **making a false statement to SBA**. The OIG's joint investigation with the FBI determined that the man prepared and submitted a bogus independent auditor's report to a participating bank in an unsuccessful attempt to obtain a \$175,000 SBA-guaranteed loan for his technology company. The OIG initiated this investigation based on a referral from SBA's Minneapolis District Office.

Three Pennsylvania Businessmen Charged with Making False Statements to SBA

Three southeastern Pennsylvania men were charged in an information with one count of **making false statements** to SBA. The president and vice president, respectively, of a watch and jewelry retailer in Plymouth Meeting, Pennsylvania, and the store's certified public accountant, allegedly collaborated in the preparation of tax returns containing fictitious information and submitted them to a participating lender bank to qualify for a \$50,000 Low-Doc loan. On learning that the tax returns submitted as part of the application differed significantly from those on file with the IRS, SBA canceled the loan before any proceeds were disbursed. The accountant pled guilty to the charge and has surrendered his CPA license. The discrepancies, which were detected by SBA's tax return verification program, were referred to the OIG by the Philadelphia District Office.

Three Georgia Businessmen Sentenced on a Variety of Charges

Three LaGrange, Georgia, businessmen--the proprietor of a restaurant, a corporate president, and an attorney in private practice--were convicted on a variety of **false statement, theft, and conspiracy** counts. The restaurant owner was sentenced to 20 months incarceration, 4 years supervised release, 200 hours community service, \$35,000 restitution, and a \$350 special assessment. The corporate president was sentenced to 18 months incarceration, 4 years supervised release, \$85,000 restitution, a \$4,000 fine, and a \$150 special

assessment. The attorney was sentenced to 2 months home detention, 3 years probation, \$4,620 restitution, and a \$2,000 fine. The restaurant owner had received a \$400,000 SBA-guaranteed loan for his restaurant from a non-bank lender in 1990. He had submitted false documents relating to his use of the loan proceeds and forged an endorsement on a joint-payee loan disbursement check. The second businessman's corporation sold the land and a building for use as a site for the restaurant. He conspired with the restaurant owner to fabricate documentation of a capital injection into the restaurant. The attorney in the real estate transaction admitted complicity in their fraud scheme. The OIG opened this investigation based on a referral from SBA's Atlanta District Office.

Illinois Businesswoman Pleads Guilty to Theft by Deception

The sole proprietor of a weight loss center in Chicago, Illinois, was charged with and pled guilty in Cook County (Illinois) Circuit Court to one misdemeanor count of **theft by deception**. She was sentenced to 2 years supervised conditional discharge and 30 days community service. The woman admitted filing with the Cook County Recorder of Deeds two fraudulent lien releases on properties previously pledged as collateral for a \$64,900 SBA-guaranteed loan. After obtaining the unauthorized releases, she pledged the properties to a local mortgage company to obtain more than \$50,000 in additional financing. The OIG's investigation found that the woman prepared and filed two release deed forms that she represented to have been prepared by an SBA attorney. At the time she filed the false

releases, she was unaware the attorney had died several years earlier! The OIG initiated this investigation based on a referral from the SBA's Chicago District Office.

Indiana Businessman Charged with Making False Statement to SBA

A Muncie, Indiana, businessman was charged in an information with one count of **making a false statement** to obtain a \$400,000 SBA-guaranteed loan. The SBA/OIG's joint investigation with the FBI disclosed that the man falsely certified that the loan proceeds were to be used as operating capital for his foundry and machine shop, albeit he actually intended to (and subsequently did) use a substantial portion of the loan proceeds for his personal benefit. This investigation was initiated based on a referral from the Indianapolis District Office.

Florida Dairy Product Supplier Suspended from Federal Programs-- Balance of SBA-Guaranteed Loan Canceled

Following notification by the OIG, SBA's Miami District Office **canceled the final disbursement of \$734,037.80 of a \$1,200,000 SBA-guaranteed loan** to a Fort Lauderdale, Florida, dairy product supply company. SBA took this action after the General Services Administration suspended the firm from participating in all Federal programs. The dairy supply company allegedly falsely entered into an agreement with the U.S. Department of Agriculture (USDA) to export milk powder to the United Arab Emirates. Investigation by USDA's OIG determined that the firm had diverted

the milk powder through Singapore to the Philippines in violation of the agreement. The firm had earlier received an SBA-guaranteed loan of \$375,000 to purchase inventory and equipment. The company's repayment ability remains heavily reliant on the Government's export subsidies that will be eliminated by the current suspension.

Jewelry Store Owner Indicted for Making False Statements

The owner of a retail jewelry store in San Luis Obispo, California, was indicted on five counts of **making false statements to a Federally-insured financial institution**. An SBA/OIG investigation conducted jointly with the FBI revealed that the businessman submitted altered copies of his 1986 and 1987 individual income tax returns in applying for a \$450,000 SBA-guaranteed loan approved in 1988. He subsequently provided altered copies of tax returns, both individual and corporate, for 1988-90 and obtained yet another SBA-guaranteed loan for \$100,000. Both loans ultimately went into default and were liquidated. Following the liquidation efforts, a total of \$336,895.72 was charged off by the SBA. The investigation was initiated based on information provided by the Fresno District Office.

Georgia Tax Accountant Pleads Guilty to Submitting False Documents

A former Decatur, Georgia, tax accountant pled guilty to one count of **submitting false documents to SBA** in connection with a \$154,000 SBA-guaranteed loan to his sole proprietorship. The OIG's investigation established that he submitted altered copies

of tax returns for the years 1986-88, thereby substantially overstating his income for the purpose of procuring his loan. The accountant also submitted as collateral for the loan a "deed to secure debt" on which his wife's signature had been forged. The OIG initiated the investigation based on a referral from the Atlanta District Office.

One Sentenced, Two More Indicted for False Statements to SBA Lender

One loan applicant pled guilty and was sentenced and two other borrowers were indicted for **making false statements to a Federally-insured lender** in southern California. These were the latest results of a joint OIG/FBI investigation.

❶ The former owner of a food company in Garden Grove, California, pled guilty to one count. She was sentenced to 4 months imprisonment, 4 months home detention, and 1 year supervised release. She submitted false tax returns and a false equipment purchase contract to obtain SBA-guaranteed loans totaling \$420,000.

❷ The former owner of a restaurant and billiard club in San Gabriel, California, was charged with six counts, two of which charged him with submitting altered income tax returns with his application for a \$150,000 SBA-guaranteed loan which subsequently defaulted. The four other charges were related to non-SBA loans.

❸ The former owner of a beauty salon in Long Beach, California, was charged with two counts of submitting false documents to obtain disbursement of his \$150,000 SBA-guaranteed loan. This loan also defaulted.

The OIG initiated the investigation, centered on the packager of the loans, based on information provided by the Santa Ana District Office.

California Landscaper Sentenced for Making False Statements and Filing False Tax Returns

The owner of a landscape maintenance company in Anaheim, California, was sentenced to 366 days imprisonment, 3 years supervised release, and payment of all personal and corporate taxes he owed. He had pled guilty to three counts of **making false statements to Federally-insured lenders** and two counts of **filing false tax returns**. These charges stemmed from two investigations. The OIG initiated the first investigation when the owner's bookkeeper reported that he wanted her to prepare false tax returns and related financial documents as part of an application for a \$400,000 SBA-guaranteed loan. Fortunately, the loan application was declined by the bank before it became aware of the false financial figures, and the man subsequently pled guilty to one false statement charge. The second investigation began when, suspecting that this was not the first time this same individual had used false documents to defraud a bank, the prosecutor requested that the OIG examine the files of his other loans. This led to both the identification of two other bank loans that were obtained with false tax returns and the discovery that he was under investigation by the IRS for other suspected crimes. The OIG then joined the ongoing IRS investigation, which resulted in the four later charges and the second guilty plea.

Florida Swimming Pool Supplier Pleads Guilty to Making False Statements

The president of a swimming equipment seller in Fort Myers, Florida, pled guilty to one count of **making material false statements** to influence actions of SBA. He was sentenced to 5 years probation and a \$9,000 fine. The businessman submitted personal and corporate tax returns he knew to be fraudulent in an effort to obtain a \$100,000 SBA-guaranteed loan. Approval of his application was canceled because of the considerable discrepancies that existed between information contained in the tax returns he submitted with the loan application and those he filed with the IRS. The OIG initiated the investigation based on a referral from the Miami District Office.

New York Banker Sentenced for Soliciting Commissions for Procuring Loans

A former vice president of the New York City branch of an Argentine bank was sentenced to 18 months imprisonment, 5 years supervised release, and a \$150 special assessment. He had been convicted of **soliciting commissions for procuring loans** guaranteed by SBA. The \$20,000 in commissions were paid by three loan applicants in return for his assistance in obtaining loan approvals totaling \$930,000. The banker headed the SBA-guaranteed loan program of the bank, which was at that time one of SBA's largest participating lenders in New York City. The OIG investigation was conducted jointly with the FBI.

California Gas Station Owner Indicted for Forgery and Possession of Stolen Mail

The owner of a gas station in San Diego, California, was indicted on 15 counts of **forging U.S. Treasury checks** and 2 counts of **possession of stolen mail**. The Secret Service asked the OIG to join its investigation, which had identified \$340,000 in stolen U.S. Treasury checks deposited into the man's business bank account. The OIG's portion of the investigation also confirmed that he had obtained an \$80,000 SBA-guaranteed loan from a participating lender bank for business improvements. As part of his application, the man provided "copies" of 3 years' corporate income tax returns which, as he admitted when interviewed, significantly overstated the business' taxable income. In the returns filed with the IRS, the business reported losses for the 3-year period.

Utah Motorcycle Dealer Pleads Guilty to Bank Fraud

An owner of a motorcycle dealership in Salt Lake City, Utah, was charged with and pled guilty to one count of **bank fraud**. He was sentenced to 6 months home confinement, 3 years supervised release, and \$71,799 restitution. The dealership had received a \$185,000 SBA-guaranteed loan in 1979, pledging three pieces of real property as collateral. The felony information to which he pled guilty charged that in the fall of 1993, when the loan was in serious default, he caused the filing of reconveyance documents fraudulently releasing the liens on the properties. Having obtained release of the liens, he then pledged two of the

properties to another Federally-insured bank to obtain an additional \$150,000 in financing. The SBA/OIG investigation also determined that the businessman forged the signature of a former officer of the participating lender on the release-of-lien documents. The investigation was based on a referral from the Salt Lake City District Office.

Texas Couple Pleads Guilty to Making False Statement to FDIC-Insured Bank

An Alvin, Texas, couple were indicted on one count of **conspiracy**, five counts of **making false statements to an FDIC-insured bank**, and five counts of **submitting false documents to a Federal agency**. They later pled guilty to one count of **making a false statement to an FDIC-insured bank**; in return, the Government agreed to dismiss the other ten felony charges. In an effort to obtain approval of a \$338,000 SBA-guaranteed loan to finance their purchase of a convenience store in Houston, Texas, the couple altered and submitted copies of the previous owner's tax returns. They also submitted false tax returns for another store in LaMarque, Texas, to obtain approval of a \$200,000, SBA-guaranteed loan for its purchase. SBA officials foiled their scheme by declining the loan applications after the profits reflected on the false returns could not be verified. The charges were the result of an OIG investigation which was based on a referral from the Office of District Counsel of the Houston District Office.

California Father Convicted for Bank Fraud and Making a False Statement

A Woodland Hills, California, man was convicted on charges of **bank fraud** and **making a false statement to a Federally-insured lender**. His daughter had also been indicted on two charges, which were previously dismissed based on her claim that, at only 18 years of age, she had not understood the significance of the documents she signed. The OIG investigation revealed that the daughter's application for a \$665,000 SBA-guaranteed loan to purchase real property for the operation of a nursery contained false financial documents, including false tax returns. Her father, acting under an alias, had purchased the property for \$450,000 and then immediately sold it to her for \$900,000, thereby doubling its purchase price. The participating bank financed the purchase based on this inflated price. The man also falsely represented to the bank that he was giving his daughter a gift of \$160,000 toward the purchase of the property. The nursery never opened for business, and the loan went into default after only two loan payments had been made. Because of statements the father made about a plan to flee the country should he be convicted, the court immediately remanded him into the custody of the U.S. Marshals Service following the jury verdict. The OIG initiated this investigation based on a referral from the Los Angeles District Office.

Pennsylvania Restaurant Owner and Associate Sentenced for Conspiracy and Making False Statements

The owner of a restaurant in Downingtown,

Pennsylvania, and his associate were sentenced. The owner was sentenced to 4 months home detention, 3 years probation, a \$1,500 fine, and a \$150 special assessment; his associate was sentenced to 200 hours community service, 2 years probation, and a \$150 special assessment. Each had pled guilty to **conspiracy** and **making false statements** in connection with the owner's application for a \$65,000 SBA-guaranteed loan for his business. The OIG's investigation found that the associate prepared and the owner signed and submitted false Federal income tax returns to a participating bank. The returns showed a net profit of more than \$40,000 for each of the years 1993 and 1994; however, the restaurant actually incurred losses in both years. On learning that the tax returns submitted as part of the application differed significantly from those on file with the IRS, SBA officials canceled the loan before any proceeds were disbursed. The discrepancies, which were detected by SBA's tax return verification program, were referred to the OIG by the Philadelphia District Office.

California Loan Broker and Nine Others Charged with Making False Statements

A loan broker from La Canada, California, and eight other persons connected to SBA-guaranteed loans he brokered were charged with making false statements. The broker and seven of the nine others have pled guilty.

The loan broker was charged with and pled guilty to five counts of **making false statements in a loan application to a Federally-insured financial institution**.

He also pled guilty to a **criminal forfeiture** count allowing the Government to recapture the illegal proceeds of his crimes. Between 1987 and 1992, the man brokered more than two dozen fraudulent loans totaling more than \$9 million, primarily for Korean-American clients. His scheme involved the submission of falsified financial information, including tax returns, financial statements, invoices, and cashiers checks representing bogus cash infusions into the businesses, to induce the banks and SBA to grant the loans. When the banks and SBA approved the loan applications, the broker would launder part of the proceeds through a business that he fraudulently represented had sold equipment to the various applicants.

❶ The owner of a Los Angeles automotive transmission shop was charged with and pled guilty to one count of **making a false statement on a loan application to a Federally-insured financial institution** in connection with his \$420,000 SBA-guaranteed business loan. The investigation revealed that the owner submitted altered tax returns for the years 1988-90, each of which significantly overstated his income. He also submitted invoices in the names of nonexistent businesses.

❷ The owner of a Los Angeles sporting goods store was charged with and pled guilty to one count of **making a false statement on a loan application to a Federally-insured financial institution** in support of her \$1,000,000 SBA-guaranteed business loan. The investigation revealed that she submitted altered tax returns for the years 1988-90, each of which significantly overstated her income.

