



Office of Inspector General U.S. Small Business Administration

May 2003 Update

Business Loan Programs

Washington Business Owner Indicted for Making False Statements and Bank Fraud. On May 6, 2003, the former owner of a Cheney, Washington, business was charged in a superseding indictment with 1 count of **false statements to SBA** and 26 counts of **bank fraud**. The false statement charge pertained to false statements he made to obtain an \$880,000 SBA-guaranteed loan from a financial institution. He concealed notes payable totaling \$305,000, a \$60,000 gambling debt, and the sale of 10 percent of an investment firm for \$100,000 a few days before signing the loan documents. In February 2002, he was indicted on seven counts of **bank fraud** against a financial institution and pled guilty to those charges. However, he later pulled his plea, citing a conflict of interest on the part of his attorney. This superseding indictment charges those original 7 counts of **bank fraud** against the financial institution, to include the **false statement** to the SBA count, and adds 16 other **bank fraud** counts for fraud against another financial institution.

California Business Owner Pleads Guilty to Making False Statements. A former owner of a business in Castaic, California, pled guilty on May 9, 2003, to two counts of **making false statements** to a Federally-insured financial institution, pursuant to a plea agreement. The defendant had been indicted on five counts of **making false statements** to two Federally-insured financial institutions in June 2000. After his indictment, he became a fugitive. He was apprehended in August 2002, in Las Vegas, Nevada. He submitted altered Federal income tax returns to a financial institution for the years of 1988, 1989, and 1990, as part of his loan application for a \$1 million SBA-guaranteed loan. The defendant later defaulted

on the loan. Subsequent investigation disclosed that he submitted two completely different altered Federal income tax returns to a another financial institution for the years of 1988 and 1989, in order to obtain a home loan in the amount of \$580,000.

Illinois Restaurant Maintenance and Repair Company Owners Agree to a Settlement. The former owners of a restaurant maintenance and repair company in Monee, Illinois, signed a settlement agreement on May 19, 2003. The agreement stipulated that the two agree to pay \$715,500 to the United States. As part of the agreement and included in the \$715,500, the couple agreed to release any claim to funds seized previously in the amount of \$344,312. In addition to these previously seized funds, the couple also agreed to release \$371,187 from funds currently being held by a writ of garnishment previously served upon the two. The release of the \$371,187 dissolves the writ of garnishment. This investigation was initiated based on a referral from the lending company and was conducted jointly with the Federal Bureau of Investigation (FBI). For more information on this case, see the January 2003 Update at this address <http://www.sba.gov/IG/update03-01.pdf>.

OIG Issues Audit Report on \$1 Million Section 7(a) Loan. On May 22, 2003, an audit report was issued concerning a \$1,027,500 loan made under the Section 7(a) loan program. The loan defaulted and was transferred to liquidation status within 24 months of its approval. The objective of the audit was to determine whether the lender and borrower materially complied with SBA's policies and procedures when originating, closing, and liquidating the loan. The loan was judgmentally selected for review as part of OIG's continuing effort to audit SBA-guaranteed loans charged-off or transferred to liquidation status early.

OIG determined that the lender did not originate the loan in accordance with the terms of the SBA loan authorization. Specifically, OIG found that the lender: (1) disbursed loan proceeds without adequate documentation; (2) did not comply with requirements for verifying borrower financial data; and (3) did not ensure the borrower was operating lawfully. Because a workout situation was developed for the loan, OIG recommended that the District Director notify the lender that SBA can be released from honoring the guaranty due to the non-compliances identified. OIG also recommended that SBA note the deficiencies in the loan file and flag the loan guaranty tracking system. The District Director agreed with the recommendations.

OIG also found that the borrower's principal made false statements during the origination of the loan. The principal was referred to the OIG Investigations Division for consideration of criminal or civil prosecution.

