



Office of Inspector General Small Business Administration

June 2002 Update

Business Loan Programs

Texas Restaurant Owners Indicted for Insurance Fraud. A Houston, Texas, couple that owned a restaurant were each indicted on May 1, 2002, on one count of **insurance fraud**, by a Grand Jury in Harris County, Texas. The charges arose out of a fraudulent property insurance policy that the couple purchased to satisfy the closing requirements for a \$150,000 SBA-guaranteed loan. A fire destroyed the restaurant 3 days after the bank approved the loan. The couple concealed the extent of the fire from the bank and obtained disbursement of the loan. At the closing, the wife signed a general security agreement that required her to maintain collateral insurance at the restaurant premises. After proof of insurance was provided, the bank disbursed the loan proceeds, unaware that the couple was no longer operating the restaurant. Subsequently, the wife allegedly filed a fraudulent claim on the insurance policy and defaulted on the loan. Initially, the husband applied for the loan; however, his name was removed from the application because of his criminal history. SBA/OIG conducted this investigation jointly with the Bureau of Alcohol, Tobacco and Firearms.

Arizona Business Executive Sentenced for Making Material False Statements. An Arizona business executive was sentenced on May 22, 2002, to 90 days of community confinement, 90 days home detention, and 3 years of supervised release, and was ordered to pay a \$5,000 fine and \$172,000 in restitution. He had pled guilty to one count of **making a material false statement** to obtain a \$900,000 SBA-guaranteed loan for the purchase of six fast food franchises. The investigation disclosed that, at the direction of his

business brokerage firm, the defendant submitted false financial information in order to obtain the loan. Specifically, he claimed on his "Personal Financial Statement" form that he had \$140,000 worth of stock in restaurants and that he had \$471,949 in "earned fees." The investigation revealed that although he knew about the SBA's cash injection requirement, he did not have the cash necessary to close the loan. As a result, he agreed to allow his business brokerage firm to obtain a temporary cash injection from a third party. In order for the scheme to work, the defendant arranged to obtain a real estate sales license so that he could receive a commission for the sale of the six franchises he purchased through the business brokerage firm. The defendant knew that a portion of the commission would be used to repay the third party that made his cash injection. As reported previously, the couple that operated the business brokerage firm was indicted on March 22, 2001, on one count of **conspiracy**, six counts of **wire fraud**, three counts of **making material false statements**, and five counts of **money laundering**. The case was a joint investigation with the Federal Bureau of Investigation (FBI) and was based on a referral from the SBA Arizona District Office.

New Jersey Plating and Finishing Company President and Two Principals Sentenced for Environmental Charges. A principal of a now defunct metal plating company in East Rutherford, New Jersey, its successor metal and plating company, and a principal of the successor company were sentenced on May 31, 2002, on fraud and environmental charges. The president of the successor company was also sentenced on environmental charges. The president and a principal of the original company each received 18 months probation. The president of the original company was

fined \$4,000 and ordered to make restitution to the State of New Jersey in the amount of \$25,000. The principal of the original company was fined \$3,000 and ordered to make restitution to New Jersey in the amount of \$75,000. The president of the successor company received 5 years probation, was fined \$4,000, and was ordered to make restitution to the State in the amount of \$125,000. The successor company was fined \$5,000. The sentences resulted from the defendants' guilty pleas on December 21, 2001, to charges of **unlawful storage of hazardous waste in the third degree, and theft by failure to make required disposition of property received in the third degree.** The pleas were based upon two indictments on October 17, 2000. One related to a \$500,000 SBA-guaranteed loan in December 1996. The indictment alleged that the defendants had failed to purchase machinery and fixtures for which the loan was intended, provided a forged landlord waiver in applying for the loan, and knowingly passed three forged checks to banks.

Although the original company was also indicted along with its principals, those charges were later dropped because the company no longer existed. The second indictment alleged that the same defendants, along with the successor company and its president, violated the Water Pollution Control Act by discharging chemical and industrial wastes associated with the process of metal plating. The president of the successor company pled guilty to two counts of **unlawful storage of hazardous waste in the third degree.** The successor company pled guilty to **causing the abandonment of hazardous waste and toxic pollutants in the second degree.** SBA/OIG participated in the investigation at the request of the State of New Jersey, Division of Criminal Justice, and was later joined by the U.S. Environmental Protection Agency OIG.

Texas Businessman Sentenced for Bank Fraud. A Plano, Texas, businessman was sentenced on June 3, 2002, to 4 months incarceration, 4 months home confinement, and 5 years supervised release. He was also ordered to pay \$99,191.14 in restitution to a bank in Oklahoma. He had pled guilty to a one-count charge of **bank fraud** for fraudulently influencing the bank to fund \$105,340 in proceeds from an SBA-guaranteed loan. The investigation revealed that he presented documents to the bank representing that his company had purchased equipment for \$131,675.43, when in fact no such purchase was made. The case

was a joint investigation with FBI and was initiated based on a referral from the Oklahoma District Office.

