



## Office of Inspector General Small Business Administration

### August 2002 Update

#### *Business Loan Programs*

Two Audit Reports Issued on Two SBA-Guaranteed Loans. OIG issued two audit reports on two separate SBA-guaranteed loans in August 2002. The first audit found that the financial documentation submitted by the borrower contained several obvious modifications that apparently were not noticed and/or questioned by the lender. The principal's 1997 W-2 form and Federal Income Tax Return were altered in several places and the lender did not obtain an Internal Revenue Service (IRS) transcript to verify the information which would have alerted them that the figures were altered. OIG recommended that the Illinois District Office seek recovery of \$93,689 from the lender, less any subsequent recoveries. The District Office agreed with the recommendation.

The second audit found several issues: 1) the borrower did not have repayment ability; 2) the lender did not verify equity injection or exercise prudent control over the use of proceeds; 3) the loan proceeds were not disbursed in accordance with the settlement sheet (SBA Form 1050); and 4) the lender did not verify the tax return information with the IRS. OIG recommended that the Santa Ana District Office seek recovery of \$197,751.97 from the lender on the guaranty paid, less any subsequent recoveries. The District Office indicated that the lender had agreed to repay the guaranty.

SBA Preferred Lender Agrees to Release SBA Guaranty Obligation. On August 6, 2002, an SBA preferred lender agreed to release SBA of guaranty obligations on nine defaulted business loans, totaling more than \$6.5 million. The loans in question were identified in an alleged fraudulent "flipping" scheme. The scheme involved individuals purportedly submitting fraudulent SBA loan applications, which inflated the value of gas stations, to obtain financing for 100 percent of the inflated purchase price. The Agency cost savings was the result of the joint Federal Bureau of Investigations (FBI) and SBA/OIG investigation, diligent efforts of the SBA Houston District Office, and the lender's decision to release SBA's liability.

Utah Vitamin and Herb Production Packaging Company Part-Owner Charged with Unlawful Activity, Forgery, Theft, and Money Laundering. On August 8, 2002, the part-owner of a vitamin and herb production and packaging company in Provo, Utah, was charged in an information by the Utah County Attorney's Office with one count of **pattern of unlawful activity**, one count of **forgery**, eight counts of **theft by deception**, and eight counts of **money laundering**. The SBA/OIG joint investigation with the Utah County Sheriff's Office determined that the part-owner obtained a \$905,000 SBA loan in the name of a laboratory by falsely representing that he had authorization from the board of directors of that lab and that the board members were guaranteeing the loan. The defendant used the loan to purchase a building in his name and then represented to the board that they would be leasing a new building for their expansion

from a disinterested third party. He then began collecting excessive lease payments from the lab under a fabricated name via a post office box. In addition, the Utah County Sheriff's Office investigation determined that he diverted over \$1.5 million in company funds under false pretenses and used the funds to send his wife to school, purchase property, and other personal expenses. Information provided by SBA/OIG was instrumental in developing Utah County's already open investigation and securing the prosecution of the defendant. The SBA/OIG case was initiated based on a referral from the SBA Salt Lake City District Office.

## ***Surety Guarantees***

Audit Report Issued on Loss Adjustment Expenses Incurred on a Bonding Company. On August 19, 2002, OIG issued an audit report on the loss adjustment expenses incurred on a bonding company. The audit was conducted based on a complaint from the contractor, who believed the surety was charging his company unreasonable legal fees. The audit found that 98 percent of the loss adjustment expenses (LAE) claimed by the surety company for the SBA-guaranteed bonds were allocable, allowable, and reasonable. The surety company incurred and was reimbursed its guaranteed percentage by SBA for only \$1,547 of LAEs that were not specifically allocable to a claim for loss resulting from the breach of the terms of the bonded contract. The audit also disclosed that SBA did not give the surety company permission to close its files in a timely manner. As a result, the auditors made recommendations to the Acting Associate Administrator, Office of Surety Guarantees, to recover the Federal share of \$1,392 from the surety company for the unallowable LAEs and ensure file closures are approved expeditiously. The Acting Associate Administrator, Office of Surety Guarantees, agreed with the recommendations. Final action was completed on one of the two recommendations in this report on August 20, 2002. The Office of Surety Guarantees agreed to take expedient action to approve file closures on requests from sureties to discontinue pursuit of recovery and the office revised SBA's policies and procedures

accordingly to avoid incurrence of unnecessary LAEs in the future.