❸ The owner of a combined grocery market and liquor store was charged with and pled guilty to one count of **making a false statement** to SBA in connection with his \$231,000 disaster business loan. The investigation first discovered that an altered tax return for 1989 had been submitted to obtain the \$161,119 SBA-guaranteed loan that enabled the man to purchase the market. The investigation also found that he submitted altered 1989 and 1990 returns to obtain the disaster loan for repair of damage stemming from the 1992 civil unrest. Each of the three returns significantly overstated his income. The defendant sold the store in 1992, including SBA's only collateral for the disaster loan, and received nearly \$500,000 from the sale of the business.

❹ The owner of a clothing manufacturer in La Canada, California, was charged with and pled guilty to one count of **making false statements in a loan application to a Federally-insured bank**. He had obtained a \$1,000,000 SBA-guaranteed business loan, supported by an application that contained altered copies of income tax returns for 1987-89, each of which significantly overstated the net profit from his business.

❺ The owner of a general merchandise discount store in Los Angeles, California, pled guilty to one count of **making false statements in a loan application to a Federally-insured bank**. The false statements were made in connection with his \$1,000,000 SBA-guaranteed business loan from a participating lender bank. The loan was referred to the OIG by officials at the bank who became suspicious of the documentation supporting the borrower's capital injection. In addition to the false

documents associated with the capital injection, the man submitted altered Federal income tax returns for 1987-89 that significantly overstated his income to support his loan application.

⑥ The owner of a market in West Covina, California, pled guilty to one count of **making false statements in a loan application to a Federally-insured bank**. He had obtained a \$285,000 SBA-guaranteed business loan based on an application containing altered copies of income tax returns for 1988-90. Each of the returns significantly overstated his income.

⑦ The former owner of a Pomona, California, restaurant was indicted on five counts of **making false statements to Federally-insured financial institutions**. The restaurateur submitted altered tax returns to the lender of his \$550,000 SBA-guaranteed business loan that significantly inflated his business income. He also submitted a false financial statement to induce the participating lender to grant a payment deferment and not foreclose the loan.

⑧ A former personal banking officer at a Federal bank, located in Paramount, California, was charged with one count of **making a false statement to SBA**. In an attempt to help her sister, who had applied for a \$2.1 million Section 504 loan, the banker prepared a false deposit verification form for submission to both SBA and the participating lender. On the form, she represented that her employer had two accounts, with a combined balance of \$790,000, held solely in her sister's name. In fact, as she knew, the accounts were never

the sole property of her sister. The accounts listed on the form had been opened by another person, and the banker had added her sister's name to them at a later date. The false statement was detected during the OIG's and U.S. Secret Service's joint investigation of the loan broker who had submitted the loan application to the participant. As results of this part of the investigation, SBA canceled the loan, producing a \$750,000 cost avoidance (SBA's guaranteed share), and the banker was terminated from her position.

⑨ The former owner of a cafe in Riverside, California, was indicted on five counts of **making a false statement in a loan application to a Federally-insured bank**. He allegedly submitted altered income tax returns for the years 1987-89 with his application for a \$225,000 SBA-guaranteed loan to purchase the cafe. He allegedly represented on his Business Plan that his personal capital came from the sale of another business; in fact, he had borrowed the funds from a friend. The cafe owner also represented that he intended to purchase machinery and equipment totaling \$125,000 from a company which was in fact controlled by the loan broker. The loan broker returned the funds to the cafe owner who subsequently repaid the undisclosed personal loan.

The OIG initiated the investigation, which the U.S. Secret Service subsequently joined, after the participating lender and the SBA's Los Angeles District Office referred the matter. Loans still being examined in this investigation total over \$16 million.

California Loan Packager Sentenced to Prison Term for Fraud

A Westminster, California, loan packager was sentenced to 24 months imprisonment, 3 years supervised release, and \$86,000 restitution. The man had previously pled guilty to two counts of **bank fraud** and one count of **making false statements to a Federally-insured financial institution**. This action was the latest result of an extensive SBA/OIG joint investigation with the FBI to examine a fraudulent loan packaging scheme implemented by this individual. To obtain SBA-guaranteed loans for himself and numerous clients, he created false financial documents such as tax returns and invoices. A total of 14 borrowers, all of whom were his clients, have been convicted of **making false statements to Federally-insured lenders**, and one bank official has been convicted of **illegal receipt of commissions for procuring loans**. Two of the actions, which took place during this reporting period, are reported below:

❶ A former owner of a retail jewelry company in Garden Grove, California, pled guilty to one count of **making a false statement on a loan application to a Federally-insured financial institution** in connection with his \$100,000 SBA-guaranteed business loan.

❷ The former owner of a Paramount, California, marble flooring company was convicted on all counts of his indictment. The indictment charged the man with **making false statements on a loan application to a Federally-insured financial institution** in connection with his \$300,000 SBA-guaranteed business loan.

The OIG initiated this investigation based on a referral from SBA's Los Angeles District Office.

Ohio Businessman Indicted on Four Fraud Charges

The president of a now-bankrupt Chardon, Ohio, manufacturer of medical equipment, was indicted on one count of **bank fraud**, two counts of **making false statements**, and one count of **wire fraud**. An OIG investigation determined that, at the time the businessman was negotiating to obtain a \$700,000 SBA-guaranteed loan, he concealed from both SBA and the participating lender bank his intent to sell a substantial portion of the business assets. He also diverted a majority of the proceeds from those sales to pay off other debts and caused \$100,000 to be fraudulently wired from another bank to the participating lender. During a May 1996 interview by an OIG special agent, he also made material false statements by stating that officials of the participating lender had known about and approved the sale of assets. This investigation was initiated based on a referral from the Cleveland District Office.

South Dakota Rancher Pleads Guilty to Making False Statement

An Eagle Butte, South Dakota, rancher pled guilty to one count of **making a false statement** to a Federal agency. In return, the Government agreed to dismissal of 15 other felony charges on which he had been indicted. The SBA/OIG's joint investigation with the Department of the Interior (DOI) OIG determined that, to obtain a \$150,000 SBA-guaranteed loan, the rancher concealed

from SBA and the participating lender that he had failed to repay a previous \$30,000 loan guaranteed by DOI's Bureau of Indian Affairs (BIA). He also submitted a document falsely claiming that he had received a \$50,000 BIA grant. The investigation also found that the rancher tampered with a witness by attempting to persuade the participating bank's loan officer to remove the fraudulent BIA document from the loan file. The DOI/OIG asked the SBA/OIG to join the investigation.

Washington Manufacturer Indicted for Bank Fraud and Money Laundering

The former president of a Port Angeles, Washington, crane manufacturer was indicted on one count of **bank fraud** and one count of **money laundering**. The OIG's joint investigation with the FBI and the IRS found that he made false statements about his criminal history, his Social Security number, and his cash injections into the corporation, to obtain a \$100,000 SBA-guaranteed business loan. In addition, once the loan was disbursed, the businessman misused approximately \$12,000 of the loan proceeds to pay personal expenses, including his rent and his credit card bills. The loan defaulted after the man fled the Port Angeles area with the corporation's investors' funds. A warrant was issued for his arrest, and SBA/OIG and FBI agents arrested the man. The OIG's investigation was initiated after SBA's Seattle District Office referred an inquiry from the Washington State Attorney General's Office.

OIG Criminal Investigator Receives Special U.S. Attorney Award

The United States Attorney's Office for the Eastern District of Pennsylvania issued a special commendation to Martin Carroll, a special agent in the OIG's Philadelphia Resident Office, for his outstanding performance, dedication, and professionalism in an investigation that resulted in the payment of \$1.56 million by a Preferred Lender to the Government. The U.S. Department of Justice (DOJ) award was presented by U.S. Attorney Michael R. Stiles. Mr. Carroll was the primary investigator in a case, based on the findings of an OIG audit, in which the bank made a \$1 million SBA-guaranteed loan to a foundry, knowing that the company did not qualify. The audit found, and the investigation confirmed, that the bank concealed the fact that the foundry's chief executive owned 46 percent of the company and that his substantial assets therefore made the company ineligible for a Section 7(a) loan. The borrower defaulted on the loan 9 months after it was approved, and SBA purchased the guaranteed portion from the bank. The case resulted in a civil penalty of over \$600,000 and approximately \$950,000 in reimbursement to SBA for its payment and interest on the loan guarantee, the largest recovery in the history of SBA's participation in the DOJ's Affirmative Civil Enforcement program.

Disaster Loan Program

Pursuant to Section 7(b) of the Small Business Act, as amended, SBA's disaster loans represent the primary form of Federal assistance for non-farm, private sector disaster losses. For this reason, the **Disaster Loan Program** is the only form of SBA assistance **not limited to small businesses**. Disaster loans from SBA help homeowners, renters, businesses of all sizes, and non-profit organizations fund rebuilding. SBA's disaster loans are also a critical source of economic stimulation in disaster-ravaged communities, helping to energize employment and stabilize tax bases.

By providing disaster assistance in the form of loans which are repaid to the U.S. Treasury, the SBA disaster loan program helps reduce Federal disaster costs compared to other forms of assistance like grants. When victims need to borrow to repair uninsured damages, the low interest rates and the long terms available from SBA make recovery more affordable. Because SBA tailors the repayment of each disaster loan to each borrower's capability, unnecessary interest subsidies paid by the taxpayers are avoided.

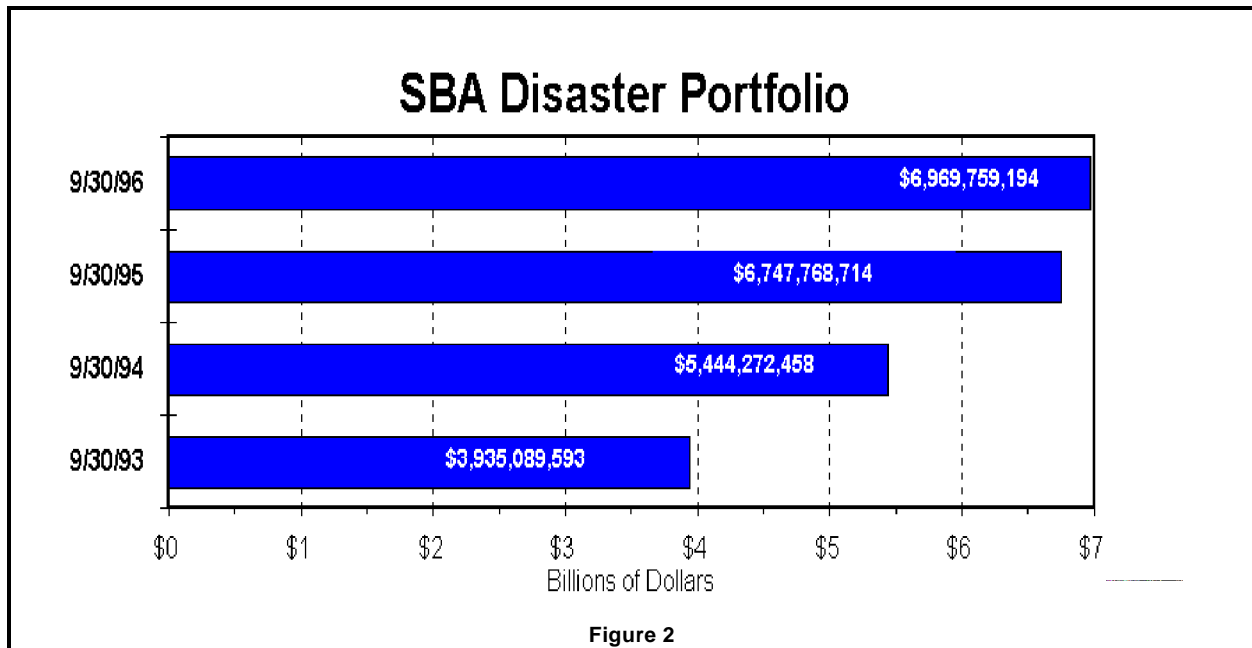
The need for SBA disaster loans is unpredictable. During FY 1996, SBA approved 37,822 loans for \$987.9 million. Since the inception of the program, SBA has approved more than 1,336,800 disaster loans for more than \$23.9 billion. As of the end of FY 1996, the SBA disaster loan portfolio included more than 274,000 loans valued at over \$6.9 billion. The total available for FY 1997 disaster loans, including carryover and contingency funds, is approximately \$1,535 billion.

SBA is authorized by law to make two types of disaster loans: (1) physical disaster loans, which are a primary source of funding for permanent rebuilding and replacement of uninsured disaster damages to real and personal property homeowners, renters, businesses of all sizes, and non-profit organizations; and (2) economic injury disaster loans (available by law only to small businesses), which provide necessary working capital until normal operations can resume after a physical disaster. SBA delivers disaster loans through four specialized Disaster Area Offices located in Niagara Falls, New York; Atlanta, Georgia; Fort Worth, Texas; and Sacramento, California.

Summary of OIG Activity

The following summarizes OIG activities relating to SBA's disaster loan programs during the reporting period:

- Six audits and one inspection were underway during the reporting period.
- Disaster loan investigations resulted in 7 indictments and 13 convictions, and produced \$586,500 in court-ordered restitution, \$405,460 in other recoveries by SBA, and \$27,990 in fines and civil penalties.
- Office of Security Operations name checks resulted in the declination of 10 disaster loans totaling \$299,331.
- Nine disaster loan investigations were closed, leaving an inventory of 83 active cases involving 404 subjects. Due to workload demands, another 2 disaster loan cases were referred to other law enforcement agencies for investigation, resulting in a total of 12 disaster loan referrals to monitor.
- Two Standard Operating Procedures were reviewed during the reporting period.



Efforts to Improve SBA Program Management

Program Vulnerability Memorandum Issued on Terminology on Disaster Home Loan Forms

The Inspector General (IG) issued a program vulnerability memorandum (PVM) to the Associate Administrator for Disaster Assistance (AA/DA), citing the outcomes of two recent OIG investigations involving disaster home loan fraud. In each case, an applicant, who resided elsewhere when a disaster struck, obtained an SBA home loan for a property he claimed as his "primary residence" on the disaster home loan application (Form 5C).

In the first case, the owner of a damaged house applied to both SBA and the Federal Emergency Management Agency (FEMA) for financial assistance in recouping his "disaster losses." The investigation revealed, however, that at the time of the earthquake a tenant was renting the house, and none of the personal property damaged by the quake belonged to the landlord. A grand jury charged the landlord with making false claims to both FEMA and SBA. At the trial, he asserted that because he owned the house and was preparing to occupy it, he considered it his "primary residence." He claimed neither SBA nor FEMA ever advised him of the definition of "primary residence." He also established that he owned the personal property he listed on the Verification of Personal Property Damage (Form 739) and claimed that, although it was at his actual residence at the time of the quake, it was damaged by the quake there and that he subsequently moved it to the

house listed on the loan application. Because Form 739 asks for the location of damaged property without drawing a distinction between real and personal property, the defendant asserted at trial that he believed he was allowed to claim earthquake-damaged personal property, regardless of its location at the time of the quake, at the address he listed. He was convicted of making a false claim to FEMA but acquitted of defrauding SBA. A subsequent polling of the jurors revealed that they agreed the defendant was not entitled to receive FEMA funds because he did not reside at the house when the quake hit, but they were confused about the SBA charge and acquitted in part because SBA forms were unclear. The jurors called the forms unclear because they lacked a clear definition of "primary residence" and did not specifically ask for the location of damaged personal property.

