



Office of Inspector General

September 2015



Business Loans

SBA Receives \$937,500 Cost Avoidance for Two SBA Guaranteed Loans of \$900,000 and \$350,000

On August 12, 2015, the U.S. Small Business Administration (SBA) received a \$937,500 cost avoidance relating to two SBA-guaranteed loans approved by a bank to an Arizona medical equipment firm. One loan was in the amount of \$900,000, and the other loan amount was \$350,000. The bank agreed not to request a loan guaranty from SBA as a result of evidence uncovered during the investigation suggesting a lack of due diligence on the lender's part. The ongoing investigation found various problems in the loan processing and approval process. The SBA Office of Inspector General (OIG) is working on this case jointly with the Internal Revenue Service (IRS) Criminal Investigation (CI) and the Federal Bureau of Investigation (FBI).

California Woman Pleads Guilty to Conspiracy by Misapplying Bank Funds for SBA Loans

On September 25, 2015, a California woman pled guilty to conspiracy in Federal court. She had worked as a vice president and manager for SBA loans at a bank. Although she did not have direct authority to lend bank funds, she reviewed borrowers' applications and recommended that loans be approved and funds disbursed.

Consequently, the woman conspired

with others to misapply bank funds. The conspiracy's purpose was to issue loans under favorable terms to unqualified or under-qualified borrowers so that the conspirators could personally enrich themselves, while knowing these disbursements served no benefit to the bank. Enrichment was in the form of personal payments from borrowers and compensation from the bank for inflated lending performance. She and the others supported the disbursement of bank funds by supplying or knowingly accepting false and fraudulent information in the borrowers' loan applications and by overlooking negative aspects of the borrowers' creditworthiness. This is an ongoing joint investigation with the FBI, Treasury Inspector General for Tax Administration, Federal Deposit Insurance Corporation, and Federal Housing Finance Agency OIG.

SBA Needs to Improve its Oversight of Loan Agents

On September 25, 2015, OIG issued Audit Report 15-16, *SBA Needs to Improve its Oversight of Loan Agents*. This report is the second of two and presents the results of OIG's audit of the Small Business Administration's oversight of loan agents.

Loan agents frequently play an important role within SBA lending programs, often facilitating access to capital by connecting borrowers in search of financial assistance with lenders offering SBA products or by providing other services. However, at times, these third-party relationships have resulted in SBA program loss and risk. Since 2005, SBA

OIG has investigated at least 22 cases with confirmed loan agent fraud totaling at least \$335 million. Further, our analysis determined that loan agents were involved in approximately 15 percent of all 7(a) loans and resulted in increased risk of default.

In 2000, OIG identified loan agent tracking and enforcement as an SBA management challenge that continues to this day. Since December 1, 2010, SBA recorded over 51,000 7(a) loan agent compensation disclosures, representing a variety of services. However, we found the quality of SBA's loan agent data was poor and materially incomplete. Further, although previously recommended in 1998, SBA had not established effective controls over the tracking and monitoring of loan agent performance and therefore, could not adequately assess potential risks or identify problem agents. Finally, SBA had not established a method to track loan agents and their compensation on 504 loans.

OIG recommended nine actions that will help strengthen SBA's oversight of loan agents and their relationships with SBA lenders. The Agency agreed with OIG's findings and recommendations, and has already taken some steps to improve its oversight of loan agents.

Missouri Businessman Sentenced to Imprisonment For Using False Documents to Support \$695,000 Defaulted Loan

On September 29, 2015, a Missouri businessman and former president of a wireless communications firm was sentenced in Federal court to imprisonment of 1 year and 1 day, as well as 3 years of supervised release. He previously pled

guilty to using a false document in connection with a defaulted \$695,000 SBA loan to his business.

The businessman made misrepresentations when applying for an SBA Section 7(a) guaranteed loan through a bank. Specifically, he stated that seven individuals owned shares of his firm in the aggregate of 20 percent of the company's total value when, in fact, none of these individuals owned any interest in or portion of the firm. The SBA loan defaulted within a few months after approval.

The businessman was 1 of 17 defendants charged in a complex scheme to defraud SBA. He was initially charged via a 185-count indictment for his involvement in a bank fraud scheme that took advantage of SBA's guaranteed business loan program. This is a joint investigation with the FBI.

Former SBA Branch Manager Sentenced and Ordered to Pay \$91,885 in Restitution

On September 29, 2015, a former SBA branch manager in Missouri was sentenced in Federal court to 3 years of probation and was ordered to pay restitution of \$91,885. He previously pled guilty through a *nolo contendere* plea to submitting a false document to SBA. The man had falsely reported on his confidential financial disclosure report that he had no reportable liabilities and no reportable outside positions when, in fact, he was the managing member of a custard stand in Texas. He also had obtained an SBA guaranteed loan of approximately \$80,000 for this business.