## ***Entrepreneurial Development***

Audit Report Issued on Sponsorship Activities. On August 26, 2002, OIG issued a final audit report of a district office's sponsorship activities. The audit was the result of a request by the former Deputy Associate Administrator for Field Operations that OIG review the office's compliance with SBA's policies and procedures for co-sponsorships and SBA gift authority. The audit showed that the office: (1) solicited and accepted gifts from prohibited sources and from a source requiring a conflict of interest determination; (2) did not deposit gift funds into the Business Assistance Trust (BAT) Fund; (3) used gift funds for prohibited purposes; (4) inappropriately expended excess funds; (5) collected and used registration fees without authority; and (6) did not have adequate controls in place to ensure proper accountability of funds. We concluded that these non-compliances occurred because senior district office management personnel did not believe the requirements of standard operating procedure 90 75 2 were applicable to any of the office's events and because oversight by regional and Headquarters personnel was not adequate.

OIG recommended that SBA management provide better guidance to field office staff and improve its oversight over field office SBA-sponsored and cosponsored activities. The guidance should address: (1) the distinction between the types of events and the appropriate procedures for planning and conducting cosponsored and SBA-sponsored events; (2) the appropriate sources from whom to solicit and accept gifts; (3) the requirement to obtain conflict of interest case-by-case determinations; (4) the proper procedures for disbursing excess gift funds; (5) the remission of gift funds to the BAT Fund at the U.S. Treasury; (6) the proper accountability of event funds; and (7) the appropriateness of charging fees. SBA management agreed with six recommendations and disagreed with one. Revisions were made to the report based on management's comments.

## ***Agency Management***

Audit Report Issued on Former Regional Administrator's Travel On August 7, 2002, OIG issued an audit report on the travel of a former SBA regional administrator (RA). The audit was performed at the request of the Senate Small Business Committee and found that the former RA's travel did not always comply with travel regulations and identified erroneous payments totaling \$9,653.34, consisting of \$828.41 for excess travel costs due to indirect travel through his home town and \$8,824.34 for other unallowable travel payments. Since SBA allowed RAs to be the authorizing official on their own travel and the documentation did not always establish whether the travel was essential, OIG does not believe that SBA appropriately controlled self-authorized travel.

The former RA self-authorized travel for 258 duty days during a 2 ½ year period. During this time-frame, out of a possible 128 weekends, he traveled to, from, or through his home town on 52 weekends. On 20 of these weekends, the former RA's Travel Authorizations and/or Requests for Reimbursement noted he was conducting official SBA business in his home town, other than solely traveling from or to his home town. While there is no prohibition against taking an indirect route while traveling, the travel regulations are clear that any excess cost must be borne by the traveler as a personal expense and the original trip must have an official Government purpose. The combination of the frequency of trips involving his home town, the inability to reconstruct satisfactory justification for some trips from travel documentation, the use of allowed self-authorization and self-approval of many of these trips, and the identification of instances of excess costs relating to trips through his home town gives the appearance that official Government travel was not appropriately controlled by SBA. Accordingly, safeguards must be implemented to ensure that SBA has control over official Government travel and eliminate the appearance of, and possible actual, travel abuse. SBA has taken steps to preclude this situation from recurring in the future. The report contained three recommendations to obtain reimbursement from the former RA for the unallowable travel payments and preclude this situation from

recurring. The Chief Financial Officer (CFO) and the Assistant Administrator for Field Operations agreed with the recommendations. The CFO had other comments concerning the issuance of the proposed travel SOP. The former RA disagreed with most of the questioned costs.

The activity Update is produced by SBA/OIG,  
Phyllis K. Fong, Inspector General.

OIG has established an e-mail address ([oig@sba.gov](mailto:oig@sba.gov)) that we encourage the public to use to communicate with our office. We welcome your comments concerning this Update or other OIG publications. To obtain copies of such documents please contact:

Vanessa Piccioni, SBA/OIG,  
409 Third Street SW., 5<sup>th</sup> Floor  
Washington, DC 20416  
mail: [OIG@SBA.GOV](mailto:OIG@SBA.GOV)  
Telephone number (202) 205-6580  
FAX number (202) 205-7382

Many audit and inspection reports can be found on the Internet at  
<http://www.sba.gov/IG/igreadingroom.html>

If you are aware of suspected waste, fraud, or abuse in any SBA program, please call the:

**OIG FRAUD LINE at (202) 205-7151**  
or

**TOLL-FREE FRAUD LINE (800) 767-0385**