



## Office of Inspector General Small Business Administration

December 1996 Update

### *Business Loans*

Georgia Caterer Found Guilty of Conspiracy and Bank Fraud. A co-owner of a now-defunct Atlanta, Georgia, catering company was found guilty on December 10, 1996, of **conspiracy, bank fraud, and submitting false loan documents to SBA.** The OIG investigation, based on a referral from SBA's Atlanta District Office, disclosed that the owner and his former wife and business partner defrauded SBA and Federally-insured lenders of more than \$1 million, including a \$650,000 SBA-guaranteed loan from a non-bank participating lender. The couple had fled the country prior to their 1991 indictment, but were deported to the United States--she from Russia in 1995 and he from Cyprus in April 1996. As a condition of his extradition under Cypriot law, the U.S. Government dismissed 15 other felony counts on which he had been indicted. As previously reported, his wife negotiated a guilty plea to two counts and agreed to cooperate with the Government's prosecution of her husband.

South Dakota Rancher's False Statements Lead to Prison Sentence. An Eagle Butte, South Dakota, rancher was sentenced on October 16, 1996, to 24 months imprisonment, 3 years

supervised release, \$115,000 restitution, and a \$5,000 fine. He had previously pled guilty to one count of **making a false statement** to a Federal agency. 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 applicant 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.

Ongoing California Loan Broker Investigation Yields Additional Results. The SBA/OIG's ongoing investigation of a La Canada, California, loan broker recently yielded the following five additional results:

- ❶ The owner of an automobile transmission establishment in Los Angeles, California, was sentenced on November 25, 1996, to 3 years probation, 300 hours community service, a \$50,000

fine, and restitution to SBA of \$366,155. He previously 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 applicant 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.

② The former owner of a Pomona, California, restaurant pled guilty on December 6, 1996, to one count of **making a false statement on a loan application to a Federally-insured financial institution**; in return, the other counts on which he had been indicted were dismissed. In applying for his \$550,000 SBA-guaranteed loan, the businessman submitted tax returns to the participating lender which significantly overstated his business income; he also submitted a false financial statement to induce the lender to grant a payment deferment and not foreclose on the loan.

③ The owner of a general merchandise discount store in Los Angeles, California, was sentenced on December 9, 1996, to 3 months in a halfway house, 3 months in home detention, 3 years probation, 1,500 hours community service, and \$1,144,070 restitution. He had pled guilty to one count of **making a false**

**statement on a loan application to a Federally-insured financial institution** in connection with his \$1,000,000 SBA-guaranteed loan. In addition to false documents associated with his capital injection, the man submitted altered Federal income tax returns for 1987-89, which significantly overstated his income, to induce approval of the loan.

④ A California businesswoman was charged in a criminal information on December 11, 1996, with one count of **making a false statement within the jurisdiction of SBA**. She had been approved for a \$1.5 million Section 504 loan to acquire a motel in Tehachapi, California; \$725,000 of the loan, which SBA canceled as a result of this investigation, would have been funded by an SBA debenture. The investigation revealed that the applicant made false statements concerning the source of her capital for the project. She was assisted by her sister, a former personal banking officer at a bank in Paramount, California. The accomplice prepared a false deposit verification form for submission to both SBA and its participating lender bank. On the form, the bank officer represented that her bank had two accounts, with a combined balance of \$790,000, held solely in the loan applicant's name. In fact, the accounts were never the sole property of her sister. The accounts listed on the form had

been opened by another person, and the accomplice had added her sister's name at a later date. The bank officer previously pled guilty to a felony in connection with her part in this scheme.

⑤ The former owner of a Riverside, California, cafe pled guilty on December 17, 1996, to one count of **making a false statement on a loan application to a Federally-insured bank**. In return, the Government agreed to dismissal of four other counts on which he had been indicted. In pleading guilty, the man admitted submitting altered income tax returns for the years 1987-89 with his application for a \$225,000 SBA-guaranteed loan to purchase the cafe. He also 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 man also represented that he intended to purchase machinery and equipment totaling \$125,000 from a company which was controlled by the loan broker. The loan broker returned the funds to the applicant, who then repaid the undisclosed personal loan.

As a result of this investigation, the loan broker previously pled guilty to **making false statements on a loan application to a Federally-insured financial institution** and agreed to **criminal asset forfeiture** of the proceeds of his crime. The OIG initiated the investigation after a participating lender and SBA's Los Angeles District

Office referred the matter. The U.S. Secret Service subsequently joined the investigation at the invitation of the OIG.

More Clients of California Loan Packager Indicted or Pled Guilty. A fourth former client of a Garden Grove, California, loan packager has been indicted, and two others who were indicted earlier have entered guilty pleas, all on charges of **making false statements on loan applications to Federally-insured financial institutions**.

