



Office of Inspector General U.S. Small Business Administration

November 2009 Update

Business Loan Programs

Review of the Recovery Act's Impact on SBA Lending. On November 25, 2009, the OIG issued a report on an initial review of the Recovery Act's impact on SBA lending. The objectives of the review were to provide transparency on SBA loan activity and lender participation under the Recovery Act and to determine the impact of program changes on the levels and characteristics of SBA lending.

The review determined that both 7(a) and 504 lending increased sharply under the Recovery Act—from March 2009 to July 2009, 7(a) and 504 loan approvals jumped 39 percent and 73, respectively. While this improvement was significant, both 7(a) and 504 loan approvals remained below 2008 and 2007 levels. Small and medium lenders in the 7(a) program recovered more quickly—with loan activity returning to year-ago levels—and took on a larger share of SBA lending. As a result, loan activity was more widely dispersed under the Recovery Act, with the top 20 lenders accounting for 38 percent of all 7(a) loans (excluding *SBAExpress*) compared to 53 percent in 2007.

The review also found an increased trend toward SBA-approved loans, which could impact Agency staffing requirements and program risk. In the 7(a) program, the number of SBA-approved loans more than doubled from March to July. Without adequate training and supervision, the increased demands on SBA loan center staff could impact the quality of Agency loan reviews. The shift towards SBA-approved loans was also substantial in the 504 program, with the share of Agency-approved loans jumping to 94 percent of total loan approvals, from 80 percent 2 years ago. Efficiency gains in Agency processing times, combined with weaker economic conditions, may have reduced the incentive for Certified Development Companies (CDC's) to use their delegated authority to

approve loans. If CDC's continue to send more loans to SBA for approval, the Agency would lose the CDC's contribution to any losses should these loans default.

SBA management generally agreed with the report's findings and noted that, in anticipation of the increased loan transactions under the Recovery Act, the Agency took a disciplined approach to developing staffing estimates to forecast staff capacity needs and recruited staff with previous lending experience and expertise that would be able to process loans faster than less experienced new hires. Additionally, management noted that they will continue to actively monitor 504 program performance in light of increases in SBA-approved loans.

Colorado Business Owner Pleads Guilty. On November 6, 2009, the part owner of a Cortez, Colorado construction company pled guilty to one count of submitting a false loan application. In order to receive two SBA-guaranteed loans totaling \$1.35 million, he hid his criminal history. Criminal history records showed that he pled guilty to embezzling over \$115,000 from a New Mexico industry group while serving as its Executive Director, and he also pled guilty to a third-degree assault charge in 1994. The total estimated loss on the two loans is \$970,000. This case was initiated based on a referral from the Federal Bureau of Investigation (FBI) and the OIG is conducting this investigation jointly with the FBI.

Maryland Business Owner Pleads Guilty. On November 10, 2009, the owner of a restaurant supply company in Cambridge, Maryland, pled guilty to one count of conspiracy. The investigation disclosed that, in March 2007, she entered into an agreement with the owner of a Lusby, Maryland restaurant to perform construction/renovation work and provide equipment at a cost of \$145,000. It is alleged that the restaurant

owner subsequently asked the supply company owner to falsely represent the total cost of the project to be \$295,000 and, in support of the restaurant owner's loan application, to submit a copy of the false contract to an SBA lender. The restaurant owner then obtained a 75 percent SBA-guaranteed loan in the amount of \$417,000. After the owner of the equipment supply company received the initial disbursement from the loan proceeds, she rebated \$97,000 back to the restaurant owner, who has also been charged in this case.

Georgia Businessman Indicted. On November 10, 2009, the president of a sports bar and mortgage brokerage firm in Snellville, Georgia, was indicted on one count of bank fraud and one count of false statements. The indictment alleges that, in conjunction with an application for a \$1.8 million SBA-guaranteed loan, he submitted falsified Internal Revenue Service and SBA documents showing (1) gross sales of approximately \$23 million for the mortgage brokerage firm, when actual reported sales were only about \$250,000, and (2) that he had no previous criminal history, when in fact he had been arrested and convicted on numerous occasions.

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 November 20, 2009, a Michigan man was sentenced to 24 months incarceration and ordered to pay an SBA lender and a financial institution \$4,572,928 and \$1,100,000, respectively, in restitution. The restitution payments are to be paid jointly with other co-conspirators, who were also charged in the case. The Michigan man previously pled guilty to a two-count federal information charging him with conspiracy to defraud the SBA and a Dearborn, Michigan financial institution. The first count relates to false statements as to material facts on SBA-guaranteed loans made by lenders in Troy, Michigan and Knoxville, Tennessee. The false statements included counterfeit bank documents and checks used to verify the required borrower equity injection on at least 9 SBA-guaranteed loans. The second count relates to a scheme to

defraud a financial institution by using a non-sufficient funds credit card convenience check to obtain an official check from the financial institution in the amount of \$1,680,000. The official check was used to close on the purchase of a Bloomfield, Michigan house with the intent to promptly resell or "flip" the property to a straw buyer who would use 100% financing to pay a substantially inflated price for the house.

Agency Management

Audit of SBA's Fiscal Year 2009 Financial Statements. Pursuant to the Chief Financial Officer's Act of 1990, on November 13, 2009, the Independent Auditors' Report and accompanying reports on internal control and compliance with laws and regulations were issued for the fiscal year ending September 30, 2009. The audit, which was performed by KPMG LLP under a contract with the OIG, found that SBA's consolidated financial statements presented fairly, in all material respects, the financial position of the Agency as of and for the years ending September 30, 2009 and 2008. The financial statements also presented fairly, in all material respects, SBA's net costs, changes in net position, budgetary resources, and combined statements of budgetary resources for the years then ended. With respect to internal control over financial reporting, the independent auditors reported a material weakness over financial reporting, and continued to report a significant deficiency related to information technology security controls. KPMG's test for compliance with certain laws, regulations, contracts, and grant agreements determined that SBA did not fully comply with the Debt Collection Improvement Act of 1996 because the Agency did not consistently follow Treasury guidelines for referring delinquent debts for collection. The Agency concurred with the independent auditor's finding and agreed to implement the recommendations.

This monthly update is produced by the SBA OIG,
Peggy E. Gustafson, Inspector General.

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