



Office of Inspector General Small Business Administration

January 1998 Update

Business Loans

Two Georgia Businessmen Indicted for Conspiracy and Making False Statements. Two Georgia businessmen were indicted on January 14, 1998, on seven counts of **conspiracy, making false statements to a Federally-insured bank, and making false statements** to SBA. One man was corporate secretary of a food company which obtained a \$155,000 SBA-guaranteed loan in May 1995 to purchase a grocery store in Kennesaw, Georgia. A second man, the chief executive officer of a brokerage company, was the broker for the sale of the grocery store. The investigation, initiated based on a referral from SBA's Atlanta District Office, found that the two conspired to conceal the true purchase price from the participating lender bank

and SBA. The original loan application indicated a purchase price of \$300,000, with the seller financing \$100,000; however, SBA declined the application based on that price, stating that repayment of the debt was unrealistic. According to the indictment, the broker subsequently told the bank's senior vice president that the buyer and seller had agreed to reduce the purchase price to \$200,000. He also faxed an Offer to Purchase to the bank indicating a purchase price of \$200,000. The loan application was re-submitted and approved by SBA. This investigation revealed that the purchase price was never reduced to \$200,000, but remained at \$300,000, restructured into \$200,000 for the sale of assets and \$100,000 for the sale of goodwill. SBA and the bank were never informed about the goodwill aspect

of the sale. Furthermore, at the loan closing the food company executive submitted a \$25,000 check as part of the required capital injection; he did not have sufficient funds to back the check and allegedly made arrangements with the seller to exchange the check for a \$25,000 promissory note after the closing. The indictment charges that this agreement was concealed from SBA and the bank.

Washington Restaurant Chain Executive Pleads Guilty to Making False Statements. The president of a corporation which owned several sandwich stores in the Tacoma, Washington, area was sentenced on January 9, 1998, to 1 year and 1 day imprisonment, 5 years probation, and \$187,000 in restitution. He had pled guilty to **making false statements on a loan application to a Federally-insured financial institution.** To obtain a \$322,197 SBA-guaranteed business loan, the man provided fraudulent guaranties, financial statements, and other documents to a participating lender bank and SBA. The investigation found that he had forged the signature of one shareholder and had several employees forge the signature of another shareholder on the guaranties, financial statements, and other documents. In addition, the investigation found that the president converted SBA collateral by selling it to a leasing company through a third party and leasing the equipment back from the leasing company. The investigation, conducted jointly with the FBI, was based on a referral from the bank to the U.S. Attorney's Office.

Texas Couple Charged With Making False Statements. The former owners of a convenience store in San Antonio, Texas, were charged in an information on January 5, 1998. Each was charged with two counts of **making false statements** in their application to SBA for a \$131,100 handicapped-assistance business loan. The information charges the couple with not disclosing to SBA that they had previously filed for bankruptcy and had already sold the business for which the loan was obtained. The joint investigation with the Social Security Administration's OIG was based on a referral from SBA's San Antonio District Office.

Two California Business Owners Plead Guilty to Bank Fraud. Two California businessmen--a car wash owner and a grocery store owner--pled guilty on January 12, 1998, to one count each of **bank fraud** committed while applying for an SBA-guaranteed loan. The OIG had been asked to join an investigation already under way by the FBI and the IRS into the submission of altered tax returns to financial institutions. SBA records revealed that the owner of the car wash had received SBA-guaranteed loans for \$700,500 and \$105,000 and that the owner of the grocery had received a \$255,000 SBA-guaranteed loan. The investigation confirmed that the "copies" of their Federal tax returns, submitted to the participant bank with their loan applications, had been altered from those submitted to the IRS in an effort to substantially overstate their

incomes. Both men were clients of the same tax return preparer.

California Grocer Sentenced for Making False Statement. The owner of a grocery store in West Covina, California, was sentenced on December 11, 1997, to 4 months imprisonment followed by 3 years supervised release. He was not ordered to pay a fine or to make restitution due to his financial condition. The man had 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. The grocer was identified during an extensive investigation, conducted jointly with the U.S. Secret Service, examining the submission of false documents as part of loan packages prepared by a loan broker who had previously pled guilty to **bank fraud** in connection with this investigation.