In the other investigation, an applicant claimed a damaged vacation home as his "primary residence." The investigation revealed that while he did not live there, he lived in the vicinity of his work location. The borrower claimed in an interview that he intended to move to the vacation home permanently following retirement. Criminal prosecution of this subject was declined because of the lack of a published definition of "primary residence."

The first case also highlighted another limitation in Form 5C, which asks whether the applicant has ever been convicted of a felony "in connection with a riot or civil disorder." The form does not ask for disclosure of any other convictions for serious offenses, as other SBA programs do.

To tighten these loopholes, the IG's PVM suggested changes to and expansions of the terminology in Forms 5C and 739. These included substituting "primary home," which is used elsewhere, for "primary residence" and enumerating a list of a primary home's attributes. A definitive statement of the ineligibility of secondary or to-be-occupied homes was also suggested. The expansion of the criminal history question is intended to protect SBA from making disaster home loans to any applicant with a serious criminal record. Also, the PVM suggested expanding the property-location question on Form 739 to differentiate, as appropriate, the locations of damaged personal and real property.

In his response to the IG, the AA/DA disagreed with most of the recommended changes, stating that "we think the costs outweigh the benefits," that such additions would be "contrary to the Government's efforts to simplify and shorten applications," and that the suggestion regarding Form 739 evidenced "some confusion about" the eligibility for assistance of personal property located elsewhere in a disaster area than at a primary residence. He did agree to substitute the term "primary home" for "primary residence" when Form 5C is reprinted.

Activities to Enhance Fraud Detection and Deterrence

North Carolina Businessman Sentenced for Making False Statements and Mail Fraud

The owner of a Charlotte, North Carolina, furniture franchisee was sentenced to 6 months home confinement, 3 years

probation, a \$10,000 fine, and \$300,000 restitution. He had pled guilty to one count each of **making false statements** to SBA and **mail fraud** in connection with a \$114,000 economic injury disaster loan approved in 1989. The OIG's joint investigation with the FBI disclosed that the man had submitted false statements regarding his personal financial condition and criminal history to induce SBA's approval of the loan in the aftermath of Hurricane Hugo. The investigation also showed that he had used the U.S. Mail in furtherance of his scheme to defraud SBA.

Georgia Disaster Loan Applicant Pleads Guilty to Making False Statements

A St. Marys, Georgia, man was indicted on nine counts of **making material false statements** to induce SBA to disburse a \$125,000 disaster business loan based on physical damage to a mobile home park. He pled guilty to one count; in return, the Government agreed to dismiss the other eight felony charges. The investigation found that he had falsely represented himself as the sole owner of a mobile home park and six mobile homes when they were damaged or destroyed during a severe storm. He also falsely stated that he would use proceeds of the disaster loan to repair or replace the six mobile homes. The OIG initiated the investigation based on information from an anonymous caller.

Three Guilty in Mississippi Tree Farm Scheme

The proprietor of a tree farm and lumber business in Hattiesburg, Mississippi, and his wife were found guilty by a Federal trial

jury. He was convicted on one count of **conspiracy** and two counts of making material **false statements** to influence SBA, and his wife was convicted on one count of making material **false statements** to influence SBA. His attorney pled guilty to making material **false statements** to influence SBA. All the charges relate to a \$222,400 economic injury disaster loan received in 1993. Both the businessman and his attorney had been charged with submitting a personal financial statement falsely representing that he owned certain real and personal property that, in fact, had previously been foreclosed on and seized by creditors. All three defendants had been charged with submitting title documents falsified to support the fictitious claim that the couple was mortgaging an 80-acre real property to SBA. Finally, the indictment alleged that the couple improperly negotiated joint-payee Treasury checks representing \$124,900 of the disaster loan proceeds. Parenthetically, evidence developed by the OIG's investigation also resulted in the businessman's indictment by a Lamar County, Mississippi, grand jury on one count of **false pretense** for improperly negotiating one of the joint-payee Treasury checks; this particular charge has not yet gone to trial. The OIG initiated the investigation based on a referral from SBA's Gulfport Branch Office.

U.S. Virgin Islands Loan Applicant Indicted for Making False Statement

A St. Croix, U.S. Virgin Islands, disaster loan applicant was indicted on charges of **making false statements to SBA**. The SBA/OIG's joint investigation with the Federal Emergency Management Agency

(FEMA)'s OIG developed evidence that the application for a \$10,000 disaster home loan contained false claims for lost property, a fabricated bill of sale for an automobile, and falsified property rental agreements. The investigation was based on a referral from the Disaster Assistance recovery center in St. Croix.

North Dakota Resident Indicted for Making False Statements and Theft of Public Money

A resident of Mandan, North Dakota, was indicted on three counts of **making a false statement to SBA** and three counts of **theft of public money**. The SBA/OIG investigation determined that the loan applicant failed to show a \$103,189 judgment on her application for a \$35,000 disaster home loan. A court-authorized search of her home by an OIG agent and Deputy U.S. Marshals documented that she had not used the loan proceeds to repair her home, as she had claimed. Consequently, she was charged with theft of public money for failing to return the loan proceeds that had not been used for their authorized purposes. The OIG initiated the investigation based on a referral from the Fargo District Office.

Government Awarded Treble Damages in Judgment Over Fraudulent Disaster Loans

The Government was awarded a \$418,000 civil judgment against a restaurant holding company and its president for **false claims, conversion of collateral, and breach of contract** in connection with two disaster loans. The company, which was operating a

restaurant in Des Moines, Iowa, at the time of the Midwest Flood of 1993, had already received the first \$110,000 of the loan proceeds when the Des Moines District Office was told that the firm's president had sold equipment pledged as collateral for SBA loans. The OIG's subsequent investigation showed that he had failed to disclose a significant debt when applying for the disaster loans, lied to conceal his misuse of disaster loan proceeds, and repeatedly lied to prevent SBA from recovering the collateral he had unlawfully sold. The judgment included three times the \$110,000 amount of loan proceeds disbursed, a \$10,000 penalty for each of five false claims, plus a 10 percent surcharge. The OIG initiated this Affirmative Civil Enforcement investigation based on a referral from the Des Moines District Office.

Minnesota Businessman Sentenced to Prison for Fraud Scheme

The owner of an agricultural service company in Clarkfield, Minnesota, was sentenced to 23 months imprisonment, 2 years supervised release, and \$5,000 restitution to the State of Minnesota. He had been indicted on 16 criminal counts, including 2 counts of **making false statements** in applying for a \$500,000 SBA disaster business loan in 1992 to repair tornado damage to his business. He and three other defendants had also been indicted on multiple felony counts of conspiracy, bribery, mail fraud, and false statements to defraud the Department of Housing and Urban Development (HUD) in another loan scheme. Adjudicated guilty of **conspiracy** and **mail fraud**, all the other charges against him were dismissed. In his SBA loan

application, he had also failed to disclose two Government loans on which he had defaulted. Aware of the 1978 SBA loan, but not the HUD loan, SBA declined his \$500,000 application. The SBA/OIG joined the HUD/FBI investigation after being made aware of the situation by the Minneapolis District Office.

Florida Company Executive Sentenced for Making False Statement

The president of a sports entertainment business in Belleair Beach, Florida, was sentenced to 1 year probation, 100 hours community service, and a \$150 fine. He had previously pled guilty to one count of **making false statements to SBA**. Having submitted Borrower's Progress Certifications to SBA that contained a number of false statements to induce disbursement of \$190,400 in business physical disaster loan proceeds, he also submitted fraudulent copies of invoices, proposals, checks, and other documents purportedly corroborating his certification of damaged video equipment used in his business. In 1995, after being interviewed by an OIG special agent, he voluntarily repaid the \$95,609 balance of the fraudulently-obtained loan, the \$19,393 balance of his economic injury disaster loan, and the \$40,837 balance of his disaster home loan. This investigation was based on a referral from the Disaster Assistance Area 2 Office.

Florida Veterinarian and Wife Plead Guilty to Making False Statements

The president and owner of a corporation that operated veterinary clinics in Homestead and Miami, Florida, and his wife pled guilty

to two counts and one count, respectively, of **making false statements to SBA**. Each was sentenced to 4 months home detention with electronic monitoring, 3 years probation, and a \$7,500 fine. The company had received a \$106,100 loan to repair or replace machinery, equipment, inventory, and real property damaged by Hurricane Andrew. The SBA/OIG investigation disclosed that, to obtain the loan and to conceal their misuse of some of the proceeds, the couple submitted fictitious receipts, invoices, and copies of checks as documentation of expenses they had neither incurred nor paid. The investigation was based on a referral from FEMA's OIG.

California Meat Market Owner Indicted for Filing False Claim and Making False Statements

A former owner of a meat market in Huntington Park, California, was indicted on one count of **filing a false claim** with the SBA and five counts of **making false statements** to the Agency. The OIG initiated the investigation of the owner following receipt of a letter from his insurance company. The investigation revealed that the man had received a \$174,100 disaster business loan following the 1992 civil unrest in Los Angeles, claiming extensive damage to his store from looting. The loan went into default, however, after only two payments were made. Interviews with numerous witnesses confirmed that no looting took place at the market. When interviewed, he confessed that he had overstated his losses and admitted that he also inflated his income on the bogus tax returns submitted with the loan application. The IRS had no record of the

owner having filed any tax returns for the years in question, 1988 through 1991.

More Results From Ongoing Investigation of California Loan Packagers

In the latest results from the continuing investigation of two southern California brothers who acted as disaster loan packagers, two more of their clients have been charged with crimes against SBA, five have entered guilty pleas, and three of the five have been sentenced. All of these actions involve applications for economic injury disaster loans filed in the wake of the 1992 civil unrest in Los Angeles, California.

① An owner of a clothing manufacturer was charged with and pled guilty to **filing a false claim** with SBA. He was sentenced to 5 years probation, \$28,000 restitution, and 2,000 hours community service. In his application for a \$300,000 loan for his business, the man provided copies of income tax returns that were never filed with the IRS and that significantly overstated his business income.

② A client of the disaster loan packagers pled guilty to a misdemeanor count of **theft of Government funds**. He was sentenced to 5 years probation, \$218,500 restitution, and 2,000 hours community service. In connection with his application for a \$360,000 loan for his business, the applicant claimed to be the sole owner of a clothing manufacturer in Los Angeles, when he actually owned only 65 percent. He concealed the other owner's interest from SBA in an effort to hide the other owner's poor credit history.

③ A Northridge, California, man pled guilty to one count of **making a false statement to a Federally-insured bank**. He was sentenced to 3 months in a half-way house, 3 months home detention, 5 years probation, 300 hours of community service, and \$35,000 restitution. To facilitate the approval of a loan, the applicant submitted a false employment verification form, claiming that his wife was employed at a salary in excess of \$100,000 per year; in fact, she was unemployed. The couple became subjects of the investigation when the Disaster Assistance Area 4 Office questioned their application for a \$300,000 disaster loan for the wife's non-existent business, a fashion boutique. SBA turned down the application, and the investigation later established that the business did not exist.

④ An owner of a clothing manufacturer pled guilty to **knowingly converting SBA disaster loan proceeds to his own use and the use of others**. The charge emanated from his fraudulent application for a \$180,000 loan for his business. Because he applied for a loan for which he knew he was ineligible, his expenditure of the proceeds constituted conversion.

⑤ The owner of a clothing manufacturer in Los Angeles, California, was charged with and pled guilty to **filing a false claim with SBA**. With his application for a \$500,000 loan for his business, the man submitted altered copies of income tax returns that significantly overstated his business's income. He also submitted a schedule of liabilities that included numerous creditors with which he had never done business.

⑥ The owner of a clothing manufacturer in Los Angeles, California, was charged in a criminal information with one count of **filing a false claim** with SBA. She submitted allegedly fictitious income tax returns for 1990-91 with her application for a \$300,000 loan. Based on the financial information in those returns, which significantly overstated her business income, SBA disbursed \$61,500 to the businesswoman. She has yet to make a single payment on this loan. Her application reflected the assistance of an employee of the loan packagers currently under investigation. This employee has pled guilty to earlier charges relating to his own SBA disaster loan.

These were the most recent results of a joint OIG and U.S. Secret Service investigation of falsified loan applications prepared by the two southern California brothers acting as disaster loan packagers. The case was opened as a result of a tip from a concerned citizen and a referral from the Disaster Assistance Area 4 Office.

Development Company Owner Charged With Filing False Claim

An owner of a Monterey Park, California, development company was charged in an information with one count of **filing a false claim** with SBA. This action resulted from an OIG investigation based on information provided by the Auditing Division. The businessman applied for a \$300,000 economic injury disaster loan following the 1992 Los Angeles civil unrest. The investigation disclosed that the application package included copies of fictitious individual income tax returns for the

businessman and a copy of a fictitious 1991 corporate income tax return. Relying on these documents, SBA approved and disbursed a \$109,300 loan that ultimately went into default without a single payment having been made.

Small Business Investment Companies

The primary business of **Small Business Investment Companies (SBICs)** is to provide a source of equity capital and long-term loans to new or expanding small businesses. SBICs are profit-making corporations that make investments in small businesses. SBICs finance small firms in two general ways: (1) straight loans and (2) equity-type investments which give the SBIC actual or potential ownership of a portion of a small business' equity securities. Many SBICs also provide management assistance to the companies they finance.

SBA licenses, regulates, and provides financial assistance to SBICs, which are privately owned, operated, and capitalized. The Small Business Investment Act (SBI Act), as amended, authorizes SBA to purchase or to guarantee the timely payment of all scheduled interest and principal on debentures issued by such companies. Under Section 301(d) of the SBI Act, SBA also licenses **Specialized SBICs (SSBICs)** to help those small businesses owned and managed by socially or economically disadvantaged persons. As of the end of FY 1996, there were 282 licensed, active SBICs, including 88 SSBICs, with private capital of \$4.5 billion and leverage of \$1.4 billion for total capital of \$5.9 billion. In addition, there were 166 SBICs in liquidation owing SBA an estimated \$320 million. In FY 1996, the program level for investment companies, including participating securities, was \$374 million.

The SBI Act generally requires that all SBICs licensed by SBA be examined every 2 years to ensure licensee compliance with law and Agency regulations. The Small Business Credit and Business Enhancement Opportunity Act of 1992 transferred the responsibility for examining SBICs from the OIG to the Agency effective October 1, 1992. While SBA's Investment Division is now responsible for these examinations, the OIG continues to have authority to audit the SBIC program pursuant to its responsibility to oversee all Agency programs and activities.