Disaster Loan Program

Guam Resort Owner Indicted for Making a Material False Statement. The owner of a resort in Talofofo, Guam, was indicted on May 7, 2003, on one count of **making a material false statement**. In January 2003, he submitted a disaster loan application to repair damage to his business caused by a typhoon. He lied on his application when he said he had not been arrested, convicted, or indicted for any offense, when in fact, he had been indicted, arrested, and convicted in 1998 for **bribery of a public official**. In 1998, he attempted to bribe an SBA employee with \$5,000 to approve a loan after Super typhoon Paka in December of 1997. This investigation was initiated based on a referral from the Guam Branch Office. OIG conducted this investigation with FBI.

Small Business Investment Companies

Agency Completes Final Action on Four Recommendations Related to an Audit of the Small Business Investment Company Application Procedures. In response to four recommendations made in an audit of the SBIC application process, the Investment Division permitted an applicant to

resubmit its application. The Investment Division agreed to reevaluate the application and completed that process in February 2003. The Division also sent directions to all analysts reviewing SBIC applications that they should prepare a letter of denial for the Associate Administrator's signature for all applications denied. After reviewing the resubmitted application and deciding to deny it, the Investment Division sent a letter to the applicant informing it of the decision in February 2003.

Agency Management

OIG Issues Audit Report on Agreed-Upon Procedures on Sensitive Payments. OIG issued an audit report on May 29, 2003, related to a previous report on sensitive payments. This audit was conducted as a result of a complaint received from a former SBA Regional Administrator (RA) with respect to the past finding entitled "SBA Paid Costs of Some Personal Travel by a Regional Administrator." OIG conducted a supplemental review of the RA's FY 2000 travel. The objective of the review was to determine if the RA complied with SBA's policies and procedures and the Federal Travel Regulations (FTR) when performing official Government travel and requesting reimbursement for related travel expenses during FY 2000. OIG concluded that the RA complied with SBA policies and procedures and the FTR in performing travel and requesting reimbursement for travel expenses during FY 2000. It was also found that SBA's policies and procedures and the FTR do not adequately address situations where an employee originates and/or terminates travel from a location other than their official duty station.

OIG recommended that the Chief Financial Officer (CFO) implement appropriate policies and procedures to address when it is appropriate for employees to originate or terminate travel from other than their official duty station and require authorizing officials to attach a written justification to the travel voucher when an employee is authorized to initiate or terminate travel from a location other than their official duty station. Additionally, it was recommended that SBA implement a formal policy that prohibits individuals from self-authorizing travel that originates and/or terminates from a location other than their official duty station. The CFO disagreed that the former RA complied with SBA's policies and procedures and the FTR when performing

official travel, however, he stated that SBA will develop policy regarding alternate points of origination and destination for employee travel. He further stated the travel SOP would be modified to prohibit self-authorization of travel involving alternate points of origination and destination.

OIG Issues Advisory Memorandum on SBA's Directives System. OIG issued an inspection advisory memorandum on May 22, 2003, entitled "Problems with SBA's Directives System." According to the memorandum, the system of directives is breaking down, with negative consequences for Agency staff, resource partners, and small businesses. Expired Policy and Procedural Notices continue to be used, while drafts of proposed Standard Operating Procedures are sometimes used before they are officially cleared and issued. The resulting uncertainty can create an inefficient use of employee time, delay service delivery to small businesses, create a negative public image, and produce unforeseen legal issues.

The memorandum recommended that the Associate Deputy Administrator for Management and Administration establish a working group representing major Agency offices and at least one field office. Within 60 days after its creation, the group should develop a plan for revising the fundamental structure of the directives system. The Agency concurred with the substance of the recommendation.

The activity Update is produced by SBA/OIG,
Harold Damelin, Inspector General.

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Teresa Clouser, SBA/OIG,
409 Third Street SW., 7th Floor
Washington, DC 20416
mail: OIG@SBA.GOV
Telephone number (202) 205-6580
FAX number (202) 205-7382

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