California Automobile Repair Shop Owner Sentenced for Making False Statements. The owner of an auto repair center in North Hollywood, California, was sentenced on December 15, 1997, to 5 years probation, a \$5,000 fine, and \$144,000 restitution. He had pled guilty to one count of **making false statements in a loan application to a Federally-insured bank.** The man had obtained a \$276,000 SBA-guaranteed loan based on an application containing altered individual and corporate income tax returns for 1987-89. Information

concerning this borrower came to light as part of the extensive investigation, conducted jointly with the U.S. Secret Service, involving loan applications prepared by two California brothers acting as loan packagers.

Washington State Meat Processor Pleads Guilty to Making False Statements. The former owner of a meat processing and packaging business in Endicott, Washington, pled guilty on January 15, 1998, to a one count information that charged him with **making false statements** to an SBA/OIG special agent. The investigation found that, to sell his business for an increased price, he provided altered tax returns to both SBA and a participating non-bank lender to show higher income than he had reported to the IRS. When interviewed about the tax returns submitted to SBA and the lender, the man made false statements to the SBA/OIG special agent regarding their accuracy. This investigation, conducted jointly with the IRS, was based on a referral from SBA's Spokane District Office.

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Disaster Assistance

Pennsylvania Attorney Indicted for Making False Statements. A Harrisburg, Pennsylvania, attorney was indicted on January 20, 1998, on one count of **making false statements** to SBA by overstating his income and omitting a theft conviction on his application for three SBA disaster loans. The man

made the allegedly false statements in connection with applications for \$40,000 in disaster assistance relating to floods in Pennsylvania's Susquehanna River valley in 1996. The loans were declined when SBA discovered that his income certification did not match the income reported on his Federal tax returns. The case, worked jointly with the FBI, was based on information provided by the Disaster Assistance Area 3 Office.

Missouri Nautical Consultant Pleads Guilty to Making False Statement. A marina operator/developer in West Alton, Missouri, pled guilty on January 16, 1998, to a one count information that charged him with **making a material false statement** to SBA to obtain disaster assistance for his company. The business was damaged by the Great Midwest Flood of 1993. The man presented bogus invoices to falsely document that he had spent \$12,862 of disaster loan proceeds for repair of a lift well (nautical machinery) when he had actually paid only \$4,500. The investigation also determined that, in applying for the \$93,700 disaster loan, he falsely indicated that certain equipment would be used as collateral for the loan; he actually sold the equipment, however, before he received any disaster assistance.

California Lighting Company Owner Pleads Guilty to Making False Statements. The owner of a lighting company in Los Angeles, California, pled guilty on January 6, 1998, to one count of **making false statements to SBA** and one count

of **making a false statement on a bankruptcy petition.** In return, the Government agreed to dismissal of the other six counts on which he was previously indicted. The company owner was approved for a \$25,900 disaster business loan following the 1994 Northridge earthquake; however, no proceeds beyond the first \$10,000 were disbursed because SBA became aware of a foreclosure on a property which he owned (and where he resided) but had not disclosed on his application. The man also applied for a disaster home loan following the 1995 floods in southern California, but this loan was declined due to lack of repayment ability. The investigation, which the OIG initiated based on information provided by SBA's Disaster Assistance Area 4 Office, found that his business had closed before SBA disbursed any funds. It also showed that he used a false Social Security number (SSN) and provided altered income tax returns in support of both applications. The owner filed for bankruptcy to forestall eviction from the property that was in foreclosure and used a second false SSN in the bankruptcy petition.

Nebraska Businessman Sentenced for Making False Statement. A guarantor of economic injury and physical damage disaster loans received by a Plattsmouth, Nebraska, resort was sentenced on November 13, 1997, to 5 years probation (including 6 months home confinement), \$63,000 restitution to SBA, and a \$100 special assessment. He previously pled

guilty to one count of **making a false statement to SBA**. A joint investigation by the U.S. Secret Service and the SBA/OIG had shown that the man defrauded SBA by submitting a false invoice in order to cause the release of loan proceeds. The resort, which featured camping, fishing, and swimming, received disaster loan proceeds totaling \$206,400 following the 1993 flood of the Platte River; it has made no repayment to SBA. This investigation was based on a referral from SBA's Omaha District Office.

