



PROJECT NO. 14801

DATE: July 11, 2014

TO: Jerome Edwards
Director of Policy and Evaluation

FROM: Robert A. Westbrook /s/
Deputy Inspector General

SUBJECT: Potential Fraud and Improper Payments Found in Hurricane Sandy Loans

This memorandum is to bring to your attention potential fraud and improper payments that we identified during the survey phase of OIG Project 14801 – *Targeted Review of Hurricane Sandy Loans*. During our review, we performed detailed testing of sixteen charged-off loans focusing on loan approval, disbursement, servicing, and liquidation, which revealed potential fraud by one borrower, and loan processing deficiencies that led to \$88,400 in improper payments. We are notifying you of this potential fraud and the improper payments so that your office can take appropriate action to identify these types of improper payments in future reviews and to implement appropriate controls to detect fraud and prevent improper payments from recurring. We have summarized the issues we found below:

Borrower Submitted Altered Repair Invoice to Obtain \$20,000 Disbursement

In order to obtain a \$20,000 disbursement, a borrower submitted an invoice for automobile repairs that was an obviously altered version of an invoice submitted for a different damaged vehicle. The borrower claimed that he had two vehicles damaged in Hurricane Sandy; a 2005 GMC Envoy and a 2005 Hyundai Santa Fe GLS. The loss verification agent did not examine these two vehicles because they had already been removed from the damaged property at the time of his physical inspection. Instead, the SBA allows repair shop estimates or invoices that detail the damage to the vehicles and the cost to repair them as verification of motor vehicle damages. To support his claim of loss, the borrower submitted two invoices for vehicle repairs, one of which was a partial duplicate of the other.

The first invoice, for the GMC Envoy consisted of two pages. Page one included the invoice number, date, and vehicle description, including the Vehicle Identification Number, engine size, odometer reading, and a listing and description of the parts and labor required. The first page also contained a written disclaimer stating that the vehicle had been flooded with salt water and repair costs exceeded the value of the vehicle, thus, repairs could not be guaranteed. Page two of the invoice contained the \$14,542 total for parts, labor, and taxes. It also included the signature of the borrower, authorizing the work to be performed.

The second invoice submitted for the 2005 Hyundai Santa Fe was incomplete and partially duplicated the prior invoice for the 2005 GMC Envoy. The first page of this invoice was simply a copy of the first page of the invoice for the 2005 GMC Envoy. The second page, labeled with a different invoice number, contained the total repair costs for the Hyundai Santa Fe totaling \$11,121, and the borrower's authorization to perform the work. Whether intentional or not, the first page of the invoice for the 2005 Hyundai Santa Fe, which identifies the vehicle, mileage, and details the work to be performed, was not included in the documents submitted.

In preparation for a \$20,000 disbursement in loan funds approved for motor vehicle damage, the SBA requested that the borrower submit proof of loss for the damaged 2005 Hyundai Santa Fe. In response, the borrower submitted a falsified invoice that was almost identical to the invoice for the GMC Envoy except that the vehicle description was replaced with "2005 Hyundai Santa Fe GLS" and the GMC Envoy VIN number was removed. All other information, including the invoice number, odometer reading, description of work to be performed, parts numbers, and costs for parts and labor were verbatim from the GMC Envoy invoice. This suspect invoice also included the same engine specification as the original GMC Envoy invoice; a 4.2 liter in-line six cylinder engine (standard equipment for the 2005 Envoy) whereas the largest engine available for a Hyundai Santa Fe is a 3.5 liter V-6. Further, the invoice amount, \$14,542, equaled the amount of the original GMC Envoy invoice, and exceeded the \$8,700 blue book value assigned to it in the Loss Verification report (based on total loss of the vehicle).

The SBA received this altered invoice, accepted it as proof of loss for the vehicle, approved it and disbursed \$20,000 to replace the two motor vehicles. This loan defaulted and was charged off without the borrower ever making a payment. The SBA should have detected the altered invoice because it already knew that the first set of documents was incomplete, and second document submitted was nearly identical to the first. We have referred this matter to our Investigations Division and they are working with the Assistant U.S. Attorney to prepare this matter for criminal prosecution.

The SBA did not Obtain IRS Tax Return Transcript

A disaster loan borrower claimed gross annual income of \$90,000 and authorized the SBA to obtain tax return transcripts to verify the income. The IRS verification indicated that the prior year's taxes had not been filed and the tax return was overdue (the six month automatic extension period had lapsed). The SBA withdrew the application and notified the borrower of the SBA requirement that taxes be current in order to receive disaster assistance. The borrower then resubmitted his application, along with an incomplete copy of the prior year's tax return, stamped "received: by the IRS New York Field Office. The SBA then accepted the application and approved and disbursed a \$28,700 disaster loan. The SBA did not obtain the tax return transcript from the IRS even though the borrower resubmitted a signed form 8821, *Tax Information Authorization*. The SBA policy, as described in SOP 50 30 7 *Disaster Assistance*, requires tax returns to be verified, in order to verify income and ensure that federal taxes are current. The paper tax return copy submitted by the borrower only included the first page of the tax return and was not a complete tax transcript. It did not include the taxes paid or tax balance due, if any. Further, SBA policies do not permit loans if taxes are delinquent and SBA did not obtain the information necessary to make this determination.

The SBA Made a \$26,000 Disbursement to a Delinquent Borrower

A borrower, approved for a \$40,000 loan to replace personal property, received an initial disbursement of \$14,000 with monthly payments to begin on June 22, 2013, after a five month deferment period. The SBA made a subsequent \$26,000 disbursement to the borrower on July 10, 2013, even though the borrower was 19 days delinquent on the payment due in June. Disaster Assistance SOP 50 30 7, stipulates that no disbursements may be authorized unless all loan payments are current. The borrower never made any payments on this loan and it was charged off in September 2013.

The SBA Did Not Verify Loss for a \$33,700 Personal Property Disaster Loan

The SBA did not physically verify loss before approving and disbursing a \$33,700 personal property disaster loan. The loss verification report stated that the borrower was a renter and that the landlord would not allow anyone to come on to the property to verify the loss. The loss verifier based his personal property estimate on the borrower's statements since direct observation was not possible. The Borrower claimed that losses included high end audiovisual equipment, expensive clothing, and furnishings. The SBA's SOP 50 30 7 establishes that disaster loan eligibility is established by verification of losses. The *Loss Verification Training Manual* published by the Office of Disaster Assistance states that the only time that a "Desktop" verification of personal property losses is allowable is when the Associate Administrator or Deputy Associate Administrator for Disaster Assistance has waived the requirement because an entire geographic area is inaccessible. In those situations, the waiver must be included in the loan file and the loss verifier must cite the use of the waiver in the file. We found no evidence of a waiver for personal property verification in the loan file nor did we find any mention of a waiver in the loss verifier report or loan file.

Conclusion

Our review of sixteen charged off loans disclosed \$88,400 in improper payments that resulted from deficiencies in loss verification, application processing, and disbursement processing. We are alerting you of these deficiencies so that your office can plan its Quality Assurance Reviews to detect these types of deficiencies and assist ODA in designing internal controls to prevent and detect these issues in the future.

If you have any questions concerning this memorandum, please call Robert A. Westbrooks, Deputy Inspector General at (202) 205-7100 or Andrea Rambow, Acting Director, Credit Programs group at (202) 205-4428.