



Office of Inspector General Small Business Administration

August 2001 Update

Business Loan Programs

California Loan Brokerage Owner Sentenced to Jail.

The principal owner of an Inglewood, California, loan brokerage firm was sentenced on August 6, 2001, to 1 month in jail, 5 months home detention, 5 years probation, and \$388,300 restitution to SBA. He previously pled guilty to four counts of **making false statements to a federally insured financial institution** and one count of **subscribing to a false statement on a tax return**. In the plea agreement he admitted his role in the submission of four SBA-guaranteed loan applications containing altered tax returns. The loans totaled \$2.46 million, and losses to SBA and the participating lender bank exceeded \$2.3 million. He also admitted failing to report the company's gross receipts for 1991 and 1992, resulting in a total tax loss of approximately \$520,000. The company may have brokered as many as 160 SBA-guaranteed loans having an aggregate value of some \$60 million. OIG's examination of loan files disclosed evidence of such fraudulent activities as false personal financial statements, false tax returns, and manipulation of documents to falsely show that the borrowers made substantial initial cash injections. OIG's investigation of the company and its president's connection to the failure of the bank was conducted jointly with the Internal Revenue Service and the Federal Bureau of Investigation (FBI). The investigation to date has resulted in the convictions of 15 borrowers for whom the company brokered loans; 2 loan brokers, including the defendant; 1 tax preparer; and 1 bank official.

Missouri Dry Cleaning Business President Sentenced to Prison for Making False Statements.

The former president of a defunct dry cleaning business in Kansas City, Missouri, was sentenced on August 5, 2001, to serve 18 months in prison and 5 years on probation and to pay \$197,027 in restitution, more than 57 percent of which was in connection with his SBA-guaranteed loan. He previously pled guilty to **making false statements to a federally-insured bank** in order to receive a \$98,235 SBA-guaranteed loan in 1998, on which he immediately defaulted. In the loan application package, he provided a false tax return for the business and falsely claimed that he had no criminal history. A Suspicious Activity Report filed by the bank resulted in a joint investigation by OIG, the Secret Service, the Social Security Administration's OIG, and the Postal Inspection Service. The investigation determined that he also made false statements, used false Social Security numbers, and provided false tax returns to obtain five personal loans. He defaulted on all six of these loans.

Texas Brake Parts Company President and Wife Indicted for Bankruptcy Fraud, Money Laundering, Making False Statements, and Conspiracy.

The president of a brake parts company in Tyler, Texas, and his wife were indicted on April 3, 2001, on 13 counts of **bankruptcy fraud**, 1 count of **money laundering**, and 1 count of **conspiracy**. On May 9, 2001, a superseding indictment was filed which added four more counts of bankruptcy fraud, two counts of **making false statements**, one more count of conspiracy, and one more count of money laundering. The president allegedly created fraudulent invoices showing inventory of the business as being sold when,

in fact, the merchandise was still in his possession. He then went on to file for both personal and corporate bankruptcy while allegedly using the company's inventory to start a second company. Both defendants allegedly executed their scheme by "check-kiting" assets through numerous accounts. The SBA loans obtained by them totaled \$500,000. This case is scheduled for trial on September 24, 2001. OIG initiated this investigation based on a referral from SBA's Dallas/Fort Worth District Office and worked it jointly with FBI.

OIG Issues Audit Report on SBLC Examination Process. On August 17, 2001, OIG issued a final audit report on SBA's follow-up action taken in response to the Small Business Lending Company (SBLC) examination reports. In September 1998, SBA implemented a program to improve its oversight of the SBLCs by requiring annual safety and soundness examinations of the 14 SBLCs that participate in the Section 7(a) guaranteed loan program. The first two annual examinations were performed in FY 1999 and FY 2000, by the Farm Credit Administration under a contract with SBA.

The audit showed that SBA took several actions to improve oversight of the SBLC examination process, but additional actions are needed to fully ensure that the SBLCs take timely corrective actions in response to examination findings and recommendations. In its audit report, OIG recommended that SBA: (1) develop and implement formal SBLC examination follow-up procedures; and (2) develop and promulgate internal control standards for the SBLC program similar to those required for lenders subject to examination by financial institution regulators. SBA agreed with both recommendations and plans to implement a systematic follow-up process and develop internal control standards for the SBLCs.

Disaster Assistance Program

Arizona Couple Guilty of Mail Fraud. A Paradise Valley, Arizona, couple has been adjudicated guilty of **mail fraud**. On August 20, 2001, the wife pled guilty to all four counts on which she was previously indicted. On September 4, 2001, the husband was convicted on one of the four counts on which he was previously indicted. The couple had obtained a \$231,300 disaster home loan after the 1994 Northridge, California, earthquake. OIG's investigation revealed that the

couple had submitted a series of false invoices to SBA indicating that various contractors had done work when in fact they had not. They also received two loan payment deferments from SBA. Both times they claimed they had no money or assets. The investigation later revealed that the couple owned five properties in the Phoenix, Arizona, area that were not disclosed to SBA. Both defendants are scheduled to be sentenced in December 2001. OIG initiated the case based on a referral from SBA's Santa Ana Loan Servicing and Liquidation Center.

Agency Management

OIG Issues FY 2000 SBA Management Letter. On August 14, 2001, OIG issued the FY 2000 SBA Management Letter outlining **five conditions identified** during the audit of SBA's FY 2000 financial statements. The conditions were not required to be included in the auditors' report as they were nonmaterial weaknesses. The conditions identified related to: (1) Subsidy models for budget estimates and financial statement re-estimates, (2) personal property and equipment, (3) expired appropriations, (4) foreclosed property records and valuation, and (5) loan accounting records and servicing. SBA generally agreed with the findings and recommendations and described corrective actions taken and planned to address the five conditions.

OIG Issues Audit Report on Paper Report Production. OIG issued an audit report entitled Paper Report Production on August 3, 2001. The audit revealed that the Agency's **production of hard copy reports** could be reduced. The Office of the Chief Information Officer's (OCIO) print facility uses at least 500,000 sheets of paper to print a variety of different reports. Many of the report recipients interviewed by OIG indicated that they use little, if any, of the information contained in the reports, while others stated they would prefer to receive reports in an electronic format.

Much of the information contained in the paper reports is currently available electronically using query tools such as InfoQuest, RiskLender, ELIPS, and PMQD. OIG recommended that the OCIO coordinate with program offices and the Office of Administration to identify which reports can be discontinued or provided electronically, and to periodically review paper report production to eliminate unneeded printing. OCIO agreed with the recommendations.

Office of Inspector General

OIG has established an e-mail address (oit@sba.gov) that we encourage the public to use to communicate with our office. We welcome your comments on our publications, suggestions for possible audits, or referrals of possible incidents of waste, fraud, or abuse.

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