California Businesswoman Sentenced for Filing False Claim.

The owner of a jewelry shop in Norwalk, California, was sentenced on January 26, 1998, to 3 years probation, 125 hours community service, and a \$50 special assessment. She was also ordered to continue making timely payments on her SBA disaster loans. The woman had previously pled guilty to **filing a false claim** with SBA. After her Los Angeles videotape rental store was looted and burned during the 1992 civil unrest, the woman was approved for SBA disaster loans totaling \$185,000 to rehabilitate that business. The OIG's investigation revealed that, as part of the loan application, she submitted a copy of a fictitious 1989 individual income tax return and an altered copy of her 1990 individual income tax return. Both of these documents significantly overstated her income. The investigation also revealed that, instead of using the \$159,700 of loan proceeds to reopen the video store, she opened the

jewelry shop. (As a result of the OIG's investigation, SBA canceled the final loan disbursement of \$25,300.) The investigation was initiated based on referrals from SBA's Disaster Assistance Area 4 Office and Fresno Loan Servicing Center.

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*Minority Enterprise
Development*

Maryland Computer Firm Withdraws From Section 8(a) Program After Eligibility Is Questioned in Audit. A Maryland computer manufacturing firm **withdrew voluntarily from the Section 8(a) program** after an OIG audit concluded the owners **exceeded the net worth limitations** for both initial and continuing eligibility. According to the audit report issued on January 21, 1998, the owners were inappropriately admitted into the program in 1994 when investment property owned by one of the company's principals was misrepresented as part of his personal residence. At the time of the application, three parcels of land adjacent to the owner's home were under a contract for sale to subdivision developers. Had that land not been excluded from his net worth under the exemption for a personal residence, the owner would have exceeded the net worth limit for entry into the Section 8(a) program.

In 1996, the owners kept their net worth below the \$750,000 limit to

ensure continuing eligibility by transferring assets worth a combined \$2.3 million to their wives. The OIG concluded that, under SBA regulations, assets transferred within 2 years of submission of the owner's annual personal financial statement still count as part of the owner's net worth. Consequently, this firm would have been ineligible for continuing participation. Including the transferred assets, the two owners' net worth was \$1.1 million and \$1.2 million, respectively.

The OIG recommended that SBA initiate action to terminate the firm from the Section 8(a) program. The Acting Associate Deputy Administrator for Minority Enterprise Development agreed with the audit's finding on initial eligibility, but stated the continuing eligibility rules in effect in 1996 would not have included the transfer of assets in the continuing eligibility calculation. The owners of the firm disagreed with the audit findings, but satisfied the intent of the recommendation by voluntarily withdrawing from the program. The regulations governing transfer of assets are currently under review for possible clarification and revision.

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Agency Management and Financial Activities

Former SBA Employee in California Pleads Guilty to Theft of Property. A former SBA employee from Van Nuys, California, pled guilty on January 12, 1998, to two counts of

theft of Government property.

The SBA/OIG's joint investigation with the OIG of the Federal Deposit Insurance Corporation (FDIC), by which he was previously employed, disclosed that after the man was hired as a loan specialist by SBA's Los Angeles District Office in 1995, he embezzled at least \$64,929 in disaster loan payments due SBA. In most of the cases, he falsely told delinquent borrowers that SBA had turned over their files to a collection agency to which he directed the borrowers to make their payments. The collection agency was actually an entity which the employee owned. The investigation also disclosed that he had embezzled \$5,883 from the FDIC by depositing a payment due the FDIC into a bank account which he owned. The SBA/OIG initiated its investigation based on a referral from SBA's Santa Ana Home Loan Servicing and Liquidation Center.

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Editor's Notes:



The following identifies the use of adjectives in these **Updates** to describe tax returns fraudulently submitted in support of loan applications:

Fictitious tax returns: The applicant submits "copies" of tax returns never filed with the IRS.

Altered tax returns: The applicant submits altered copies of tax returns actually submitted to the IRS.

Bogus tax returns: The applicant submits tax returns containing false information to both the IRS and SBA.



Most audit and inspection reports can be found on the Internet at:

WWW.SBAONLINE.SBA.GOV/IG/REPORTS.HTML

The Activity Update is produced by the SBA/OIG, Karen S. Lee, Acting Inspector General.

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