



Office of Inspector General U.S. Small Business Administration

February 2004 Update

Agency Management

The OIG Issues Cotton & Company's Agreed-Upon Procedures Report. On February 3, 2004, the OIG issued Cotton & Company's Agreed-upon Procedures Report on SBA's Federal Agencies' Centralized Trial Balance System (FACTS). As part of SBA's annual financial statement audit, OIG's independent auditor, Cotton & Company, performed agreed-upon procedures to determine if SBA's summarized FACTS data is consistent with its FY 2003 financial statements. The following findings were noted: twenty two differences between amounts in SBA's financial statements and footnotes and amounts presented for FACTS I resulting from rounding; one difference between the amount in SBA's financial statements and the amount presented for FACTS I reporting resulting from a formula error; four differences between amounts in SBA's financial statements and amounts presented for FACTS I reporting resulting from a difference in data presentation; six items designated as differences on the FACTS I reporting schedules not containing explanations for the differences; three differences between FACTS I notes and amounts included in SBA's audited financial statements and notes resulting from incorrect data entry; and six insufficient explanations for items identified as differences between FACTS I notes and amounts included in the notes to SBA's audited financial statements.

The report is intended solely for the use of the Department of Treasury's Financial Management Service, Office of Management and Budget, and General Accounting Office, and does not contain any recommendations.

Two Final Actions Completed on Audit of SBA's FY 2002 Financial Statements. In the audit, the OIG recommended that SBA's Chief Financial Officer (CFO) ensure that the Office of Financial Analysis adhere to documentation requirements of Federal Financial Accounting and Auditing Technical Release No. 3. As a result, the CFO rebuilt a new subsidy model for 7(a), and all supporting documentation was designed to comply with the technical release. In the near future, the CFO will be revising its 504 and Small Business Investment Company (SBIC) subsidy models. The second final action was completed when the CFO agreed to revise the estimation of cash flows for the disaster program to consider the changes in the portfolio as it ages and is sold. This will be used for re-estimates and, therefore, will allow a comparison between the assumptions and actual experience.

Final Action Completed on Audit of SBA's FY 2002 Financial Statements – Management Letter. A recommendation in this audit was completed when the Administrator signed the FY 2003 Federal Managers' Financial Integrity Act (FMFIA) letter and included the material weaknesses on subsidy and financial reporting weaknesses.

Two Final Actions Completed on Audit of Travel Card and Purchase Card Controls. In the audit, the OIG recommended that SBA's CFO develop written procedures that clearly identify the roles and responsibilities of all offices for ensuring that separated employee cards are canceled or deactivated and require maintenance of appropriate documentation to support performance of these actions. As a result, new procedures were developed and a notice was issued to the appropriate parties clarifying roles and procedures for canceling and deactivating separated employee travel

cards. The second final action was complete when procedures were developed to ensure that travel cards were held only by current SBA employees. These procedures also require monthly comparison of the payroll file with open travel accounts.

Business Loan Program

Texas Real Estate Proprietor Pleads Guilty To Bank Fraud. A Dallas, Texas, real estate proprietor, pled guilty on February 6, 2004, to one count of **bank fraud** involving his packaging/brokering of 10 SBA-guaranteed loans. The investigation revealed that he recruited individuals and assisted them with submitting false and fraudulent documents to obtain loan approval. He did this by artificially inflating the borrowers' checking accounts, submitting fraudulent gift letters to represent funds for required down payments, used loan proceeds to purchase cashiers checks in the names of the borrowers, and used these checks to fraudulently represent the borrowers' capital injections. Sentencing has not yet been scheduled. This investigation was initiated based on a referral from the participating lender. The OIG conducted this investigation jointly with the Federal Bureau of Investigation (FBI).

New Jersey Man Indicted. On February 9, 2004, a Forked River, New Jersey, property owner was indicted on one count of **conspiracy** and one count of **making a material false statement**. The indictment relates to an SBA-guaranteed loan obtained by a New Jersey automotive repair business. The investigation revealed that the business owner obtained a loan from a lender in the amount of \$560,000 that required him to make a capital injection of at least \$149,575. The investigation revealed that he did not make the capital injection and conspired with the property owner to fraudulently misrepresent the capital injection. They entered into an \$80,000 mortgage agreement, which was concealed from the lender, in lieu of the capital injection. The business owner defaulted on the entire balance of the loan, which caused SBA to pay the guarantee. The OIG conducted this investigation based on a referral from the lender.