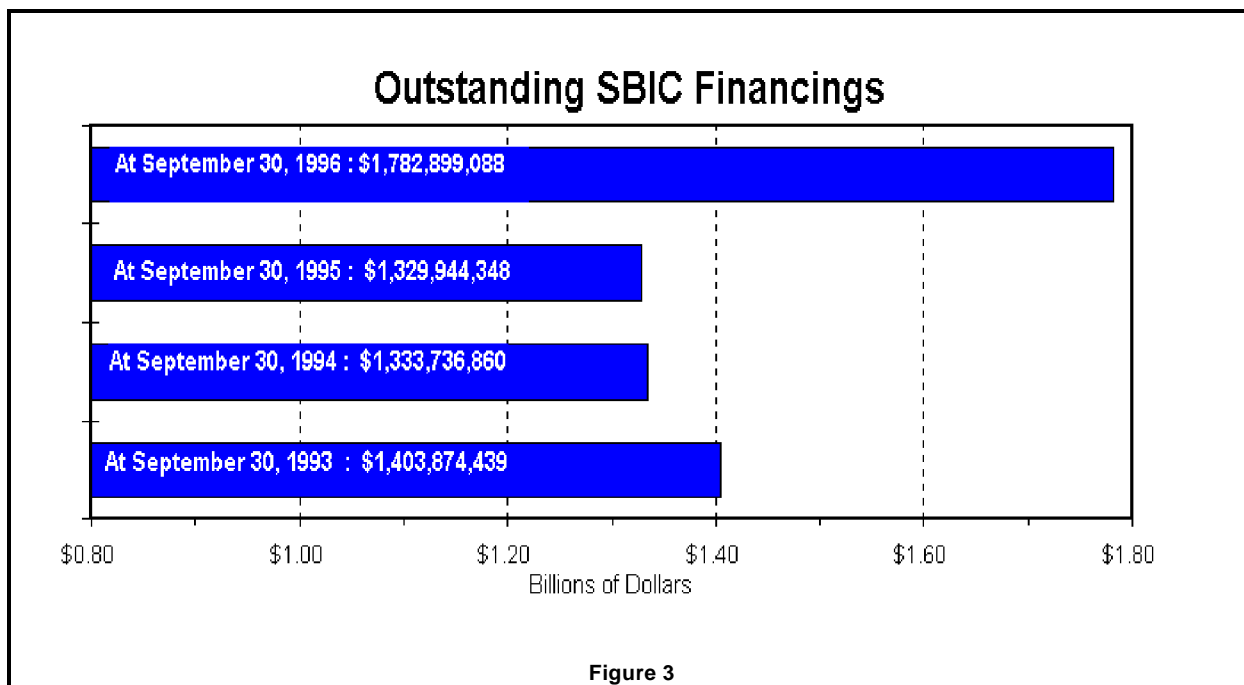
Summary of OIG Activity

The following summarizes OIG activities relating to the SBIC program during the reporting period:

- Two SBIC investigations were closed, leaving an inventory of 11 active cases involving 32 subjects. Three SBIC cases continued to be monitored which, due to

workload demands, had previously been referred to another law enforcement agency for investigation.

- One proposed piece of legislation and two proposed regulations were reviewed.



Efforts to Improve SBA Program Management

Review of Small Business Investment Act Amendments

The OIG reviewed H.R. 3720 (a bill to amend the Small Business Investment Act of 1958) and commented on two provisions. First, the bill allows an SBIC to include, as part of its private capital, ". . . unfunded binding commitments . . . to contribute capital to the licensee." The bill provides some limits by requiring that such investors meet certain criteria to be set by the Administrator. It also specifies that such commitments may not be used as a basis for actually funding leverage. The OIG is concerned, however, that this provision, if enacted, could unnecessarily increase the risk of admitting potentially underfunded SBICs to the program.

Second, the bill would require SBA to provide each applicant with a written report detailing the status of its application within 90 days of its filing. The OIG does not see the need for this requirement and, in view of SBA's constrained staffing outlook, believes that it could result in even more delays in processing such applications.

Review of SBIC Regulations

The OIG reviewed a proposed amendment to Part 121.103(b)(5) that would provide an exemption from the affiliation requirements for investors who coinvest with SBICs, as long as the small business concern retains an entrepreneurial group that has a 10% ownership interest. Under the proposal, a group of investors and SBICs could own up to 90% of a small business concern and not be considered affiliated entities; neither would they be presumed to control the small business.

In the absence of a well-documented empirical basis for this proposal, the OIG expressed concern with the proposed amendment's contentions that all or a great majority of the ownership interest in a business does not equal control, that major co-owners would not collaborate in controlling a firm, or that controlling interests by large entities have no bearing on a firm's status as a small business. In short, the proposal does not appear to be consistent with the principle that a small business concern be independently-owned and operated. To allow a small business to be 90%-owned by SBICs and investors would serve to deprive that firm of control of its operations, which would not be in its best interest.

The OIG also noted that the proposed change in the SBIC affiliation rules could lead to a similar change in other SBA program areas, as SBA rethinks the relationship between the concepts of ownership and control of a business. Because of this possibility, the OIG recommended that this proposal be given a comprehensive review by other program offices.

Surety Bond Guarantees

Small and emerging contractors who cannot get surety bonds through regular commercial channels can apply for SBA bonding assistance under the **Surety Bond Guarantee Program**. Under this program, SBA guarantees a portion of the losses sustained by a surety company as a result of the issuance of a bid, payment, and/or performance bond to a small business concern.

Businesses in the construction and service industries can meet the SBA's size eligibility standards if their average annual receipts (including those of their affiliates) for the last 3 fiscal years do not exceed \$5 million. Any contract bond is eligible for SBA guarantee if the bond is covered by the Contract Bonds section of the Current Manual of Rules, Procedures and Classifications of the Surety Association of America, required by the invitation to bid or by the contract, and executed by a surety company that is determined by SBA to be eligible to participate in the program and certified acceptable by the the Department of the Treasury.

The **Preferred Surety Bond (PSB)** program allows selected sureties to issue, monitor, and service surety bonds without SBA's prior approval. SBA accomplishes two primary objectives through this program: (1) expanding the number of sureties participating in the surety bond guarantee program, and (2) increasing bonding availability to business concerns that would otherwise not be able to obtain bonding in the standard marketplace. Title II of Public Law 100-590 also requires an annual audit of each surety participating in this program.

SBA can guarantee bonds for contracts with a face value of up to \$1.25 million. In FY 1996, SBA contingent liability for new final bond guarantees, including those issued under the PSB program, was \$724 million. The appropriated guarantee authority level for FY 1996 surety bond guarantees was \$1.767 billion; in FY 1997 it is \$1.767 billion.

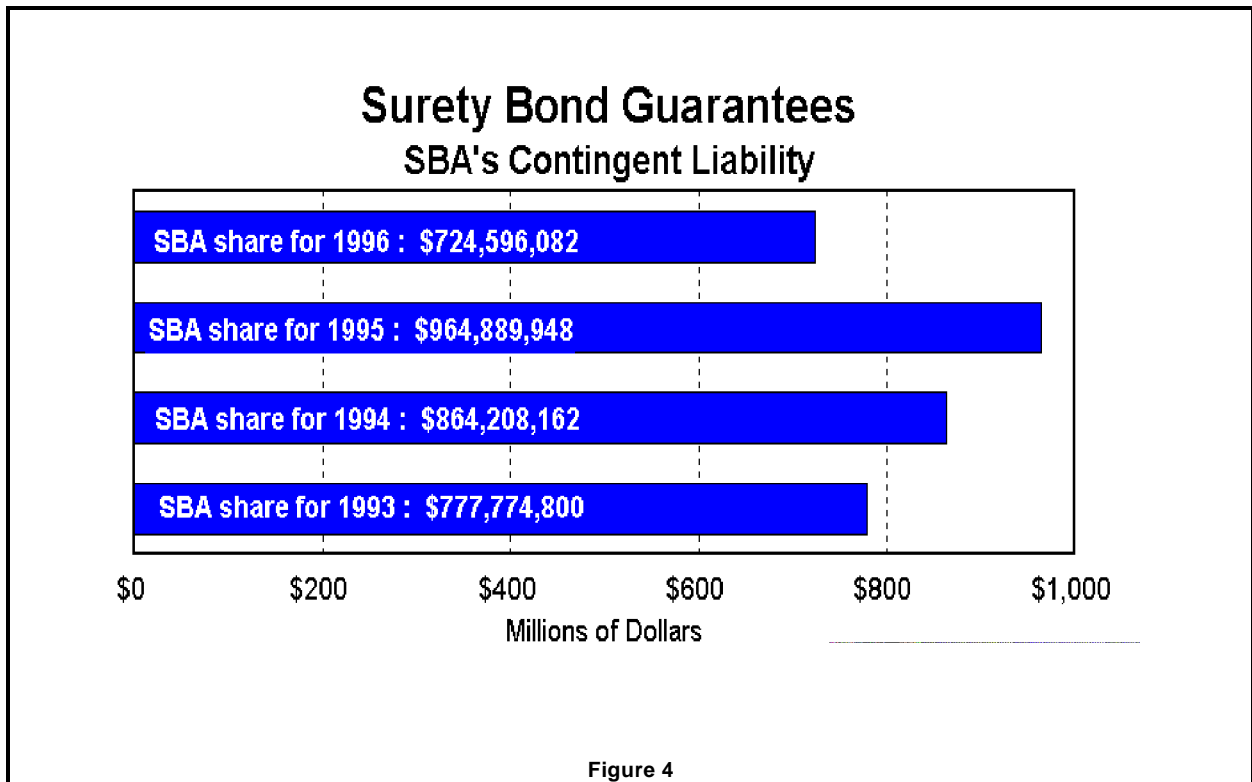
Summary of OIG Activity

The following summarizes OIG activities relating to SBA's surety bond guarantee program during the reporting period:

- One audit of a surety is underway.
- No inspection reports were issued during this period, but follow-up was conducted on the results of a previous inspection.
- One surety bond investigation remained active at the end of the

reporting period.

- One surety bond investigation continued to be monitored. Due to workload constraints, it had previously been referred to another law enforcement agency for investigation.



Government Contracting Programs

SBA provides assistance to small businesses in obtaining a fair share of Federal Government contracting opportunities. SBA also works with each department or agency to establish procurement goals for contracting with small, small-disadvantaged, and women-owned businesses. The Agency's government contracting programs include **Prime Contracts, Subcontracting Assistance, Certificate of Competency, Natural Resources Sales Assistance,** and the **Procurement Automated Source System.**

The goals of the **Prime Contract Program** are to increase small business opportunities in the Federal acquisition process and to expand full and open competition to effect savings to the Federal Government. Supporting initiatives are carried out by traditional and breakout procurement center representatives assigned to major Federal acquisition activities.

The **Subcontracting Assistance Program** promotes the optimal use of small businesses by the Government's large prime contractors. This is carried out by commercial market representatives who monitor the procurement activities of the large prime contractors.

The **Certificate of Competency (COC) Program** provides an appeal process to assure that small business concerns, especially those new to the Federal procurement market, are given a fair opportunity to compete for and win Government contracts. If a small business is the successful offeror on a contract but is found non-responsible, it can appeal to SBA. After reviewing a firm's capabilities, SBA can issue a COC that requires the contracting officer to award the contract to that business.

Natural Resources Sales Assistance helps small businesses obtain a fair share of Federal property offered for sale or disposal, with a focus on sales of Federal timber, royalty oil, coal leases, and other mineral leases.

The **Procurement Automated Source System (PASS)** is SBA's computerized inventory of U.S. small businesses that are interested in Federal procurement opportunities, either directly with the Government or with prime contractors. Both Federal agencies and large prime contractors use PASS as a resource in identifying small businesses for procurement opportunities.

Summary of OIG Activity

The following summarizes OIG activities relating to SBA's Government contracting programs during the reporting period:

- Government contracting investigations produced a \$32,500 recovery by SBA.
- One Government contracting investigation was closed; seven others were active involving 16 subjects.
- Due to workload constraints, one additional Government contracting case was referred to another law enforcement agency for investigation, giving the OIG a total of two Government contracting referrals to monitor.
- Two proposed regulations were reviewed, as were six Standard Operating Procedures (SOP).

Efforts to Improve SBA Program Management

Review of Government Contracting SOPs

As part of SBA's initiative to update and streamline its SOPs, the SBA/OIG reviewed proposed revisions to six government contracting SOPs and commented on several. In reviewing SOP 60 03 5, Subcontracting Assistance Program, the OIG commented on purchase order analyses, outside resources, contractor ratings, and subcontractor of the year award procedures.

The review of SOP 60 04 4, Certificate of Competency Program, led to comments to clarify the "significant portion" requirement, "cost of materials" definition, joint ventures, contractor contacts, and integrity referrals. Finally, in reviewing the Prime Contracts Program procedures (SOP 60 02 6), the OIG commented on the locations of procurement center representatives (PCRs) and consultations between PCRs and contracting officers.

Review of Department of Defense's Nonmanufacturer Rule

The OIG reviewed a proposed rule that would amend the Defense Federal Acquisition Regulation Supplement (DFARS) to include a new definition of "nonmanufacturer" for use with the Department of Defense's (DOD) small and disadvantaged business set-aside program. The OIG objected to the proposed definition as it significantly varies from the definition of "nonmanufacturer" used by SBA in its small business size standards, and the prior approval by SBA to a variance, as required, has been neither requested nor given. DOD, in proposing this change, has not explained why the SBA size standard is not appropriate and has not provided any reasons as to why the proposed change would better meet its needs. In addition, the proposed DFARS definition is inadequate in that it does not specify the number of employees an employer may have to be eligible as small nor does it specify that the end item of a small business manufacturer must be supplied. Finally, we noted that because the DFARS and SBA definitions differ significantly from each other, adoption of the DFARS proposal is likely to cause

confusion for small businesses involved in the Federal procurement arena. The Agency incorporated the OIG's objections into its opposition to the proposed DOD rule.

Activities to Enhance Fraud Detection and Deterrence

Latest Result From Affirmative Civil Enforcement (ACE) Program

During this period, the OIG's participation in the Department of Justice's ACE program produced another result in the Government contracting area. A Uniontown, Pennsylvania, dairy agreed to pay the Government \$32,500 to settle (while denying any fraud) a civil action filed by the U.S. Attorney's Office for Eastern Pennsylvania under the False Claims Act. An OIG investigation had disclosed that the firm **falsely certified** that it was eligible to bid on Government contracts set aside for small businesses. The dairy's owner was awarded contracts to provide dairy products to Fort McNair, Andrews Air Force Base, and Bolling Air Force Base after falsely certifying that, together with its affiliated companies, it had fewer than 500 employees. In fact, the dairy's owner was affiliated with three companies, with total reported net sales of \$160 million and total number of employees exceeding 500; therefore, it was formally judged by SBA to be ineligible for small business set-aside contracts. The owner nevertheless continued to bid on and obtain such set-asides, submitting to the Government at least 686 false claims for reimbursement totaling \$483,671. This matter was referred to the OIG by the Office of Government Contracting's Area II Office.