Kentucky Construction Company Employee Sentenced for Misdemeanor Fraud. A former employee of a roadside construction company in Louisville, Kentucky, was sentenced on June 6, 2002, to 3 years probation. He had pled guilty to a one-count charge of **misdemeanor fraud** for knowingly converting collateral that was pledged to SBA to his personal use. The defendant worked for his brother and his brother's partner. The brother and his partner obtained a \$250,000 (75 percent) SBA-guaranteed loan. As reported previously, his brother and his partner pled guilty to a criminal information that charged both with **conspiracy to defraud the Government** by submitting fraudulent invoices to influence the bank to disburse the loan. In addition, his brother and his partner allowed a company vehicle to be individually titled to the defendant with the proceeds from the sale of the vehicle to be retained by the defendant for personal use. As reported previously, the defendant's brother was sentenced to 6 months home confinement and 2 years probation. His brother's partner is scheduled for sentencing on August 7, 2002. The court will determine the amount of restitution to be ordered at a later date. The investigation was initiated based on information received from the Kentucky District Office.

Small Business Investment Companies

Former New York Specialized Small Business Investment Company Board Member Sentenced for Conspiracy and Mail Fraud. A former board member of a now-defunct specialized small business investment company (SSBIC) in Rockland County, New York, was sentenced on May 22, 2002, to 6 years incarceration, followed by 3 years probation. The defendant was also ordered to pay \$11,659,499 in restitution to other Government agencies. He had pled guilty to **conspiracy and mail fraud** charges. The charges related to his participation in schemes to defraud the Government of tens of millions of dollars from various Federal programs, including SBA's SSBIC program. The plea resolved his 1997 indictment (along with six other defendants, including his son) on 21 counts of **conspiracy, embezzlement of Federal program funds, making material false statements, mail fraud, wire fraud, mortgage fraud, and money laundering.** As an SSBIC board

member, the defendant misappropriated SBA funds by extending loans to small businesses affiliated with the SSBIC's officers and directors and concealed these improper loans by submitting fraudulent documents to SBA. When he failed to appear in court to face the charges in his 1997 indictment, a warrant was issued for his arrest. After an extensive search, he was located in Israel, where he had obtained Israeli citizenship, and was arrested by Israeli police in February 1999 in response to a formal request submitted by the U.S. Department of Justice. After extensive legal proceedings, the Supreme Court of Israel ordered the extradition of the defendant, who was returned to the United States in November 2001. He was one of the first fugitives to be extradited to the United States under an Israeli law, enacted in April 1999, which permits the extradition of Israeli citizens. SBA/OIG's investigation was based on information received from the Internal Revenue Service and was worked jointly with IRS and OIGs of the U.S. Departments of Education and Housing and Urban Development.

Entrepreneurial Development

Agency Takes Final Action on Two Recommendations Made as a Result of Audit of Women's Business Center. The Agency completed the final action on two recommendations made in Audit Report 1-17, Vermont Women's Business Center. The recommendations were to have the grantee: 1) correct and resubmit any inaccurate reports previously submitted to SBA for year 1 of the award along with supporting accounting records; and 2) correct and resubmit any inaccurate reports previously submitted to SBA for year 2 of the award along with supporting accounting records in order to provide SBA with a true reflection of the financial status of the VWBC to date. As a result, SBA received and accepted all year 1 and year 2 corrected reports and supporting accounting records, however, for the year 2 the women's business center changed its calculation of the amount due to the grantee from \$70,000 to \$69,700. To view the report and its recommendations, please visit our website at <http://www.sba.gov/IG/1-17vwbc.pdf>

Government Contracting and Business Development

North Carolina Businessman Pleads Guilty to Mail Fraud. The president of a Raleigh, North Carolina, construction company and the company pled guilty on June 3, 2002, to a one-count charge of **mail fraud**. In order to induce disbursements of contract funds, the defendant submitted false payment certification requests under various Army, Navy, Postal Service, and Veterans Administration (VA) Section 8(a) contracts, stating that all subcontractors and vendors were paid. Under the plea agreement, the defendant acknowledged responsibility for the false statements that resulted in total losses of almost \$1.3 million on 10 separate Government contracts (3-Army; 2-VA; 4-Navy; 1-Postal Service). The Government lost an additional \$700,000, as a result of having to re-issue numerous task orders on several contracts that were not completed by the company. In addition, he and the company agreed to a permanent injunction (debarment) barring him and/or any entity in which he might have a financial interest from doing business as a general contractor, subcontractor, vendor, or supplier with the United States Government. SBA/OIG initiated this investigation based on a referral from Army Criminal Investigation Division in Raleigh, North Carolina.