① The former owner of a Garden Grove, California, furniture company was indicted on one count on December 6, 1996. She obtained a \$250,000 SBA-guaranteed loan for her business, but the investigation found that she had diverted the loan proceeds to the purchase of a personal residence and subsequently defaulted on the loan. The indictment charged the businesswoman with providing a false invoice to conceal the true source of her down payment for the home.

② The former owner of a Vietnamese restaurant and billiard club in San Gabriel, California, pled guilty on December 5, 1996, to one count; in return, the other counts on which he had been indicted were dismissed. The applicant submitted altered income tax returns with his application for a \$150,000 SBA-guaranteed loan, which subsequently defaulted. The other counts in the indictment related to non-SBA loans.

③ The former owner of a beauty salon in Long Beach, California, pled guilty on November 22, 1996, to one count; in return, the other count on which he had been indicted was dismissed. The applicant submitted false documents to obtain disbursement of his \$150,000 SBA-guaranteed loan. This loan also defaulted.

The OIG initiated its investigation of this loan packager in 1990 based on information provided by SBA's Santa Ana District Office; the FBI joined the OIG investigation in progress.

Texas Couple Sentenced to Prison for Making False Statements. An Alvin, Texas, wife and husband were sentenced on December 4, 1996, to 5 months and 1 month imprisonment, respectively. They were also sentenced to 3 years supervised release, the first 5 months of which will be under home restriction, and a \$50 special assessment. Both had pled guilty to one count of **making false statements on loan applications to Federally-insured financial institutions** in an unsuccessful attempt to obtain more than \$500,000 in SBA-guaranteed loans. The couple submitted fraudulent tax returns for their convenience store in Houston, Texas, in an effort to obtain approval of a \$338,000 loan to finance their purchase of the store. They also submitted false tax returns for another convenience store in LaMarque, Texas, to obtain approval of a \$200,000 loan to be used for the purchase of the store. SBA foiled the couple's 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 based on a referral from the Office of District Counsel of SBA's Houston District Office.

Missouri Doctor Arrested Based on Indictment for Making False Statements. The president of an Excelsior Springs, Missouri, convenience store was arrested on November 29, 1996, as he reentered the United States. Based on an investigation by the OIG, the medical doctor had been indicted on August 7, 1996, on one count of **making false statements** to obtain a \$300,000 SBA-guaranteed loan, but the indictment was suppressed while he was out of the country. The loan to his convenience store, the guaranteed share of which SBA purchased in 1993 for \$242,508, was made by a non-bank participating lender located in the geographical area served by SBA's St. Louis District Office. The man's alleged false statements included failure to report his debt to SBA from a defaulted 1977 loan to a group of his health clinics through SBA's Kansas City District Office. He also submitted tax returns which allegedly overstated his adjusted gross income. This matter was referred to the OIG by a servicing loan officer in SBA's Kansas City District Office.

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## *Disaster Assistance*

Audit Finds Electronically Disbursed Disaster Funds Are Supported by Appropriate Internal Controls. The OIG issued an audit survey report that found that internal controls for a **new system to disburse disaster loans electronically** were generally

appropriate. The survey also found that some required procedures, however, had not been adopted. An audit survey of the conversion found that improvements were needed relating to certain physical security measures, separation of duties, documentation of certain EFT procedures, data protection (encryption), password renewal, dual controls for setting up new users, written procedures for rejected transmissions to the Department of the Treasury, and the keeping of troubleshooting logs. The audit survey also found a need for a contingency plan for emergencies, computer security training, and a computer security recertification of the Office of Disaster Assistance's Automated Loan Control System. The Associate Administrator for Disaster Assistance, who requested the review, agreed to consider these issues in the overall development of a security plan involving the system.

Disaster Loan Origination and Servicing Problems Found at SBA's Los Angeles District Office. An OIG audit of disaster loan servicing at the Los Angeles District Office (LADO) found that there were **problems in the origination or servicing of 17 of a judgmental sampling of 24 disaster loans** assigned to the LADO. Origination shortcomings included approving loans to borrowers that had access to credit elsewhere, overestimating borrower repayment ability, misjudging the impact of undisclosed liens on SBA collateral, not verifying information supplied by borrowers, and not detecting or rejecting potentially fraudulent documents. Servicing shortfalls included failure to contact borrowers, follow up on servicing actions, enforce loan terms, and respond

to early warning signals.

The auditors recommended the establishment of a quality assurance process; the Associate Administrator for Disaster Assistance concurred and agreed to take action. The auditors also recommended increased servicing and liquidation staff or the development of other alternatives to address the problems found; the Associate Administrator for Financial Assistance generally concurred with this recommendation.

