



Office of Inspector General U.S. Small Business Administration

January 2009 Update

Business Loan Programs

OIG Issues Report on Audit of the Liquidation Process at the National Guaranty Purchase Center (NGPC).

On January 30, 2009, the OIG issued an audit report on liquidation processing for defaulted 7(a) loans at SBA's NGPC in Herndon, Virginia. The objectives of the audit were to determine whether (1) the Center's liquidation process, which culminates in loan charge-off, identified and addressed lender noncompliance with SBA's procedures to mitigate losses, and (2) the Center adequately managed loans in liquidation status.

To address the first objective, we reviewed a sample of 54 loans—totaling \$6.1 million—out of a universe of 7,120 loans—totaling \$696 million—that had been charged off between October 2005 and July 2007. We found that, for 21 of the 54 charged-off loans, the Center's purchase and liquidation processes did not identify or address lender deficiencies that merited repair or denial of guaranties totaling \$1.4 million. Based on the sample results, we estimated that SBA made at least \$23 million in improper payments on the 7,120 loans charged off between October 2005 and July 2007. A number of factors contributed to the inadequate loan reviews, including lack of management emphasis on oversight due to the Center being located organizationally under the Office of Capital Access (OCA). In addition, contract staff hired to conduct charge-off reviews were not adequately trained or supervised and did not seek additional support from lenders when documentation in the loan files was inadequate to demonstrate compliance.

To address the second objective, we reviewed a sample of 60 loans—totaling \$15 million—that had not been charged off, out of a universe of 9,143 loans—totaling \$1.4 billion—that were in liquidation between July 2006 and July 2007. The review disclosed that 46 of the loans (77 percent) were in liquidation status for

an average of 3 years and were not properly monitored to determine whether (1) improper payments and liquidation proceeds due SBA had been recovered, (2) loans were charged off or removed from the portfolio when appropriate, or (3) outstanding loan balances were correct. As a result, the Center did not timely recover approximately \$2.6 million in improper payments and liquidation proceeds, timely charge-off or remove 44 loans from the liquidation portfolio, or correctly report the outstanding balances on two loans. Based on the results, we estimated that at least 6,034 loans in liquidation as of July 31, 2007, had overstated values of at least \$324 million. Loans in liquidation were not properly managed because the Center focused most of its resources on purchase activities as it was insufficiently staffed and under pressure by lenders to expediently pay guaranties. Further, SBA did not have a portfolio management system to identify when actions were needed on loans.

We made six recommendations to (1) mitigate deficiencies found in the Center's liquidation process, (2) allow the Center to better manage its liquidation portfolio, and (3) improve lender oversight.

Results of Ongoing Investigation. The following case is part of an ongoing investigation, being conducted jointly with the U.S. Secret Service (USSS), relating to a scheme in which a non-bank lender's former executive vice president and others not employed by the lender conspired to fraudulently qualify loan applicants for SBA-guaranteed loans.

- On January 9, 2008, a Michigan man pled guilty to a one-count criminal Information charging him with making a false statement for the purpose of influencing the action of the SBA. The Information alleges that he signed a HUD-1 Settlement Statement falsely representing that he paid a \$510,000 deposit for the purchase of two gasoline stations.

Disaster Loan Program

Operator of Seafood Business Pleads Guilty. On January 5, 2009, the operator of a seafood business in Port Arthur, Texas, pled guilty to one count of making a false and fraudulent statement. He submitted a disaster loan application to the SBA in which he claimed the company had a business location in Abbeville, Louisiana, that had sustained an estimated \$2.8 million in disaster damage resulting from Hurricane Rita. He also submitted a false Commercial Lease Agreement showing that the company occupied real property in Abbeville during Hurricane Rita, as well as fraudulent invoices that falsely showed more than \$1.9 million in hurricane-related repair expenses. In fact, at no time did he own or operate a business in Abbeville, Louisiana. The SBA OIG conducted this joint investigation with the Bureau of Alcohol, Tobacco, Firearms, and Explosives and the Department of Homeland Security OIG.

Government Contracting and Business Development

Maryland Business Owner Sentenced. On January 22, 2009, the owner of a construction and demolition company located in Elkridge, Maryland, was sentenced to serve 45 days in jail, 6 months home confinement, and 3 years probation, and was ordered to pay \$82,299 in restitution to the Internal Revenue Service (IRS) and a \$100 special assessment fee. He was previously charged in a sealed criminal Information and pled guilty to one count of failing to pay over taxes to the IRS. The Information and plea were unsealed at the time of sentencing. The investigation revealed that the business owner deducted and collected Federal Insurance Contributions Act taxes from the total taxable wages of his employees and did not account for or pay over the amount due to the IRS. These violations were discovered during an investigation of a licensed abatement contractor and former SBA 8(a) certified firm in Baltimore, Maryland, for which the man's company worked. The SBA OIG conducted this joint investigation with the Environment Protection Agency - Criminal Investigative Division; the Naval Criminal Investigative Service; the Internal Revenue Service - Criminal Investigative Division; and the Federal Bureau of Investigation.

Agency Management

OIG Issues Report on System Access by Contractors Without Security Clearances. On January 26, 2009, the OIG issued a report on a review of system access by contractors without security clearances, which found that SBA did not consistently ensure that contractors were properly vetted prior to granting them access to sensitive SBA systems and data, and did not consistently report and track this vulnerability in its *Plan of Action and Milestones* (POA&M). This review supplemented the OIG's evaluation of the Agency's *Federal Information Security Management Act* (FISMA) implementation for Fiscal Year 2008. We recommended that the Chief Information Officer (CIO): (1) require system owners to confirm that all contractor personnel with access to sensitive systems and data have background investigations and clearances commensurate with SBA policy; (2) immediately suspend system access for any contractors who do not comply with SBA background investigation and security clearance policies; (3) notify Contracting Officer's Technical Representatives of SBA's system access requirements related to contractor personnel; (4) require that Certification and Accreditation reviews and the security self-assessments determine whether contractor employees have the required background investigations and clearances for system access; (5) develop guidance on how contractor access vulnerabilities should be rated and reported in the quarterly and annual POA&M reports; and (6) require documentation justifying removal of previously reported vulnerabilities from the POA&M.

Former SBA Employee Pleads Guilty. On January 22, 2009, a former SBA attorney in Fort Worth, Texas, pled guilty to two counts of online solicitation of a minor, a state of Texas third-degree felony. He was sentenced the same day to 5 years deferred adjudication, a \$3,000 fine, and immediate surrender to the Denton County Jail to serve a 90-day sentence. The OIG conducted this investigation jointly with the Texas Rangers.

This monthly update is produced by the SBA OIG,
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