



Office of Inspector General U.S. Small Business Administration

September 2008 Update

Business Loan Programs

OIG Issues Report on Audit of Six Guaranteed Loans.

On September 8, 2008, as part of an ongoing review of loan liquidation activities at the National Guaranty Purchase Center (NGPC) in Herndon, Virginia, the OIG issued a report on six loans that were improperly charged off. Full denial of the loan guaranties should have been pursued due to material lender non-compliance with SBA requirements. The deficiencies included: (1) non-disclosure of contaminated property; (2) inadequate evidence of equity injection; (3) inadequate evidence of IRS tax verifications; (4) inadequate appraisals; (5) questionable repayment ability; (6) inappropriate broker fees; (7) unreported adverse events; (8) unsecured collateral; and (9) unapproved and insufficient offers in compromise. While all but one of the six loans received a complete purchase review and all six received a comprehensive charge-off review, the deficiencies were not identified or adequately resolved by SBA. As a result, the OIG recommended that approximately \$1.2 million of improper payments be recovered from the lenders.

Virginia Man Sentenced. On September 5, 2008, a Virginia man was sentenced to 70 months imprisonment, 36 months supervised release, and was ordered to pay restitution of \$3,925,596.87. The sentencing resulted from his guilty pleas to one count of mail fraud and one count of false oaths in a bankruptcy for engaging in an extensive mortgage fraud scheme involving two residential properties he owned. The properties were sold or refinanced despite the presence of a number of liens and judgments, including a judgment related to a defaulted SBA-guaranteed loan. Each time a property was sold or refinanced, he created bogus documents purporting to dismiss the encumbrances and then diverted the loan proceeds for his personal use. The total loss to lending institutions was over \$3.6 million. He also made a false statement under oath in a bankruptcy proceeding.

The OIG conducted this investigation jointly with the Federal Bureau of Investigation (FBI), the U.S. Postal Inspection Service (USPIS), and the U.S. Secret Service (USSS).

Realty Company Owner Indicted. On September 12, 2008, the owner/operator of a New York realty company was indicted on charges of bank fraud and making false statements. The indictment alleges that he failed to disclose other loans totaling \$125,000 when he applied for two SBA*Express* lines of credit totaling \$142,800.

Business Owner Sentenced. On September 4, 2008, a Delaware business owner was sentenced to 51 months in prison, 36 months probation, and restitution of \$1,191,199.82 to be paid jointly and severally with a Delaware state employee. The business owner and state employee previously pled guilty to one count each of conspiracy to commit wire fraud, conspiracy to commit money laundering, and wire fraud. The wire fraud violation related to the business owner obtaining a \$309,000 SBA-guaranteed loan to open a tanning franchise. The investigation revealed that the business owner conspired with the state employee to claim ownership of abandoned stock certificates that did not belong to them by providing false documentation to the State of Delaware, Bureau of Unclaimed Property. The business owner falsely claimed on the loan application that funds for the required equity injection came from inheritance of the stock certificates from his father. The state employee was previously sentenced to 60 months in prison, 36 months probation, and restitution of \$1,245,247.53 to be paid jointly and severally with the business owner. The OIG investigated this case jointly with the FBI and Internal Revenue Service (IRS).

Illegal Immigrant Sentenced in Identity Theft Case. On September 25, 2008, an illegal immigrant was sentenced in the U.S. District Court, Central District of

California, to 12 months and 1 day imprisonment, 60 months probation, and restitution of \$79,790.28. The sentencing resulted from his guilty plea to one count of bank fraud and one count of mail fraud. The investigation revealed that he was one of the principals involved in a sophisticated identity theft ring operated for the purpose of obtaining fraudulent SBAExpress lines of credit, conventional and/or residential loans, and credit cards. In order to obtain financing, he and other known suspects created fictitious businesses and purchased Social Security numbers that were assigned to others. The investigation further revealed that, while he claimed on his SBAExpress loan documents to be a United States citizen, he was actually in the United States illegally. He also claimed that he did not have a prior criminal history when, in fact, he had a prior felony conviction in Canada. The OIG is conducting this investigation jointly with the Los Angeles Police Department, California Department of Insurance, Department of Homeland Security (DHS)/Immigration and Customs Enforcement (ICE), USPIS, and the Social Security Administration-OIG.

Office Manager Sentenced. On September 26, 2008, the office manager for a Colorado plastic surgeon was sentenced to 60 months incarceration and 60 months parole. She was also ordered to pay restitution, with the amount to be determined at a later hearing. She previously pled guilty to one count of felony theft. The investigation revealed that she used the plastic surgeon's personal information and his signature stamp to fraudulently obtain, without his authorization, two SBAExpress loans totaling \$150,000. In addition, she obtained a non-SBA loan for \$180,948 using the same scheme. The office manager used the majority of the loan funds for her personal benefit.

Disaster Loan Program

OIG Issues Report on Early-Defaulted Gulf Coast Hurricane Disaster Loans. On September 12, 2008, the OIG issued an audit report, *Early-Defaulted Gulf Coast Hurricane Disaster Loans*. This audit was initiated in response to the increasing number of defaulted Gulf Coast disaster loans to determine whether loans that failed within 18 months of the due date of the first loan payment: (1) received adequate screening and credit evaluation during the application process; and (2) were serviced in accordance with loan provisions and regulations.