The former SBA manager was 1 of 17 defendants charged in a complex

scheme to defraud the Agency. He was initially charged via a 185-count indictment for his involvement in a bank fraud scheme that took advantage of SBA's guaranteed business loan program. This was a joint investigation with the FBI.

The OIG High-Risk 7(a) Loan Review Program

On September 30, 2015, OIG issued Management Information Memorandum 15-17, *The OIG High-Risk 7(a) Loan Review Program*, which provided an update on our oversight activities of the High Risk 7(a) Loan Review Program from April 2015 to September 2015. This memorandum contains no recommendations.

We identified potential material lender noncompliance with SBA's requirements on two of the four high-dollar/early-defaulted loans reviewed during this period. SBA honored its guaranty on these two loans for approximately \$2.9 million, and we intend to present our findings to SBA management in a future report for appropriate action. Moreover, it appeared that the lender materially complied with SBA's origination and closing requirements on the other two loans we reviewed. SBA honored its guaranty for approximately \$2.3 million on these two loans.

Finally, we identified material lender deficiencies with one other high-dollar/early-defaulted loan during a previous audit. This loan was referred to our Investigations Division due to suspicious activity. During the current reporting period, we referred this loan to SBA management to address the material lender deficiencies, as appropriate. Because this loan was purchased in October 2010, we did not make any formal recommendations to SBA.

Disaster Loans

New Jersey Man Pleads Guilty to Theft By Deception for Filing False Applications for Hurricanes Irene and Sandy Disaster Funds

On September 8, 2015, a New Jersey man pled guilty in State court to theft by deception and agreed to pay \$33,269 in restitution to the Federal Emergency Management Agency (FEMA) for filing false applications to collect Federal relief funds after Hurricanes Irene and Sandy. The man and his girlfriend previously had been indicted in June 2015. The two individuals had obtained a FEMA rental assistance grant by asserting that they were forced to relocate to a rental home because of storm damage to their primary residence during Hurricanes Irene and Sandy. In reality, the couple was never forced to relocate.

Although the man did not submit a disaster loan application to SBA, his girlfriend had contacted SBA for assistance about applying for a related loan since the deadline for Hurricane Irene disaster loan applications had expired. SBA declined a disaster loan application from her for Hurricane Sandy in April 2013. This continuing investigation is being worked jointly with a task force comprised of the New Jersey Department of Community Affairs (DCA), the U.S. Department of Homeland Security (DHS) OIG, and the U.S. Department of Housing and Urban Development (HUD) OIG, under the direction of the New Jersey Office of the Attorney General.

New Jersey Couple Enters Pretrial Intervention for Fraudulently Applying for Hurricane Sandy Disaster Funds

On September 21, 2015, a New Jersey couple entered pretrial intervention after previously having been charged in State court with theft by deception and unsworn falsification. As a result of their fraudulent applications, they received \$26,552 in Hurricane Sandy relief funds. The couple obtained \$6,730 in FEMA rental assistance, which they returned after the investigation began. They also received a \$10,000 Homeowner Resettlement Program grant and \$9,822 paid to a home design firm on their behalf from the Reconstruction, Rehabilitation, Elevation and Mitigation Program, which was funded by HUD and administered by the New Jersey DCA. The couple paid restitution of \$19,822.

The investigation disclosed that the individuals falsely claimed on their applications that a storm-damaged home they owned was their primary residence when it was actually their vacation home. They also applied for an SBA disaster home loan which was declined because SBA determined it was an ineligible real property. The woman was an employee of the New Jersey DCA, and the man was an employee of the New Jersey State Department of Treasury. Both resigned their positions. This investigation was conducted jointly with a task force comprised of the New Jersey DCA, DHS OIG, and HUD OIG, under the direction of the New Jersey Office of the Attorney General.

Government Contracting

Maryland Man and Company Debarred for Fraudulently Enrolling in 8(a) Program

On September 8, 2015, the U.S. Department of the Navy debarred a man and his Maryland-based Section 8(a)-certified firm from directly or indirectly receiving the benefits of Federal assistance programs for 5 years. The man had provided information to SBA during his 8(a) application process disclosing that he was a Federal employee serving in a position that included construction manager duties for the Naval Facilities and Engineering Command, of Washington, DC, while also operating his firm. Moreover, the investigation disclosed that he violated ethical standards by engaging in outside employment and business activities without seeking approval. Finally, he failed to disclose his outside position as the firm's president and chief executive officer on his Office of Government Ethics forms in 2011 and 2012. The Navy's debarment decision was based on a joint investigation conducted with the Naval Criminal Investigative Service.