This is the fourth Government Contracting case to generate an Affirmative Civil Enforcement settlement. Each involved a contractor who disregarded SBA's eligibility determination and bid on subsequent set-aside contracts for which he was ineligible. Because contracting agencies have no effective way of knowing whether SBA has deemed a company too large for set-aside contracts within certain industries, they have sometimes awarded contracts to ineligible businesses as a result of relying on false self-certifications. In FY 1995, the OIG issued a Program Vulnerability Memorandum suggesting that SBA periodically generate a list of companies found ineligible to self-certify as small and circulate it to all Federal agencies. Although the Assistant Administrator for Government Contracting rejected the suggestion by stating that such a listing would be unable to keep pace with SBA's recertification process, the OIG continues to believe that this practice would prevent a substantial number of fraudulent awards and preclude many size appeals. Any company on the list could rebut the presumption of ineligibility by presenting SBA's recertification to the procuring agency.

Minority Enterprise Development

Section 7(j)(10) of the Small Business Act established the **Minority Small Business and Capital Ownership Development Program** for the purpose of promoting greater access to the free enterprise system for socially and economically disadvantaged individuals. Under the Act, SBA provides business development assistance to small business concerns that are at least 51 percent unconditionally owned, controlled, and managed by one or more socially and economically disadvantaged individuals and that meet other eligibility requirements. Firms may participate in the program for a maximum of 9 years and must take steps to enhance their competitiveness during this period to be prepared to compete in the private sector upon graduation from the program.

One of the business development tools available to participant firms is access to Federal contracting opportunities authorized by **Section 8(a)** of the Small Business Act. Under the Section 8(a) program, SBA contracts with other Government agencies to provide goods and services, and subcontracts the performance of these contracts to program participants. As of September 30, 1996, there were more than 5,800 approved program participants. In FY 1996, Section 8(a) program participants received between 5,400 and 5,600 contracts and between 23,000 and 25,000 modifications with an aggregate value estimated between \$5.4 and \$5.8 billion. Generally, Section 8(a) contracts with estimated values, including all options, of more than \$5 million (manufacturing) or \$3 million (all other industries) must be competed among eligible Section 8(a) program participants. The vast majority of the contracts awarded under the program, however, have estimated values below these thresholds and are awarded on a sole-source basis.

Under the **Section 7(j) Management and Technical Assistance Program**, which is housed in the Office of Minority Enterprise Development, SBA provides specialized training, professional consultant assistance, and executive development to certified Section 8(a) firms, socially and economically disadvantaged individuals whose firms are not participants in the Section 8(a) program, low-income individuals, and small businesses located in areas of low income or high unemployment.

There are over \$9 billion in Section 8(a) subcontracts currently outstanding and subject to OIG audit, inspection, and investigation oversight activities. These contracts are reflected in other Government agencies' portfolios; therefore, their values are not included in our almost \$35 billion audit, inspection, and investigation universe.

Summary of OIG Activity

The following summarizes OIG activities relating to SBA's minority enterprise development (MED) programs during the reporting period:

- Three audit reports in MED were issued.
- MED investigations resulted in 2 convictions and produced \$10,000 in court-ordered restitution, \$26,100 in fines and special assessments, and a \$1,227,000 reduction in financial risk.
- Office of Security Operations name checks resulted in the declination of 3 applications for the Section 8(a) program.
- Five MED investigations were closed, leaving an inventory of 13 active cases involving 46 subjects. Due to workload demands, one other case was referred to another law enforcement agency for investigation, and at the end of the reporting period we still had ten MED referrals to monitor.

Efforts to Improve SBA Program Management

Audit Uncovers Unauthorized Contract Brokering by Section 8(a) Firm

A recent audit found that a Section 8(a) company filled an office supplies contract by brokering the entire procurement to other

firms who drop-shipped the orders directly to the procuring agency. In such cases, the SBA/OIG stated in an audit-related memorandum dated August 21, 1996, the Section 8(a) firm added no value and did not prepare for competitive business development, while the Government was not assured fair market pricing.

SBA regulations require that a Section 8(a) firm be a manufacturer or regular dealer in items supplied to the Government, referring to the requirements of the Walsh-Healy Act. Although that Act has been amended to eliminate the section on "regular dealers," the MED program office and the Office of General Counsel have both stated that it would still be appropriate to apply the standards of the Walsh-Healy Act to the Section 8(a) program. The OIG thus recommended that the definitions in the Agency's procedures be clarified to accommodate the Walsh-Healy amendments. Further, although "brokers" and "packagers" are ineligible under SBA regulations, these terms are not defined.

The Associate Administrator for Minority Enterprise Development (AA/MED) generally concurred with the findings of the report and drafted a procedural notice addressing the recommendation. SBA will clarify the Section 8(a) procedures to require firms to be established wholesalers and retailers in the products they sell to the Government. The Section 8(a) contractors will also have to supply the products of a small firm, if available. These requirements will aid firms in developing their businesses, while preventing pass-through contracts in products that the firms do not normally sell.

It will also preclude the passing through of contracts to large businesses.

Audit of Florida Section 8(a) Firm Yields Recommendation to Restrict Use of Basic Ordering Agreements

The OIG recommended restrictions on the **use of basic ordering agreements (BOA) by Section 8(a) companies**. Under present procedures, BOAs can result in unlimited sole source awards to a company, undermining statutory competitive thresholds. The OIG recommended (1) limiting the dollar amount of sole source BOA delivery orders to regulatory competitive thresholds--\$5 million for manufacturing and \$3 million for other SIC codes--and (2) limiting SIC codes in a BOA to one major group. These recommendations were contained in a follow-up report to an audit of a Fort Walton Beach, Florida, Section 8(a) firm that obtained sole-source delivery orders in excess of \$29 million under one BOA in force from 1992 to 1994. In two instances, delivery orders were split to avoid competitive thresholds. The audit concluded that SBA procedures permit BOAs to be used to thwart the competitive business development purposes of the Small Business Act. Because each BOA delivery order is treated as a separate contract, there is no limit on the aggregate value of orders, the SIC codes used, or the number of procuring agencies that can use a single BOA. Some BOAs include both services and supplies, which have different SIC codes and different competitive thresholds. The AA/MED agreed with the recommendation.

Activities to Enhance Fraud Detection and Deterrence

Illinois Construction Company President and Accountant Sentenced for Obstruction of Justice

The president of a Section 8(a) construction company in Villa Park, Illinois, and the company's accountant pled guilty to one count of **obstruction of justice**. The president was sentenced to 6 months home detention, 3 years probation, a \$25,000 fine, and \$10,000 restitution. The accountant was sentenced to 3 years probation and a \$1,000 fine. The OIG's joint investigation with the Air Force Office of Special Investigations (AFOSI) revealed that in 1990-1991 the two men submitted fraudulent claims to SBA and the Air Force pertaining to a Section 8(a) contract for landscaping on the Air Force Reserve Facility at O'Hare International Airport. During the course of the subsequent investigation, both provided false testimony to a Federal grand jury and attempted to tamper with witnesses whose testimony was to be presented to the grand jury. The AFOSI asked the OIG to join the investigation.

California Section 8(a) Company Accounting Manager, Trustee, and CEO's Administrative Assistant Sentenced

Sentences were imposed for the three remaining defendants of a group of ten who entered guilty pleas following the OIG's participation in a Federal task force investigation of a Section 8(a) company with offices in Los Angeles and Houston. The firm's former accounting manager and a

trustee of a trust created by the chief executive officer (CEO) and his wife both pled guilty to one count of **violation of National Aeronautics and Space Administration (NASA) security regulations**. Both were sentenced to 6 months supervised probation and 120 hours community service. The CEO's administrative assistant, who had also pled guilty to one count of **conspiring** with the firm's CEO and others to file false claims for payment by NASA under various subcontracts, was sentenced to 3 years probation and 180 hours community service. The CEO had used the trust and three other associated corporations to bill inflated rents and other expenses to NASA subcontracts, including a Section 8(a) contract initiated in 1981 for \$4.4 million and extended through December 1989 with additional charges of \$6.4 million. Also included in the conspiracy were a series of materially false statements, regarding the existence of the firm's San Diego office, that were made to secure and maintain Section 7(j) cooperative agreements totaling more than \$60,000. The SBA/OIG was asked by the NASA/OIG to join the task force, which also included the IRS, the Postal Inspection Service, the FBI, the Defense Contract Audit Administration, the Department of Labor's Office of Labor Racketeering, and its Pension and Welfare Benefits Administration.

OIG Auditor and Criminal Investigator Receive Special U.S. Attorney Awards

The U.S. Attorney's Office for the Southern District of Texas recently issued special commendations to Donald Ward, an auditor in the OIG's Los Angeles Field Office, and Cheryl Jones, a special agent in the OIG's

Dallas Resident Office, for their outstanding performance, dedication, and professionalism in the investigation of a contractor supporting the space shuttle program at the Johnson Space Center. The awards were presented by U.S. Attorney Gaynelle Griffin Jones in Houston, Texas.

Ms. Jones was SBA's primary investigator, and Mr. Ward was one of two auditors who worked with a large multi-agency task force, headed by the NASA/OIG, to uncover and successfully prosecute 5 individuals and 5 companies for defrauding NASA or SBA. The case resulted in the largest fraud indictment and conviction in NASA's history, with potential fines and recoveries totaling approximately \$12 million.

Pennsylvania Construction Company Suspended from Section 8(a) Program, \$1.2 Million in Contracts Rescinded

The award of pending Section 8(a) contracts totaling \$1,227,000 to a Pennsylvania construction company was rescinded because of an OIG investigation report. The company was suspended from the Section 8(a) program after the investigation determined that the company's entry into the program had been approved based, in part, on **fictitious corporate and individual income tax returns** submitted to SBA. Each rescinded contract was awarded to another Section 8(a) contractor. Following an appeal, the company's suspension was reversed.

Economic Development (Business Education and Training)

SBA provides assistance to small business owners, managers, and prospective owners through its many counseling and training programs. SBA established the **Small Business Development Center (SBDC)** program to make management assistance and counseling widely available. SBDCs offer one-stop assistance to small businesses by providing a wide variety of information and guidance in easily accessible locations. The program is a partnership between the private sector; the educational community; and Federal, State, and local governments. There are SBDCs in all 50 states, the District of Columbia, Puerto Rico, the Virgin Islands, and Guam, with nearly 1,000 subcenters or service locations located at colleges, universities, vocational schools, chambers of commerce, economic development corporations, or downtown storefronts. In FY 1996, SBDCs provided counseling and training to nearly 570,000 clients.

The **Service Corps of Retired Executives (SCORE)** is another of the valuable business development resource partners of SBA. Composed of approximately 13,000 volunteers working in over 700 sites, SCORE provides counseling and training to current or prospective business persons. Counseling sessions are free to the public and training is provided at a low cost. Over 27,000 clients were assisted in FY 1995.

The vast majority of SBA business development and education activities in the areas of training, counseling, and providing management information materials occur through outreach efforts with external organizations. **Cosponsorship** arrangements, authorized under the Small Business Act, play a key part in this process. The Act gives SBA the authority to cosponsor training and counseling activities for small business concerns with non-profit entities and/or with other Federal Government agencies. In addition, the Act authorizes the Agency to cosponsor training, but not counseling, with for-profit concerns.

Business Information Centers (BICs) provide business owners with access to computers, software, databases, and other resources to assist them in starting and expanding their businesses. All BICs have at least one on-site counselor and can address the varied business start-up and growth issues encountered by small business owners. There are currently 37 BICs in operation.

Summary of OIG Activity

The following summarizes OIG activities relating to SBA's economic development programs during the reporting period:

- One audit report was issued in the economic development program area; one was in progress.
- Economic development investigations produced a \$517,721 reduction to the Agency's financial risk and one investigation remained active at the end of the reporting period.
- Six Standard Operating Procedures were reviewed.

Efforts to Improve SBA Program Management

Audit of Virginia Small Business Development Center (SBDC) Finds Variety of Non-Compliance Issues

An audit of the Virginia Small Business Development Center showed that **improvements are needed in expenditure controls and program matching funds.** The audit report questioned \$31,400 in unallowable costs and identified \$176,217 in overstated match. No repayment to SBA was necessary, however, because the SBDC had provided more than the required 50 percent match of private funds to Federal funds. The audit, requested by SBA's Associate Administrator for SBDCs (AA/SBDC), covered 2 of the 15 subcenters of the Virginia Department of Economic

Development. The unallowable costs included charges for equipment not yet obligated in 1994, airfare for a trip not taken, gift bags for an employee retreat, and employee parking permits. The match errors included unreasonable rates for a volunteer counselor, inadequate documentation, double counting of invoices, and miscalculations.

The OIG recommended that SBA take corrective actions for the specific findings as well as require the lead center to review the remaining 13 subcenters for similar problems. The Richmond District Director agreed to implement all recommendations.

Puerto Rico SBDC Terminated From Agency Program

Based on the findings of an initial audit (see Semiannual Report for the period April 1, 1995 to September 30, 1995) and a subsequent investigation, the AA/SBDC terminated SBA's cooperative agreement with the University of Puerto Rico program, ending that institution's participation in the Agency's SBDC program. The audit uncovered programmatic shortcomings including the insufficient provision of counseling, insufficient cash match funding, and excessive compensation and unauthorized expenditures. The investigation confirmed the findings of the audit and documented numerous additional unauthorized activities by specific individuals. A follow-up review by SBA's San Juan District Office prior to the termination revealed that little progress had been made in correcting areas of non-compliance. The AA/SBDC's letter to the institution cited ". . . widespread misuse of

Federal funds and disregard of . . . requirements . . . over a lengthy period of time. . . .” as the basis for the decision. Funding for the program in FY 1997 was slated to be \$1,035,441. The investigative findings have also been referred to the U.S. Attorney’s office for the District of Puerto Rico.

