




OFFICE OF INSPECTOR GENERAL
Federal Housing Finance Agency

400 7th Street, S.W., Washington DC 20024

TO: Edward J. DeMarco, Director (Acting)

FROM: Steve A. Linick, Inspector General 

SUBJECT: Systemic Implication Report: Federal Home Loan Bank Collateral
Verification Reviews
SIR No.: SIR-2013-4
OIG Case No.: I -11-0011

DATE: June 17, 2013

Attached is a Systemic Implication Report (SIR) prepared by the FHFA-OIG Office of Investigations identifying a possible risk in the Federal Home Loan Bank Collateral Verification Review process. As discussed in the report, our investigation disclosed fraudulent and overvalued collateral pledged to the Federal Home Loan Bank of Atlanta.

Since these reviews are critical to ensuring the appropriate collateral is pledged to obtain advances from the Federal Home Loan Banks, we recommend that FHFA further assess whether the Federal Home Loan Banks are adequately reviewing the assets pledged as collateral and independently test those reviews.

We also recommended that if indicators of alleged fraud are detected during the course of any review, that both the credit and collateral departments within the appropriate FHLBank are notified and that a Financial Instrument Fraud Report is promptly filed. In addition, we are available to provide fraud training to FHFA examiners responsible for examining FHLBanks.

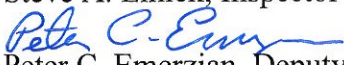
I would appreciate if the Agency could respond to the OIG's recommendation by June 28, 2013. Please let me know if you have any questions or concerns.

cc: Bruce Crandlemire, Advisor to the Director



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TO: Steve A. Linick, Inspector General
FROM: 
Peter C. Emerzian, Deputy Inspector General, Office of Investigations
SUBJECT: Federal Home Loan Bank Collateral and Credit Reviews
DATE: June 13, 2013
SIR No.: SIR-2013-4
OIG Case No.: I-11-0011

The Office of Investigations conducted an investigation involving fraud against Appalachian Community Bank (Appalachian) of Ellijay, Georgia, a former member bank of the Federal Home Loan Bank of Atlanta (FHLBA) that had \$67 million of advances outstanding at the time the bank was closed, including fraudulent and overvalued collateral pledged to the FHLBA. The investigation disclosed a problem that may be systemic throughout the Federal Home Loan Bank System, which may result in member banks pledging inadequate collateral.

Background

On March 19, 2010, the Georgia Department of Banking and Finance closed Appalachian and named the Federal Deposit Insurance Corporation (FDIC) as the receiver. Appalachian was a wholly owned subsidiary of Appalachian Bancshares, Inc. At the time of closing, the FHLBA had credit exposure of \$67 million on advances to Appalachian. An examination of a publicly available Material Loss Review prepared by the FDIC, Office of Inspector General, in October 2010, disclosed an estimated loss of \$420 million to the Deposit Insurance Fund.

The Office of Investigations performed an Internet search for information relating to Appalachian. The Atlanta Business Chronicle reported on November 18, 2009, that Appalachian Bancshares, Inc. suspended Chief Executive Officer Tracy Newton, Chief Credit Officer Adam Teague, and the head of foreclosed real estate, Rusty Beamon, for possible violations of policies involving foreclosed real estate. A public letter was also uncovered that was authored by the operator of a North Georgia real estate marketing website, dated December 29, 2009. The letter's author stated that he was hired by bank officials to market five Appalachian owned properties but soon discovered that only two of them were owned by the bank. Of the three remaining, two were owned by GPH Investments, LLC (GPH) and one was owned by Newmon Properties, LLC. His research revealed that GPH purchased the properties from Appalachian on August 18, 2009, with a Security Deed in the amount of \$3.4 million maturing on August 18, 2010, one year later. He also discovered that the address of GPH was the local Ace Hardware store and that the address for Newmon Properties, LLC was the personal residence of

Appalachian CEO Tracy Newton (Newton died in April 2012). He further alleged that properties were being sold or refinanced to shell companies tied to bank employees.

Analysis

Based upon this information, the Office of Investigations requested a listing of the collateral delivered to the FHLBA by Appalachian and uncovered that there were three loans to GPH with unpaid loan balances totaling approximately \$3.2 million. A scan of the collateral listing also revealed an anomaly relating to two separate loans to MT Construction and Development (MT Construction) and Totherow's Rentals. These two loans stood out as they were listed consecutively and had the same unpaid loan balances of exactly \$450,000. While there are valid reasons for a loan balance to remain unchanged, it can be an indicator of a non-performing loan. A review of the Articles of Incorporation for MT Construction, available to the public through the Georgia Secretary of State website, revealed that Adam Teague, the former Chief Credit Officer and Senior Vice President of Appalachian, was a member and manager of MT Construction. Online public records available through the Bay County, Florida, Clerk of Court were also reviewed and revealed that MT Construction and Totherow's Rentals purchased two separate condominiums in Panama City Beach, Florida, in April 2009. Both entities obtained separate mortgages through Appalachian of approximately \$283,000 each and modified them almost two months later for \$450,000.

On August 22, 2012, in U.S. District Court for the Northern District of Georgia, Adam Teague pleaded guilty to criminal information charging him with conspiracy to commit bank fraud, Title 18, U.S.C., Section 1349. The criminal information notes that Teague and a co-conspirator created fraudulent transactions designed to hide bad debts from the FDIC.

Teague also pleaded guilty to a scheme involving the creation of fraudulent transactions to purchase condominiums in Panama City Beach. The criminal information states:

“In or about April 2009, defendant Teague and unindicted coconspirator T.N. used shell corporations to purchase two condominiums in Panama City Beach, Florida, which they caused Appalachian to finance at a total cost of approximately \$566,000. Approximately two months later, Teague and unindicted coconspirator T.N. refinanced their mortgages and pocketed more than \$875,000, which they then used to pay other personal debts, make monthly loan payments on the refinanced mortgages, pay condominium fees, and purchase new furniture for their condominiums. The new loan issued to Teague was pledged to the FHLBank Atlanta.”

On April 5, 2013, Teague was sentenced to 70 months incarceration, 5 years of supervised release, make restitution in the amount of \$5,840,518, and forfeit \$6,994,996.

Recommendation

In light of the foregoing conduct, we recommend that FHFA further assess whether the Federal Home Loan Banks are adequately reviewing the assets pledged as collateral and independently test those reviews.

It is also recommended that if indicators of alleged fraud are detected during the course of any review that both the credit and collateral departments within the appropriate FHLBank are notified and that a Financial Instrument Fraud Report is promptly filed. In addition, we are available to provide fraud training to FHFA examiners responsible for examining FHLBanks.