California Loan Packager Sentenced to Prison for Submitting False Documents to Government. One of two Beverly Hills, California, brothers--both primary subjects of the OIG's long-time investigation of unscrupulous loan packagers--was sentenced on December 2, 1996, to 6 ½ years imprisonment and restitution of more than \$7 million in connection with the eight felony counts to which he had previously pled guilty. The man admitted that he had participated in the **submission of false documents to a Government agency**. As a part of his criminal activity, he also assisted others in the submission of false tax returns supporting six SBA disaster business loan applications, totaling more than \$3.9 million. The disaster loan applications included claims of both physical and economic injury and spanned three Los Angeles-area disasters: the 1992 civil unrest, the 1993 fires, and the 1994 earthquake. In addition, the man admitted **making false statements to Federally-insured financial institutions**, i.e., submitting false tax returns. This sentencing was one result of an OIG investigation, conducted jointly with the U.S. Secret

Service, which was prompted by a tip from a concerned citizen and a referral from SBA's Disaster Assistance Area 4 Office. Of the 24 individuals who have been charged as a result of this investigation, all but the other brother--currently a fugitive--have pled guilty.

California Clothing Manufacturer Sentenced for Converting Loan Proceeds. The owner of a Los Angeles, California, clothing manufacturer was sentenced on December 9, 1996, to 2,000 hours community service, 5 years probation, a \$2,000 fine, and full restitution to SBA. (At the time he pled guilty to **knowingly converting SB A disaster loan proceeds to his own use**, the balance of his economic injury loan was \$45,300.) This action related to the man's fraudulent application for a \$180,000 economic injury disaster loan following the 1992 Los Angeles civil unrest. Because he applied for a loan for which he knew he was ineligible, his use of the loan proceeds constituted conversion. This joint investigation with the U.S. Secret Service has focused on the submission of false documents as part of loan packages prepared by two Beverly Hills brothers referenced in the preceding article.

North Dakota Resident Sentenced for Theft of Public Money. A resident of Mandan, North Dakota, was sentenced on November 26, 1996, to 1 month home detention, 1 year probation, and 25 hours community service. She previously pled guilty to one count of **theft of public money**. The SBA/OIG investigation determined that the 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, resulting in the charge of theft of public money. The OIG initiated the investigation based on a referral from SBA's Fargo District Office.

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### *Small Business Investment Companies*

California Restaurateur Indicted for Bank Fraud. The former owner of a restaurant in La Mesa, California, was indicted on December 4, 1996, on three counts of **bank fraud**. One count involved a \$465,000 loan from a now-defunct specialized small business investment company (SSBIC) in Southfield, Michigan. The owner applied for the loan in the name of the restaurant, purportedly to make improvements to the facility. He is alleged to have falsified documents submitted to the SSBIC to conceal that the true (and ineligible) use of the loan proceeds was to make a down payment on an option contract to purchase stock in a chain of convenience stores. The joint OIG/FBI/Secret Service investigation developed from information uncovered in a previous investigation of this particular SSBIC.

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### *Agency Management and Financial Activities*

OIG Completes Study of Centralization of Agency Functions. In response to a request from the SBA Administrator, the OIG issued a study identifying SBA

functions which might potentially be centralized. Entitled "A Framework for Considering the Centralization of SBA Functions," it suggests a framework for centralizing SBA programs where appropriate, outlines an approach for deciding whether to consolidate the common functions of various SBA programs in central locations, and discusses the advantages and disadvantages of centralized operations compared with decentralized operations.

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### ***OIG Management***

Inspector General Issues Study of Inspection and Evaluation Units. The Inspection and Evaluation Committee of the President's Council on Integrity and Efficiency, which is chaired by the SBA Inspector General, issued a report on **OIG Inspection and Evaluation Units: Examples of Impact.** The report provides examples of the work performed by inspection and evaluation units in 15 offices of inspector general. The abstracts show the varied nature of OIG inspections and evaluations and the impact they have had. The document will be available through the Internet (<http://www.sbaonline.sba.gov/ignet>).

The OIG is On the Move. **Please make note of the following changes :**

The new address and telephone number for the OIG's **Dallas** field office are:

Office of Inspector General  
4300 Amon Carter Boulevard  
Suite 116  
Fort Worth, TX 76155  
Telephone: (817) 334-5933

The new address and telephone numbers for the OIG's **San Francisco** field office are:

Office of Inspector General  
455 Market Street  
San Francisco, CA 94105  
Telephone: (415) 744-6815 and 6816.

The Activity Update is produced by the SBA/OIG, James F. Hoobler, Inspector General.

Comments or questions concerning this update or requests for copies of OIG audits, inspections, or other documents should be directed to Johnny Cahn, SBA/OIG, 409 Third Street, SW, Washington, DC, 20416-4110.

Telephone number: (202) 205-6580  
FAX number: (202) 205-7382

If you are aware of suspected waste, fraud, or abuse in any SBA program, please call the OIG Fraud Line.

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