Agency Management and Financial Activities

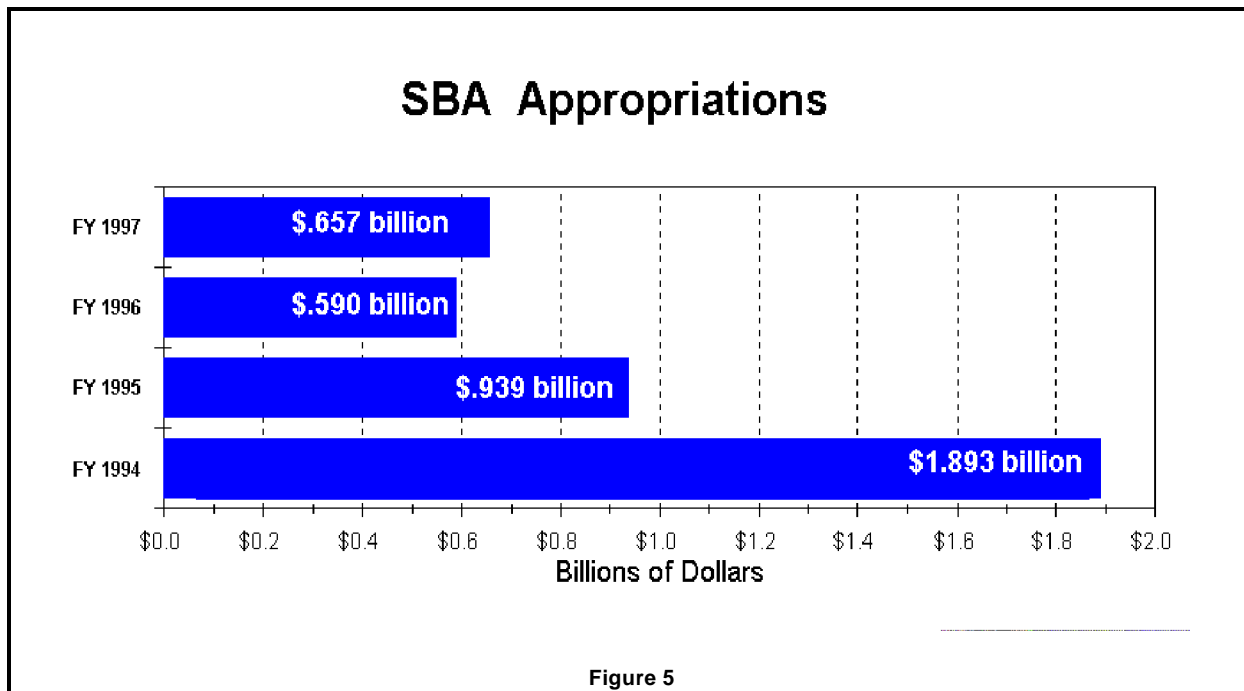
Agency **Management and Financial Activities** include SBA's administration of the loan programs, as well as the full range of internal administration and financial management operations. OIG audit, investigative, and inspection activities assist SBA managers by reviewing these operations and by conducting audits of Agency financial statements as required by the Chief Financial Officers Act, audits of cash management activities, and integrity assurance activities.

SBA's management and financial activities, represented by the Agency's total appropriation, involved about \$1.1 billion in FY 1996. Of this amount, \$589 million was for non-disaster related activities of the Agency. SBA's final FY 1997 appropriation has been enacted in P.L. 104-208, and includes \$852 million in new appropriations. Combined with carry-forward balances, and estimated recoveries, it provides an FY 1997 availability of about \$1.1 billion. Of this amount, \$657 million is for non-disaster related activities of the Agency.

Summary of OIG Activity

The following summarizes OIG activities relating to SBA's administration and financial management activities during the reporting period:

- Four audit reports on Agency activities were issued; two other audits were underway.
- One inspection survey report was issued.
- Integrity assurance investigations resulted in \$3,747 in court-ordered restitution and a \$1,632 recovery.
- Eleven integrity assurance investigations were closed, leaving an inventory of 18 active cases involving 28 subjects.
- Two integrity assurance investigations continued to be monitored. Due to workload constraints, they had previously been referred to other law enforcement agencies for investigation.
- Three proposed regulations, and 12 Standard Operating Procedures were reviewed.



Efforts to Improve SBA Program Management

Audit Expresses Qualified Opinion on FY 1995 Financial Statements

SBA's financial statements for FY 1995 received a **qualified opinion** in the annual independent audit because **SBA did not (1) maintain comprehensive inventory records of acquired property, (2) consistently value the acquired property at its net realizable value, and (3) reconcile certain fund balances with the U.S. Department of the Treasury.** The audit, required by the Chief Financial Officers Act of 1990, was performed for the SBA/OIG by the Certified Public Accounting firm of Cotton & Company.

The first two exceptions were repeats from the 1994 audit. Because of the lack of an automated inventory system with unit detail,

SBA could not reconcile the estimated \$140 million of collateral purchased property to its general ledger. A new computerized inventory system has been planned but not implemented. The valuation question was addressed in an SBA Information Notice in October 1994, but the auditors said the requirement for current appraisals of acquired property has not been consistently implemented. The Office of the Chief Financial Officer (OCFO) has indicated that detailed inventory records are maintained in SBA's field offices in paper format. The new system would provide this information in an automated format. SBA's OCFO advises that this system is planned for 1997. Also, extensive training conducted in 1996 addressed the valuation concern and will be considered in the 1996 audit. The OCFO reports that all issues have been addressed, and they will work with the auditors toward an unqualified opinion for the 1996 statements.

The third exception relates to online and offline loan accounting balances, which were \$32 million higher on SBA's books than on Treasury's. Monthly reconciliations are required by the Treasury Financial Manual, but the difference had not been reconciled at the time of the audit. SBA has retained a contractor to assist in the reconciliation and expected to become current by late 1996.

In the report on internal controls, the auditors classified the three problems with the financial statement as material weaknesses. Six other control weaknesses were reported, including: (1) computer passwords are known to persons other than the owner, (2) SBA lacks policies and procedures to verify that accounting transactions initiated by field offices are complete and accurate, and (3) SBA has not performed the required annual re-estimate of disaster loan subsidy rates since 1991. In the report on compliance with laws and regulations, the auditors found no material non-compliance with laws and regulations tested during the audit.

Management Letter Describes Six Internal Control Weaknesses

Six internal control weaknesses were reported in the management letter associated with the independent audit of SBA financial statements for 1995.

Three of the findings were repeated from the 1994 audit because SBA management had not fully implemented corrective actions. These concern the need for segregation of duties in the cash reconciliation process, the lack of security and efficiency reviews of local area network systems, and the lack of

valuations by certified real estate appraisers on collateral estimated at more than \$100,000.

The three new findings for 1995 are (1) inconsistency in applying Agency requirements in debt collection, with loans under \$15,000 not receiving intensive collection procedures; (2) non-implementation of some of the 12 findings of a June 1995 report by the Office of Government Ethics on SBA compliance with the Ethics in Government Act of 1978; and (3) lack of effective self-assessment of internal control weaknesses as required by the Federal Managers' Financial Integrity Act, with 14 of 17 reviewed district offices responded that they were not involved in the process.

SBA officials generally agreed with the findings and recommendations and have initiated corrective actions, working toward eliminating most, if not all, findings in time for the 1996 audit.

Inspection Survey Indicates That Inspector General Community Supports OIG Involvement in the GPRA Process

Under the auspices of the President's Council on Integrity and Efficiency (PCIE), the SBA and Treasury Department OIGs recently conducted a comprehensive survey of all Inspectors General (IGs) who are members of either the PCIE or the Executive Council on Integrity and Efficiency (ECIE). The survey's scope was designed to ascertain current and planned OIG involvement in the implementation of the Government Performance and Results Act (GPRA) within their host departments or

agencies, solicit IGs' views on the appropriate role of the OIGs in their agencies' GPRA process, and ascertain the status of strategic planning initiatives within individual OIGs.

Nearly all of the 27 PCIE IGs and about half of the remaining 27 ECIE IGs reported some involvement in their host agencies' implementation of GPRA. Most IGs plan to become more involved in the process over the next two years. The majority believed that OIGs should act in an advisory/consultative capacity in the Act's implementation stages but perform independent audits and reviews of results once GPRA has been fully implemented. There was no clear consensus that OIGs should focus resources on only one specific area. Most IGs, however, believed their offices should focus on a few primary activities, such as helping their department or agency to develop a strategic plan and performance measures to validate or assess results; and to perform audits, evaluations, and investigations.

While the survey did not ask whether the OIGs had the resources to take on the additional GPRA responsibilities, several IGs questioned whether they would have sufficient resources to support substantial involvement in their host departments' or agencies' GPRA process. Finally, we found that while nearly all IGs are engaged in internal OIG strategic planning, few have completed a full fiscal year cycle.

The report called attention to several issues that the PCIE may want to consider. First, do IGs have sufficient resources to take on additional GPRA responsibilities? Second,

is there a benefit in developing a common position within the community on an appropriate level of OIG participation in the implementation and review of GPRA activities? Finally, would clarifying the connection between Chief Financial Officer Act and GPRA activities help ensure the consistent use of standard performance measures? The PCIE found the survey's information useful and has addressed all questions raised.

Audit Discloses Contractor Altered Dates on U.S. Postal Service Forms

The OIG recommended denial of a mailing service contractor's final claim of \$142,659 on a \$568,000 contract that ran from 1989 to 1992. The recommendation was based on an audit by the Defense Contract Audit Agency (DCAA) for the OIG.

According to the audit, the contractor **altered dates on U.S. Postal Service forms** to obtain bonus payments for expedited delivery. DCAA also found that the firm's accounting system was not reliable because of internal discrepancies, missing invoices and supporting documentation, and duplicate invoices.

Review of General Accounting Office Management Reform Act of 1996

The OIG reviewed the Congressional draft bill entitled "General Accounting Office Management Reform Act of 1996" and commented on several of its provisions. Briefly, the legislation would change the term of office and annuity computations for the Comptroller General and his or her Deputy, establish an Office of Inspector

General (OIG) for GAO, and amend numerous laws authorizing GAO to audit and report on various Government functions.

Most of the OIG's comments pertained to the provisions establishing a GAO/OIG and recommended language changes that should be made in this bill as well as in the Inspector General Act itself at some future time. First, the office **recommended that the bill make clear the IG's authority to perform inspections and evaluations, activities that many established IGs have been conducting for years.** Second, the office noted that the bill provides that the GAO/IG have demonstrated ability in certain enumerated disciplines. We recommended that this list be expanded to include both the policy analysis and program analysis fields, in recognition of an OIG's inspection and evaluation responsibilities and the need for such expertise in the inspector general community. Finally, the bill provides that the Comptroller General may not, among other things, prevent the GAO/IG from carrying out an audit or investigation or from issuing a subpoena during the course of an audit or investigation. Again, in recognition of the inspector general community's ongoing inspection and evaluation activities, the SBA/OIG recommended that this language be revised and applied to the GAO/IG's inspection and evaluation activities.

Program Vulnerability Memorandum Issued on Regional Advocate Activities

During this reporting period, the SBA's Inspector General (IG) issued a program vulnerability memorandum (PVM) to the Chief Counsel for Advocacy (CCA). The

PVM was prompted by the actions of a Regional Advocate who, unaware that SBA has had a series of problems with a participating lender, issued press releases praising the bank's excellent small business lending practices. Following visits to several area banks, the advocate issued press releases recognizing them for their small business lending practices. He based his action on an Office of Advocacy analysis of reports filed by the banks with Federal regulators. The Office of Advocacy's analysis made no distinction, however, between SBA-guaranteed loans and regular commercial loans.

Unbeknownst to the Regional Advocate, SBA has had a series of problems with one of the banks. Because of a variety of questionable lending and servicing practices, the SBA district office declined to renew this bank's participation in the Certified Lender program in 1995. Moreover, the OIG has an ongoing investigation regarding one of this bank's SBA-guaranteed loans for which the bank and its president face possible legal action. Finally, on the same day the Regional Advocate issued the press releases, the district office made a written request to the bank president that he voluntarily release SBA from its guarantee on another loan because of numerous lending and servicing deficiencies by the bank. The district office has subsequently made an investigative referral to the OIG regarding this loan as well. Not surprisingly, the bank has cited the Regional Advocate's laudatory press release in its refusal to voluntarily terminate the SBA guarantee and will probably raise it again as SBA and the U.S. Department of Justice consider legal action.

The Office of Advocacy has no policy requiring Regional Advocates to check with other SBA offices prior to granting official recognition to participants. This lack of communication allowed the Agency to send contradictory messages to the bank in question.

The IG recommended to the CCA that, before making any public announcement of this sort, Regional Advocates should be required to contact the appropriate district office for any information related to the financial institution in question. Regional Advocates should also request a name check from the OIG's Office of Security Operations before making such announcements. These steps should ensure that potentially embarrassing situations such as described above are avoided in the future. As of the end of this reporting period, the CCA had not replied to the PVM, because the memorandum was issued late in the period.

Activities to Enhance Fraud Detection and Deterrence

OIG Conducts Employee Awareness Briefings

In addition to investigating complaints of waste, fraud, and abuse involving SBA programs, OIG Investigations Division staff presented 16 **Standards of Conduct briefings** to a total of almost 700 **Agency employees**. The involvement and cooperation of all SBA employees in combating waste, fraud, and abuse is critical to an effective OIG investigations program and to the Agency's overall productivity and efficiency.

During the reporting period, employee contributions to our mission were significant. As Figure 6 shows, more than 61 percent of all investigative referrals originated from within the Agency, in the form of referrals either from program heads or from other SBA employees. This cooperation indicates the strong commitment of SBA employees to reducing waste, fraud, and abuse in Agency programs and improving the Agency's management and control of its programs.

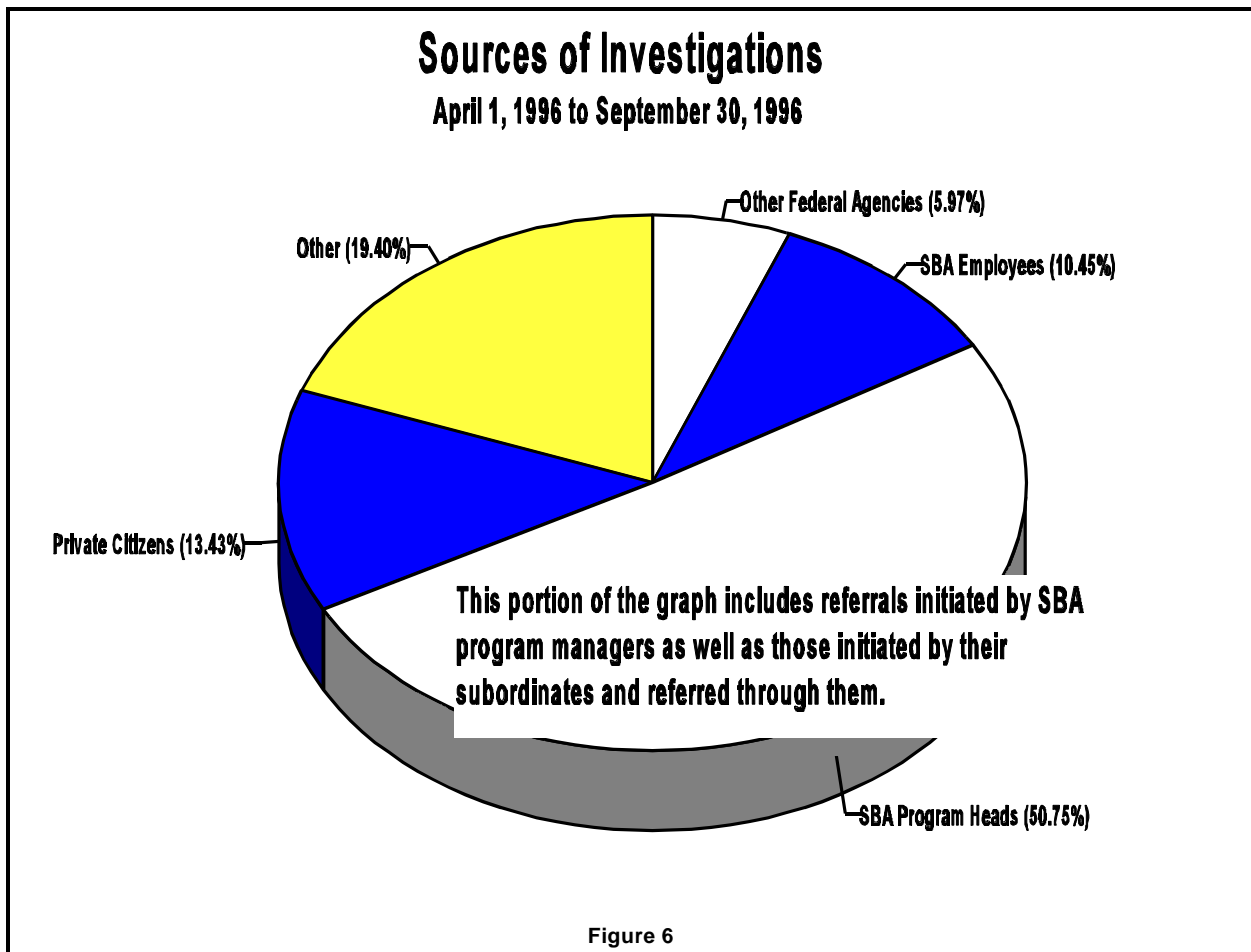
Former SBA Employee Sentenced for Conversion of Government Property

A former clerk with the Disaster Assistance Area 4 Office, Sacramento, California, was sentenced to 30 days home detention, 5 years probation, and \$3,748 restitution. He previously pled guilty to one count of **conversion of Government property** to personal use. A joint OIG/Federal Protective Service investigation of the man was initiated based on information provided by the Area 4 Office. It determined that, without authorization, he obtained a rented automobile, paid for by SBA, and used it exclusively for personal business. Area 4 officials became aware of his behavior when the employee was involved in an accident with the vehicle.