Missouri Contract Company and its President Sentenced for Mail Fraud. The president of a Poplar Bluff, Missouri, contracting company and his corporation were both sentenced on June 24, 2002, pursuant to a modified plea agreement also filed that day. The defendant was placed on probation for 3 years, ordered to pay a \$30,000 fine, \$108,771.12 in restitution, and a \$300 special assessment. All funds were due immediately upon sentencing, with his restitution to be allocated as follows: \$95,000 to SBA, \$12,101.80 to an insurance company, \$1,000 to another insurance company, \$463 to one former employee, and \$206.92 to another former employee. The company was placed on probation for 5 years, ordered to pay a \$48,000 fine, \$90,771.72 in restitution, and a \$600 special assessment. Again, all funds were due immediately with the company's restitution to be allocated as follows: \$77,000 to SBA, and the remainder to be allocated as above since the president and company were jointly and severally liable for an amount totaling \$13,771.72. The defendant and the company had previously pled guilty to three counts of **mail fraud** after the defendant admitted he intentionally devised a scheme to defraud and obtain money from insurance companies that insured the company's

property and equipment. A joint investigation with the U.S. Department of Labor OIG, and FBI had resulted in a 12-count indictment against the defendant and the company for illegal **kickbacks, mail fraud, false statements** to SBA, and major **contract fraud** against the United States. All counts other than mail fraud were dismissed as part of the plea agreement at sentencing. The false statement and contract fraud counts dismissed alleged that the defendant submitted false statements and fraudulent documents to SBA in a scheme to obtain Section 8(a) status and related contracts, falsely claiming to be a Cherokee Indian and to have suffered resulting economic disadvantage. Although these counts were dismissed as part of the plea agreement, the defendant and the company agreed to be forever barred from participation in all SBA programs and were ordered to make restitution to SBA totaling \$172,000. The defendant and the company further agreed to return all equipment received under the Section 8(a) surplus equipment program. The company had acquired Federal surplus equipment that had cost the Government \$149,836.73, by paying only \$18,473. As a result of the indictment, the defendant and the company were suspended by the Department of Defense from receiving all new Government contracts. This case remains open pending further civil and administrative action.

Agency Management

Agency Takes Final Action on One Recommendation Made as a Result of the FY 2000 Financial Statements Management Letter. The Agency completed final action on one recommendation made in Audit Report 1-15, SBA's FY 2000 Management Letter. The recommendation was to train the field office liquidation staff in valuing foreclosed property and entering data in the Liquidated Loan Tracking System and the Loan Accounting System. SBA issued an Information Notice and revised the liquidation training to include net realizable value. To view the report and its recommendations, please visit our website at <http://www.sba.gov/IG/1-15FY2000.pdf>.

Agency Takes Final Action on Two Recommendations Made as a Result of the FY 2001 Financial Statements Audit. The Agency completed final action on two recommendations made in Audit Report 2-04, SBA's FY 2001 Financial Statements. The recommendations were that: 1) the Director of the Office of Financial Assistance fully implement quality assur-

ance procedures over the subsidy re-estimation process, and 2) the Chief Financial Officer prepare consolidated Agency-wide financial statements on a quarterly basis. The Agency implemented quality assurance procedures over the subsidy re-estimation process and has issued quarterly reports for seven consecutive quarters. To view the report and its recommendations, please visit our website at <http://www.sba.gov/IG/02-04.pdf>

Agency Takes Final Action on One Recommendation Made as a Result of the FY 2001 Financial Statements Management Letter. The Agency completed final action on one recommendation made in Audit Report 2-17, SBA's FY 2001 Management Letter. The recommendation was that the Assistant Administrator for Administration issue a procedural notice to all Agency purchase credit cardholders and approving officials emphasizing the current policy in the standard operating procedure. The notice was issued on June 4, 2002. To view the report and its recommendations, please visit our website at <http://www.sba.gov/IG/02-17.pdf>

Agency Takes Final Action on Four Recommendations Made as a Result of Sensitive Payments Audit. The Agency completed final action on four recommendations made in Audit Report 1-20, Sensitive Payments. The report recommended that: 1) the Chief Financial Officer (CFO) develop detailed procedures to ensure that all vouchers are thoroughly reviewed and documentation verified; 2) the CFO provide additional training to voucher examiners; 3) the Office of Administration issue a procedural notice to remind all SBA offices of the need to follow SOP 00 12 regarding record retention of credit card statements and supporting documentation; and 4) that the Office of Administration issue a procedural notice to remind all SBA offices of the need to follow SOP 00 12 regarding use of and requirements for proper completion of SBA Form 2. In response, SBA: 1) updated the documentation for its travel review procedures and created a mandatory examination group for vouchers deemed most sensitive and added an additional independent review before any payment is made; 2) conducted training on the new administrative accounting system and the travel voucher process; and 3) issued a procedural notice reminding employees of the requirement to retain credit card statements and supporting documentation and the requirements for proper completion of the SBA requisition form.

The activity Update is produced by SBA/OIG,
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