Houston Texas Man Pleads Guilty. A Houston, Texas, man pled guilty on February 9, 2004, to one count of **making a false statement to the SBA** in connection with an attempt to obtain a \$2.7 million loan to

purchase a motel in the Houston area, when the actual price of the motel property was \$2 million. His guilty plea followed a Superseding Information that was filed on February 6, 2004. He was previously indicted on May 15, 2002, and admitted to falsely representing that he currently had \$200,000. The Texas man and his co-defendants were arrested by agents, after signing the SBA loan documents, during a closing held at a local title company. Sentencing is scheduled for May 10, 2004. This investigation was initiated based on a referral from the Houston District Office. The SBA OIG is conducting this investigation jointly with the FBI.

Virginia Business Operator and Attorney Indicted. A Norfolk, Virginia, business operator and an attorney were indicted on February 25, 2004. The business operator was charged with one count of **conspiracy to commit wire fraud** and one count of **conspiracy to make false statements**. The attorney was charged with one count of **conspiracy to make false statements** and two counts of **making material false statements**. The indictment charged the business operator with conspiring to inflate the purchase price of properties by \$1,150,000 to fraudulently obtain loan proceeds. He further conspired to falsely state that he was obtaining a combined gift of \$825,000 to be used as capital injection, knowing that it was not a gift, and that it had to be paid back from the loan proceeds. The attorney's charges involved his preparation of HUD-1 Settlement Statements for the loans that did not reflect true and accurate account of the loan proceeds which he disbursed. The SBA OIG is conducting this investigation jointly with the FBI.

Former New York Pension Plan Manager Sentenced. A former New York, NY, pension plan manager was sentenced on February 27, 2004, to 12 months and 1 day incarceration, to be followed by 3 years of supervised release. The former plan manager was also ordered to pay \$250,000 in restitution. The sentence is the result of his November 22, 2002, guilty plea to **an information** charging him with **embezzlement of employee benefit plan funds**. The investigation revealed that he was responsible for recommending investments of pension funds made through various venture capital firms, including an SBA-licensed SBIC presently in receivership. This investigation was initiated based on a request by the United States Attorney's Office, Eastern District of New York. The SBA OIG conducted this investigation jointly with the Department of Labor OIG.

Chicago Man Arrested. A Chicago, IL, man was arrested and charged in a Federal Complaint on February 10, 2004, with one count of **bribery of a public official** and one count of **submitting a false statement to a financial institution**, in connection with his application for an SBA 504 loan. In his application, he claimed that he was a U.S. citizen. An OIG investigation revealed that he was not a citizen and was residing in the U.S. illegally. When the SBA requested that the Certified Development Company obtain evidence of naturalization, he admitted that he was not a citizen and requested a meeting with the SBA official. At the meeting, he again admitted he was not a citizen, and presented a counterfeit certificate of naturalization for the SBA loan file, and offered a \$5,000 cash bribe to the official to influence an official act. He later returned with \$2,500 cash and requested that the loan be closed without delay. He was arrested outside of the SBA Illinois District Office. The Illinois District Office provided significant cooperation in this investigation. The SBA OIG is conducting this investigation jointly with the Department of Homeland Security.

Government Contracting and Business Development Programs

The OIG Issues Report on a Participant in the Surety Bond Program. On February 20, 2004, the OIG issued Cotton & Company's audit report of the Farmington Casualty Company, a participant in the SBA's preferred surety bond program. The audit found that Farmington complied with SBA's regulations for underwriting and servicing bonds, and for processing claim payments. The audit also found that Farmington correctly calculated and remitted all sample bond fees to SBA in a timely manner.

This monthly update is produced by the SBA OIG, Harold Damelin, Inspector General.

The OIG has established an e-mail address (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:

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

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