OIG Criminal Investigator Receives Special U.S. Attorney Award

The U.S. Attorney's Office for the Eastern District of Pennsylvania issued a special commendation to Nicholas Carroll, a special agent in the OIG's Philadelphia Resident Office, for his outstanding performance, dedication, and professionalism in an

investigation that resulted in the ordered payment of \$1,526,893 by a tax return preparer in restitution to the dozens of individuals he had defrauded using SBA's name. The award was presented by U.S. Attorney Michael R. Stiles. Mr. Carroll was SBA's primary investigator of a case in which the tax preparer defrauded more than 50 investors, many of them elderly, by selling them approximately \$1,143,000 of bogus tax-free municipal bonds purportedly guaranteed by SBA.



Organization, Resources, and Management Initiatives

The two missions of the Office of Inspector General are to help improve management in the Agency and to detect and deter fraud in SBA's programs. These dual missions are accomplished through the provision of audit, investigation, and inspection and evaluation oversight to the Agency's portfolio and programs. This chapter provides an overview of the OIG's organizational structure and personnel and budget resources and summarizes key internal management initiatives to use those resources as effectively as possible.

Organization

The OIG is organized into four divisions as follows:

- Auditing Division
- Investigations Division
- Inspection and Evaluation Division
- Management and Legal Counsel Division

The Auditing and Investigations Divisions each administer their field activities through field offices and resident offices around the country. The Auditing Division has offices located in Atlanta, Dallas, Los Angeles, and Washington. In addition to these cities, the Investigations Division has offices in Chicago, Denver, Houston, Kansas City, New York, Philadelphia, San Francisco, Seattle, and Syracuse. The Investigations Division's Office of Security Operations is located in Washington, D.C.

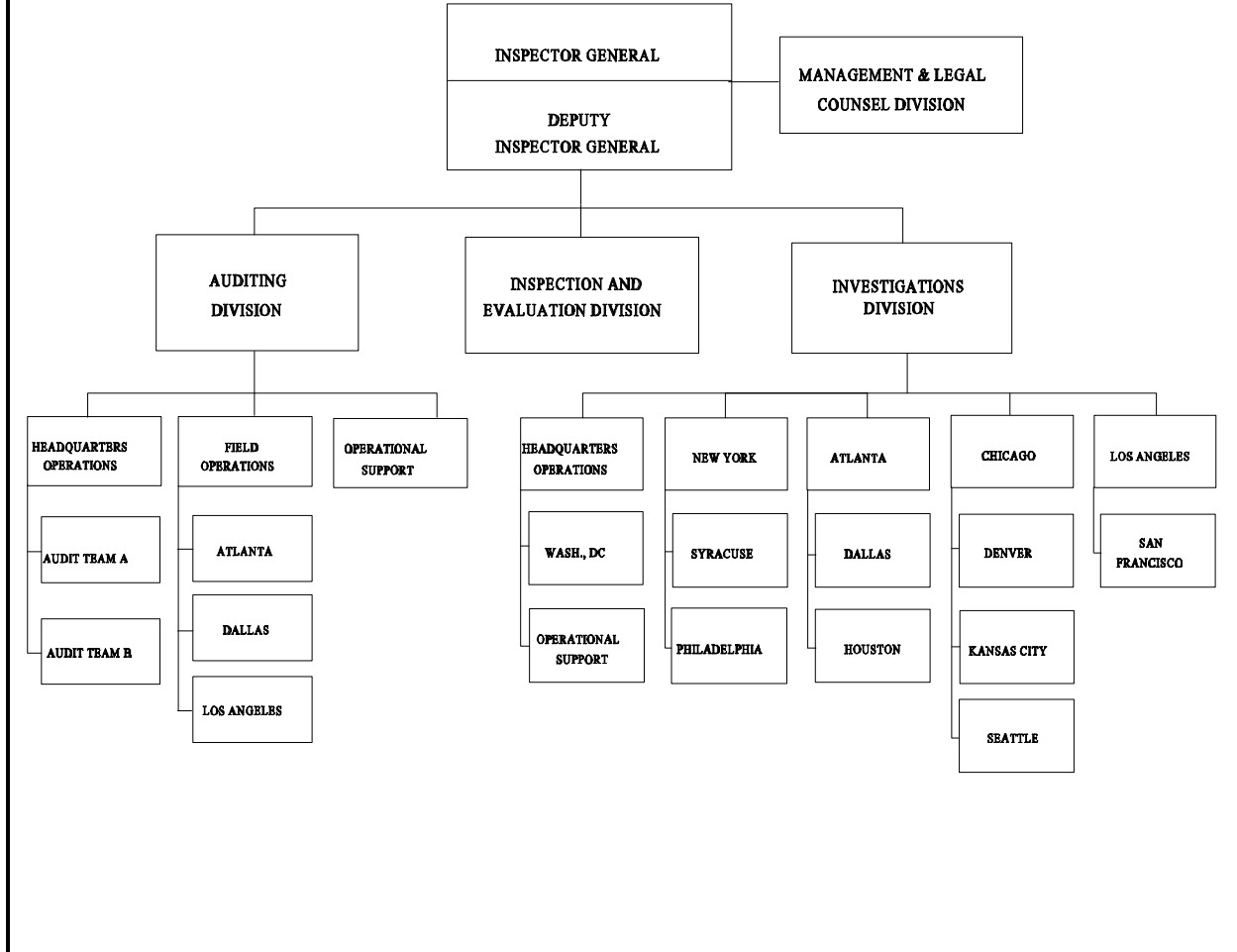
Both the Inspection and Evaluation Division and the Management and Legal Counsel

Division operate out of Washington, D.C. A current OIG organization chart can be found at Figure 7.

Resources

In FY 1996, the OIG operated under a series of congressional Continuing Resolutions (CR) at an annualized funding level of \$8.5 million and an authorized personnel ceiling of 102 full-time equivalent (FTE) positions. While this level of funding represented the same number of dollars as appropriated in FY 1995, it was not able to support OIG activity at the FY 1995 operating level. Uncontrollable expenditures such as congressionally-mandated law enforcement availability pay, annual cost of living increases, and various locality pay adjustments were not reflected in the CR spending levels. In early April, the OIG was forced to request a transfer of funds from the SBA to ensure that ongoing operations could be funded. The SBA Administrator transferred \$200,000 in May to the OIG's appropriation, enabling the OIG to avoid

OFFICE OF INSPECTOR GENERAL SMALL BUSINESS ADMINISTRATION



uncompensated furloughs of its staff and to carry out other priority activities. Even with this transfer of funds, the OIG ended the fiscal year with an average FTE of just over 98, or 4 positions under its authorized ceiling.

In FY 1994, the OIG also received \$3 million in supplemental “no year” disaster funds to be used for activities related to the

Agency's vastly expanding disaster assistance program; these funds will remain available until expended (see discussion below). By the end of the current reporting period, six auditors, five investigators, one attorney, and two secretaries had been hired on temporary appointments using disaster funding.

Funding will continue to be problematic in

FY 1997, even though the Congress has appropriated \$9 million in funding for the OIG and authorized the Administrator to transfer an additional \$500,000 to support OIG's disaster oversight activities. The nature of the funding for disaster oversight forces the OIG to pursue recruitment of disaster-funded auditors and investigators on a "non-permanent" basis. Temporary employees are understandably quick to pursue more permanent positions elsewhere, and the OIG is deprived of the expertise that they would otherwise develop through their longevity with the OIG.

The continuing reduction in OIG FTE resources remains troubling. As depicted in Figures 1 and 2, the expanding nature of the Agency's portfolio and its concomitant demand for OIG oversight would suggest that resources be increased (not reduced) to ensure adequate oversight. In recognition of this need, the President had requested \$9.985 million for the OIG for FY 1997. With the resources made available in the FY 1997 appropriation, the OIG will again find it difficult to carry out its mandate to provide oversight to the Agency's programs and activities and to safeguard the Government's investment in the extensive credit programs of the Agency.

The OIG continues to be concerned with the strong demand for investigations of fraud in Agency programs. As evidenced by the table on page 61, both business loan and disaster loan fraud continue to be our major areas of concentration, in terms of both active cases carried and time expended on those cases. This reporting period continued the high share of investigative time (79.5 percent) expended on business and disaster

loan fraud cases. With demand for SBA business and disaster loans remaining high, we expect that our investigative efforts will continue to be preoccupied by those two programs and our resources stretched severely. The table on page 61 also illustrates the Auditing Division's emphasis on the business loan and disaster assistance programs. This is demonstrated by the Auditing Division's effort in the disaster assistance program, which has gone incrementally from 3 percent to 26 percent over the last 5 reporting periods. The OIG is, of course, also greatly concerned by the meager coverage it is able to provide to other Agency programs, supporting activities, and program participants. It has been unable to provide audit oversight of the Agency computer systems, and it has been virtually unable to respond to specific Agency requests for audit coverage. Key programs such as Section 8(a) have also gone with minimal audit oversight during the past year. Other programs such as Small Business Investments Companies have had no OIG oversight.

Management Initiatives

The OIG Enters CyberSpace

The OIG has joined the Internet communications revolution as a new channel for distributing news of OIG activities. The OIG home page on the World Wide Web

tells the public how to contact the OIG and gain access to its audit, inspection, monthly activity, and semiannual reports. The SBA/OIG's homepage also contains a host of other informational items such as the description of the OIG's mission, its office locations, and testimony by office principals.

The OIG homepage is part of IGnet, an Internet network housed at SBA and serving the inspector general community of auditors, investigators, and inspectors at the Federal, State, and local government levels, as well as educational, non-profit, and private sector organizations. The goals of the IGnet are to (1) promote public access to IG information and (2) provide information and communication tools for community professionals. In addition to OIG reports, IGnet contains pages on the Government's Single Audit program, job opportunities, training opportunities, and a

variety of Internet search tools.

What's New on IGnet?	
The IG Community	IGnet Services
IG Information	Virtual Library
IG Directory	• Internet Resources
IG Community Manual	• Internet Searching
PCIE	Single Audit Library
News of the IG Community	Job Opportunities
	Training Information
	Mailing Lists

HOW TO REACH US ON THE INTERNET:

SBA OIG's home page:
<http://www.sbaonline.sba.gov/IG>

IGnet home page:
<http://www.sbaonline.sba.gov/ignet>

OIG Conducts Annual Training in Washington, D.C.

The OIG conducted its **annual training conference** at SBA's Central Office in Washington, D.C., during the week of July 8, 1996. Participants heard "state of the

OIG” remarks by the Inspector General, as well as presentations by Administrator Philip Lader and Deputy Administrator Ginger Lew. Sessions attended by OIG auditors and inspectors included Surety Bond and SBIC program updates presented by SBA program officials, ADP information presented by SBA’s Office of Information Resource Management, statistical sampling techniques, and report referencing. All OIG conference participants attended program updates on the Agency’s Economic Development programs, the Section 8(a) program, and the Disaster Assistance program; these updates were presented by senior SBA program officials. Finally, all attendees received instruction in understanding and avoiding sexual harassment problems.

All OIG investigators underwent firearms qualification training and received instruction in the “use of force” policy. They also received training in firearms safety and retention, asset forfeiture, search warrants, and critical incident trauma.

The OIG also conducted an **administrative training session for its support staff**, June 18-20, 1996. Some of the topics covered during that week were English and Editing Principles and Practices, Windows 95, Introduction to Microsoft Office Suite, Management and Legal Counsel Division Initiatives and Issues, Sexual Harassment in the workplace, and Timekeepers Refresher Training. Attendees met with their respective divisions at the completion of the training sessions.

OIG Standard Operating Procedures (SOP) Updated

As part of the SBA-wide initiative to update, revise, and clarify Agency SOPs, the OIG reviewed its own SOPs. Several outdated SOPs were canceled, and newly revised procedures were prepared for Audit, Investigations and Security, and Inspection and Evaluation programs.

President's Council on Integrity and Efficiency

The Inspector General (IG) is a member of the President's Council on Integrity and Efficiency (PCIE) and serves as chair of the PCIE's Committee on Inspection and Evaluation. He participates in PCIE initiatives to reduce fraud and improve the management of Federal programs on a Government-wide basis. During the reporting period, the IG and his staff have contributed to two key PCIE initiatives.

❶ The IG, in his role as Chair of the Committee on Inspection and Evaluation, was requested by the PCIE to join with the Chair of the Auditing Committee in a survey of community involvement in the implementation of the Government Performance and Results Act (GPRA). The survey was completed and the results are summarized in the Executive Summary section at the outset of this report. The details are presented in the Agency Management and Financial Activities Chapter (see page 50.)

❷ The IG commissioned the Inspections Round Table, the Committee on Inspection and Evaluation’s support staff, to review the

methods currently used by the inspector general community to monitor block grants and similar programs. The report documents the existing provisions for accountability as manifested in the 13 Federal block grant programs. The purpose was to lay the groundwork for determining the sufficiency of those provisions by spelling out the general accountability concepts and identifying specific issues concerning the block grant statutes. The review also offered suggestions for modifying existing block grant programs to improve their accountability. The report was issued in July 1996 and was subsequently presented to the PCIE by the IG.