General Manager Pleads Guilty for SDVOSB Conspiracy

On September 9, 2015, the general manager and part owner of a Virginia-based Government contractor that claimed service-disabled veteran-owned small business (SDVOSB) status pled guilty to conspiracy in Federal court. The man agreed to forfeit \$322,800. The plea resulted from an investigation into allegations that he conspired with other SDVOSBs to obtain Federal contracts through fraud and misrepresentation.

Specifically, the general manager directed his firm's employees to conspire with other SDVOSBs to submit what appeared to be competing bids for Federal Government contracts, when in fact they knew the bids were not competitive. The man, his firm's employees, and employees of other SDVOSBs would identify Government contracts to bid on and prepare bids for one another using the bid templates of each other. He would then direct his employees and other SDVOSB employees to submit the completed bids to the Federal Government as their own. He and employees of the other SDVOSBs knew and understood that these bids were not true competitive bids. This practice restricted legitimate competition by creating the false impression that the Government had already received multiple competing bids.

In addition, the general manager worked with co-conspirators within the Government to gain access to internal Government documents, such as internal Government cost estimates, before bidding on contracts. He agreed to pay these co-conspirators for a competitive advantage on contracts totaling approximately \$33 million. This investigation continues and is being worked in conjunction with DHS OIG, Department of Veterans Affairs OIG, General Services Administration (GSA) OIG, and the Department of Justice.

President of Ohio-Based Firm Sentenced to 1-Year Imprisonment, 2-Year Supervised Release, and \$6.75 Million in Restitution

On September 14, 2015, the president of an Ohio-based construction firm was

sentenced in Federal court to 1 year of imprisonment, 2 years of supervised release, and restitution of \$6,755,034 to be paid jointly and severally with the company. The firm was also ordered to pay a fine of \$7,500. In April 2014, the president had pled guilty to wire fraud.

From 2002 to 2011, he repeatedly submitted falsified documents to SBA and other Government agencies regarding the true principal office location of the construction firm in order to retain its HUBZone designation. Consequently, the firm was awarded over \$34 million in HUBZone set-aside Government contracts. This was a joint investigation with the Defense Criminal Investigation Service (DCIS), the U.S. Army Criminal Investigation Command, and DHS OIG.

***Virginia Security Equipment Company
Owner Debarred for 6.5 Years for
8(a) Fraud***

On September 25, 2015, the U.S. Air Force debarred the owner of a Virginia-based perimeter security equipment company from directly or indirectly receiving the benefits of Federal assistance programs for 6 years and 6 months. According to the investigation upon which the Air Force based its decision, the owner of a Maryland-based SBA 8(a) information technology firm substantially passed through numerous 8(a) set-aside Federal contracts to the owner of the Virginia company. In exchange for this arrangement, the Virginia company's owner paid the Maryland firm's owner a 4.5 percent fee on all contracts awarded to the Maryland firm. This was a joint investigation with Air Force Office of Special Investigations, Department of

Interior OIG, DCIS, and Social Security Administration OIG.

***Owner and President of Colorado Firm
Sentenced to Pay \$1.2 Million in Restitu-
tion; \$250,000 Fine; 6 Months of Incar-
ceration; and 2 Years of Supervised Re-
lease***

In September 29, 2015, the owner and president of a Colorado firm was sentenced in Federal court to 6 months of incarceration, ordered to pay \$1.2 million in restitution to the IRS and a \$250,000 fine, and 2 years of supervised release, in which he was ordered to complete 1,000 hours of community service by providing his computer skills to non-profit organizations. He paid the full restitution on the same day as the sentencing. The owner had previously pled guilty to conspiracy.

The investigation discovered that he had directed his accountant and the firm's controller in concealing millions of dollars in assets, including a condominium in Vail, CO. He diverted millions of dollars in unreported income, mostly through overseas accounts. This income was omitted from SBA annual updates and financial statements. In doing so, the business owner was able to maintain his firm's certification as an 8(a) disadvantaged business. Also, in maintaining his eligibility for the 8(a) Program, he concealed his assets and income from the IRS by filing false tax returns. The misrepresentations led to the wrongful award of over \$17 million in 8(a) set-aside contracts to his firm from 2006 to 2010. This is a joint investigation with DCIS, IRS CI, GSA OIG, and U.S. Army

Criminal Investigation Command.

**Office of Inspector General
Peggy E. Gustafson
Inspector General**

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