The OIG reviewed a statistical sample of 117 loan files from a universe of 4,985 loans that were at least 90 days delinquent or charged-off as of September 30, 2007. All but 4 of the 117 loans reviewed were either improperly originated and/or inadequately serviced. Approximately 63 percent of the loans were approved even though the applicants lacked repayment ability or were not creditworthy, and 79 percent were inadequately serviced after becoming delinquent. Projecting the sample results to the universe of early-defaulted loans, the OIG estimated that approximately 4,815 loans, totaling \$98.4 million, defaulted early due to loan origination or servicing issues. These deficiencies occurred because the SBA Office of Disaster Assistance (ODA) overstated income and/or understated debt when computing borrowers' repayment ability. In cases where borrowers' credit was found to be unsatisfactory, ODA did not provide adequate justification for applicants' existing unpaid debt, bankruptcies, or unpaid collections.

To ensure that applicant repayment ability and creditworthiness are adequately evaluated, the OIG recommended that ODA's training program re-emphasize that supervisory loans officers must: (1) thoroughly review applicant repayment ability to ensure accuracy; and (2) address all derogatory credit issues before loan approval. ODA concurred with this recommendation and has taken actions to enhance its training program for loan processing staff, has revised its procedures to review loan applications for both creditworthiness and repayment ability, and is conducting additional quality assurance reviews, as needed. The OIG did not make recommendations regarding servicing activities as the Agency addressed identified deficiencies during the audit.

Louisiana Real Estate Agent Indicted. On August 28, 2008, a Louisiana real estate agent was indicted on five counts of false statements and two counts of theft of Government funds. The indictment alleges that she made false statements and submitted false documents to SBA and the Federal Emergency Management Agency (FEMA) in order to receive disaster assistance to which she was not entitled. She was approved for an SBA disaster home loan in the amount of \$125,600, of which \$50,000 was disbursed, and an SBA disaster business loan in the amount of \$291,600, of which \$10,000 was disbursed. She allegedly submitted disaster loan applications that falsely claimed an address in the hurricane area as her primary residence and fraudulently represented that a building permit

authorized repairs. She also is alleged to have submitted two fictitious repair receipts and two fraudulent residential leases. The OIG is conducting this investigation jointly with the DHS OIG.

New York Automotive Seller Sentenced. On August 28, 2008, the former president and owner of a company that sold Hyundai motor vehicles and parts to the United Nations was sentenced to 12 months and one day in prison, 60 months probation, and was ordered to pay restitution to the SBA in the amount of \$646,900. In the wake of the terrorist attacks of September 11, 2001, he applied for and received a \$646,900 SBA disaster loan for his company. He subsequently received a series of two-party checks from the SBA, which were to be used to pay off creditors. Instead, he forged endorsements on several of the checks and deposited them into the company account. He also conspired with a Florida man to obstruct this investigation. The Florida man has pled guilty and is awaiting sentencing. The OIG investigated this case jointly with the USPIS.

Louisiana Woman Charged. On September 24, 2008, a Louisiana woman was charged, via a criminal information, with one count of false statements. She applied for both home and business SBA disaster loans to repair damage from Hurricane Katrina to her residence and rental properties, but she only qualified for one of the loans. She chose to receive the home loan, which had a lower interest rate, and certified to the SBA that she would apply all proceeds of the loan to repair her residential property. She also claimed to have retained a general contractor to perform the repairs for \$130,000. It is alleged that she instead used part of the loan proceeds to repair her rental properties and only retained a contractor for \$16,500 of repairs to her residence. The OIG is conducting this investigation jointly with the Department of Housing and Urban Development-OIG.

Louisiana Pastor Sentenced. On September 24, 2008, a Louisiana church pastor was sentenced to 17 months in prison, 36 months supervised release, and restitution of \$34,754.01. The sentencing resulted from his guilty plea to one count of mail fraud. The pastor, on behalf of his congregation, applied for a \$252,000 SBA physical disaster loan and a \$35,000 Bush-Clinton Katrina Fund grant to rebuild the church following Hurricane Katrina. However, the pastor devised a scheme to instead use the disaster assistance funds for his own benefit. He caused SBA to wire transfer the

initial \$10,000 disbursement to a bank account that he controlled, and also caused the \$35,000 grant to be sent to his home address and deposited into the same account. The OIG conducted this investigation jointly with the FBI.

Mississippi Man Sentenced. On September 30, 2008, a Mississippi man was sentenced to 16 months in prison, 36 months probation, \$13,152 in restitution to FEMA, and full restitution to the SBA, the amount of which will be determined by the U.S. Probation Office at a later date. The sentencing resulted from his guilty plea to one count of theft of government funds. The investigation disclosed that he caused physical damage to his own residence in order to fraudulently receive \$40,000 from SBA, as well as disaster benefits from FEMA. The OIG conducted this investigation jointly with the FBI and the USPIS.

Government Contracting and Business Development

Guilty Pleas for Conspiracy to Defraud SBA. On August 29, 2008, the president/owner of an asbestos abatement company pled guilty to one count of conspiracy to defraud the SBA. On September 8, 2008, an environmental company pled guilty to one count of the same charge. Both companies were participants in the SBA 8(a) program, which requires that a disadvantaged individual have control and ownership of the company. The president and owner of the asbestos abatement company qualified as the disadvantaged individual for that company. In order for both companies to maintain their 8(a) eligibility requirements, the president of the asbestos abatement company and the second company conspired with others to violate SBA requirements related to control and ownership by not disclosing that non-disadvantaged individuals provided critical bonding, insurance, financial support, and control over the companies. Further, between 2002 and 2004 the non-disadvantaged individuals, who previously pled guilty to related charges, received approximately \$900,000 more in bonuses and salaries than the president and owner. The OIG is conducting this investigation jointly with the Environmental Protection Agency (EPA) - Criminal Investigative Division (CID), the Naval Criminal Investigative Service (NCIS), the IRS, and the FBI.

This monthly update is produced by the SBA OIG,
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