**Direct Investigation Time by Program Area
April 1, 1996 to September 30, 1996**

Program Area	Direct Time %	Number of Investigations	
		Closed	In Progress
Business Loans	53%	26	153
Disaster Loans	26%	9	83
SBIC	4%	2	11
Surety Bond Guarantees	1%	0	1
Government Contracting	2%	1	7
Minority Enterprise Development	2%	5	13
Economic Development	1%	0	1
Agency Management and Financial	11%	11	18
Total	100%	54	287

**Direct Auditing Time by Program Area
April 1, 1996 to September 30, 1996**

Program Area	Direct Time %	Number of Audits	
		Issued	In Progress
Business Loans	58%	3	8
Disaster Loans	26%	0	6
SBIC	*	0	0
Surety Bond Guarantees	1%	0	1
Government Contracting	0%	0	0
Minority Enterprise Development	2%	3	0
Economic Development	12%	1	1
Agency Management and Financial	1%	4	2
Total	100%	11	18

* less than ½ percent

Profile of Operating Results

April 1, 1996 to September 30, 1996

Audit Activities	Totals
A. Reports Issued	11
B. Desk Reviews of CPA Audit Reports Issued	0
C. Audit Recommendations Issued	42
D. Dollar Value of Costs Questioned	\$887,216
E. Dollar Value of Recommendations That Funds Be Put to Better Use .	\$325,000

Audit Followup Activities

F. Audit Recommendations Closed	53
G. Disallowed Costs Agreed to by Management	\$1,313,113
H. Dollar Value of Recommendations That Funds Be Put to Better Use Agreed to by Management	\$1,437,923
I. Unresolved Audit Recommendations	23
J. Dollar Value of Unresolved Audit Recommendations	\$1,094,698
K. Settlement Based on CPA Quality Review (non-recurring category).....	\$0

Inspection Activities

A. Reports Issued	2
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Legislation/Regulation/SOP/Other Reviews

A. Legislation Reviewed	4
B. Regulations Reviewed	10
C. Standard Operating Procedures Reviewed	27
D. Other Issuances Reviewed*	55

* This includes policy notices, procedural notices, Administrator's action memoranda, and other communications which frequently involve the implementation of new programs and policies.

Status of Investigations as of September 30, 1996**Totals**

A. Total Cases	341
B. Closed Cases	54
C. Pending Cases	26
D. Open Cases	261
E. Subjects under Investigation	1268

Summary of Indictments and Convictions

A. Indictments from OIG Cases	36
B. Convictions from OIG Cases	44

Summary of Recoveries and Reductions of Risk

A. Potential Recoveries and Fines as a Result of OIG Investigations . . .	\$2,041,896
B. Reductions of Financial Risk as a Result of OIG Investigations	\$2,731,518
C. Reductions of Financial Risk as a Result of the Name Check Program	<u>\$8,125,948</u>
 Total:	<u>\$12,899,362</u>

SBA Personnel Actions Taken as a Result of Investigations

A. Dismissals	0
B. Resignations/Retirements	3
C. Suspensions	0
D. Reprimands	1

Program Actions Taken as a Result of Investigations

A. Suspensions	1
B. Debarments	0
C. Removals from Program	1
D. Other Program Actions	0

Summary of OIG Fraud Line Operation

A. Total Fraud Line Calls/Letters	1,581
B. Total Calls/Letters Referred to Offices Outside the OIG	1,571
C. Total Calls/Letters Referred to Investigations Division for Evaluation.	10

Investigations Activities - Referral Program

A. Cases Referred to FBI	14
B. Referred to Other Agencies (Excluding FBI)	2
C. Indictments from Referrals	3
D. Convictions from Referrals	5
E. Potential Recoveries and Fines as a Result of Referral Program	\$216,862
F. Reductions of Financial Risk as a Result of Referral Program	\$0

**Office of Inspector General
Staffing as of September 30, 1996**

A. Immediate Office	3
B. Auditing Division	32
Professional	28
Support	4
C. Investigations Division	46
Professional	38
Support	8
D. Inspection and Evaluation Division	9
Professional	8
Support	1
E. Management and Legal Counsel Division	9
Professional	7
Support	2
OIG Total	<u>99</u>

**Additional Temporary Disaster Staffing
Funded from Supplemental Appropriations**

A. Auditing Division	7
B. Investigations Division	6
C. Management and Legal Counsel Division	1
OIG Disaster Total	<u>14</u>

FY 1996 Productivity Statistics Second Six Months

Office-Wide Dollar Accomplishments	Totals
A. Potential Investigative Recoveries and Fines	\$2,041,896
B. Management Avoidances as Result of Investigations	\$10,857,466
C. Disallowed Costs Agreed to by Management	\$1,313,113
D. Recommendations that Funds Be Put to Better Use Agreed to by Management	\$1,437,923
E. Settlement Based on CPA Quality Review (non-recurring category)	\$0
Total	<u>\$15,650,398</u>
 Auditing Division Activities	
A. Reports Issued	11
B. Disallowed Costs Agreed to by Management	\$1,313,113
C. Recommendation that Funds Be Put to Better Use Agreed to by Management	\$1,437,923
D. Settlement Based on CPA Quality Review (non-recurring category)	\$0
 Inspection and Evaluation Division Activities	
A. Reports Issued	2
 Investigations Division Activities	
A. Cases Closed	54
B. Indictments	36
C. Convictions	44
D. Potential Investigative Recoveries and Fines	\$2,041,896
E. Management Avoidances	\$10,857,466
- Investigation Cases	\$2,731,518
- Name Check Program	\$8,125,948

FY 1996 Productivity Statistics

Full Year

Office-Wide Dollar Accomplishments	Totals
A. Potential Investigative Recoveries and Fines	\$20,467,211
B. Management Avoidances as Result of Investigations	\$38,064,884
C. Disallowed Costs Agreed to by Management	\$2,434,007
D. Recommendations that Funds Be Put to Better Use Agreed to by Management	\$7,910,345
E. Settlement Based on CPA Quality Review (non-recurring category)	\$1,100,000
Total	<u>\$69,976,447</u>

Auditing Division Activities

A. Reports Issued	23
B. Disallowed Costs Agreed to by Management	\$2,434,007
C. Recommendation that Funds Be Put to Better Use Agreed to by Management	\$7,910,345
D. Settlement Based on CPA Quality Review (non-recurring category)	\$1,100,000

Inspection and Evaluation Division Activities

A. Reports Issued	3
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Investigations Division Activities

A. Cases Closed	131
B. Indictments	72
C. Convictions	69
D. Potential Investigative Recoveries and Fines	\$20,467,211
E. Management Avoidances	\$38,064,884
- Investigation Cases	\$25,231,518
- Name Check Program	\$12,833,366

Statutory Reporting Requirements

The specific reporting requirements as prescribed in the Inspector General Act of 1978, as amended by the Inspector General Act Amendments of 1988, are listed below.

Source		Location in this Report
Section 4(a)(2)	Review of Legislation and Regulations	Pages 6 to 55
Section 5(a)(1)	Significant Problems, Abuses, and Deficiencies	Pages 6 to 55
Section 5(a)(2)	Recommendations With Respect to Significant Problems, Abuses, and Deficiencies	Pages 6 to 55
Section 5(a)(3)	Prior Significant Recommendations Not Yet Implemented	Page 76
Section 5(a)(4)	Matters Referred to Prosecutive Authorities	Pages 6 to 55
Section 5(a)(5) and 6(b)(2)	Summary of Instances Where Information Was Refused	None
Section 5(a)(6)	Listing of Audit Reports	Page 70
Section 5(a)(7)	Summary of Significant Audits	Pages 6 to 55
Section 5(a)(8)	Audit Reports Containing Questioned Costs	Page 72
Section 5(a)(9)	Audit Reports Recommending that Funds Be Put to Better Use	Page 73
Section 5(a)(10)	Summary of Reports Where No Management Decision Was Made	Page 75
Section 5(a)(11)	Significant Revised Management Decisions	None
Section 5(a)(12)	Significant Management Decisions With Which OIG Disagreed	None

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APPENDIX I

Audit Reports Issued April 1, 1996 to September 30, 1996

TITLE	NUMBER	ISSUE DATE	QUESTIONED COSTS	FUNDS FOR BETTER USE
Business Loans				
Business Loan Center	6-5-H-002-019	9/20/96	\$627,039	
Low Documentation (LowDoc) Loan Program	6-5-E-002-022	9/30/96		\$325,000
Woodway Bank and Trust Co.	6-4-W-005-013		\$117,518	
Program Subtotal	Reports 3		\$744,557	\$325,000
Minority Enterprise Development				
Basic Ordering Agreements	6-5-E-001-021	9/25/96		
Section 8(a) Regular Dealers	6-5-H-006-017	8/21/96		
Manufacturing Technology, Inc.	6-5-E-001-015	5/15/96		
Program Subtotal	Reports: 3			
Economic Development				
Virginia SBDC	6-6-H-003-023	9/30/96		
Program Subtotal	Reports: 1			
Agency Management and Financial				
Boone, Young & Associates	6-5-S-918-018	9/20/96		
FY 1995 Financial Statements	6-5-H-007-014	5/1/96		
FY 1995 Financial Statements - Management Letter	6-5-H-007-016	5/31/96		
Rushman Associates, Inc. Closeout Audit	6-5-S-918-020	9/23/96		

TITLE	NUMBER	ISSUE DATE	QUESTIONED COSTS	FUNDS FOR BETTER USE
Program Subtotal	Reports: 4			

TOTALS (all programs)	Reports: 11		\$887,216	\$325,000
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APPENDIX II - Part A

Audit Reports with Questioned Costs April 1, 1996 to September 30, 1996

		REPORTS	RECs*	DOLLAR VALUES	
				QUESTIONED	UNSUPPORTED
A.	For which no management decision had been made by March 31, 1996	5	8	\$1,906,090	
B.	Which were issued during the period	3	3	\$887,216	
	Subtotals (A + B)	8	11	\$2,793,306	
C.	For which a management decision was made during the reporting period	6	9	\$2,023,608	
	(I) Disallowed costs	6	9	\$1,313,113	
	(a) Due SBA	6	9	\$1,313,113	
	(b) Due program participant				
	(ii) Costs not disallowed	1	1**	\$710,495	
D.	For which no management decision had been made by September 30, 1996	2	2	\$769,698	

* Recommendations

** One recommendation was agreed to, in part, by management. It therefore appears in both c(i) and c(ii).

APPENDIX II - Part B

Audit Reports with Recommendations that Funds Be Put to Better Use April 1, 1996 to September 30, 1996

		REPORTS	RECs [*]	RECOMMENDED FUNDS FOR BETTER USE
A.	For which no management decision had been made by March 31, 1996	3	5	\$19,392,633
B.	Which were issued during the period	1	1	\$325,000
	Subtotals (A + B)	4	6	\$19,717,633
C.	For which a management decision was made during the reporting period	3	5	\$19,392,633
	(I) Recommendations agreed to by SBA management	3	4	\$1,437,923 ^{**}
	(a) SBA level	3	4	\$1,437,923
	(b) Program participant level			
	(ii) Recommendations not agreed to by SBA management	1	1	\$18,471,710
D.	For which no management decision had been made by September 30, 1996	1	1	\$325,000

^{*} Recommendations.

^{**} This dollar amount contains \$517,000 for which no original audit recommendation was made. The dollars represent half of the FY 1997 funding slated for the Puerto Rico SBDC which was withheld when the program was terminated. The other half of the funding is reflected as Management Avoidances reported by the Investigations Division. Normally lines C(I) and C(ii) would total line C--they are now \$517,000 out of balance.

APPENDIX II - Part C

Audit Reports with Non-Monetary Recommendations April 1, 1996 to September 30, 1996

		REPORTS	RECOMMENDATIONS
A.	For which no management decision had been made by March 30, 1996	9	24
B.	Which were issued during the period	10	38
Subtotals (A + B)		19	62
C.	For which a management decision was made during the reporting period	12	42
D.	For which no management decision had been made by September 30, 1996	9	20

APPENDIX II - Part D

Overdue Management Decisions September 30, 1996

AUDITEE	REPORT NUMBER	ISSUED	STATUS
J. W. Collins & Associates	6-5-H-006-010	3/11/96	No response from District Office.

APPENDIX II - Part E

Significant Audit Reports Described in Prior Semiannual Reports Without Final Action as of March 31, 1996

REPORT NUMBER	TITLE	DATE ISSUED	DATE OF MANAGEMENT DECISION	FINAL ACTION TARGET
0-1-0-007-140	Regulations for 301(d)	06/13/90	09/30/93	12/31/93
3-2-S-401-014	Colson Service Corp.	12/03/92	09/24/96	06/30/96
3-3-E-002-025	Controls over Advisory and Assistance Services	03/01/93	03/10/93	03/31/93
3-2-C-002-033	Administration of 8(a) Program	03/31/93	09/30/94	09/30/95
3-2-H-007-036	SBA's Oversight of Colson Services Corp.	06/16/93	03/31/95	09/30/95
4-3-H-011-016	SBA's Award of 8(a) Contracts to ASCI	05/16/94	12/30/94	06/30/95
4-3-W-009-018	Washington State SBDC	08/01/94	03/31/95	05/31/95
4-2-E-403-019	Pulsar Data Systems	08/15/94	03/22/95	None
5-3-H-004-006	SBA Loan Servicing and Debt Collection Activities	03/31/95	09/30/96	9/30/98
5-4-W-001-009	Indiana Lumbermens Mutual Insurance Co.	03/31/95	08/22/96	None
5-4-H-008-008	Population and Marketing Analysis Center	03/31/95	09/30/96	None
5-5-H-007-003	SBA FY 1993 Financial Statements	12/13/94	09/30/95	10/31/95
5-3-W-010-018	Section 7(a) Credit Elsewhere	09/18/95	03/29/96	06/30/96
5-5-H-004-015	Cordoba Corporation - Guaranteed Loan	08/10/95	09/29/95	08/02/95
5-5-H-004-016	Administration of \$825,000 Line of Credit	08/18/95	03/29/96	06/30/96
5-3-E-010-021	8(a) Competitive Mix	09/29/95	03/29/96	09/30/96
5-4-H-005-013	University of Puerto Rico SBDC	06/30/95	09/30/96	06/30/96
5-4-H-009-012	FY 1994 Financial Statements - Management Letter	06/28/95	09/30/95	09/30/96
5-4-H-009-010	FY 1994 Financial Statements	06/01/95	08/09/95	09/30/97

REPORT NUMBER	TITLE	DATE ISSUED	DATE OF MANAGEMENT DECISION	FINAL ACTION TARGET
5-4-H-003-014	National Education Center for Women in Business	08/04/95	02/15/96	09/11/95
6-5-H-006-010	J.W. Collins & Associates	03/11/96	None	None
6-4-W-008-003	California SBDC	01/11/96	09/30/96	12/31/96
6-5-S-918-006	Daniel Dennis & Co.	01/24/96	09/30/96	10/14/96
6-6-H-002-011	GeoDemographics, Ltd.	03/29/96	09/30/96	04/01/98

* A management decision has not been made on all recommendations in the audit report.