Asset Misappropriation at the Local Credit Union

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ABSTRACT

This case discusses the overlapping fraudulent activities orchestrated by two high-level, long-term management personnel of Southern Pine Credit Union (SPCU), namely the controller and the president. It discusses the schemes executed over a 17- and 13-year period, involving the creation of unauthorized share secured loans using the identities of SPCU members without their knowledge. They manipulated these loans by repeatedly paying off and rebooking them, diverting the proceeds for personal use. To conceal their actions, they fabricated credit transactions using the credentials of other SPCU employees, thereby preventing the loans from appearing on quarterly reports to the National Credit Union Administration (NCUA). The case highlights significant lapses in internal controls and oversight within SPCU, underscoring the need for stringent monitoring mechanisms to prevent such fraudulent activities in financial institutions.

Keywords: Fraud, asset misappropriation, embezzlement, internal controls, integrity, board oversight

INTRODUCTION

Who Can We Trust?

What happened to the fiduciary responsibilities of those in charge? How could the president and controller of a local credit union betray its members by stealing millions? These were the questions that arose in the community after two long-time employees of the Southern Pine Credit Union (SPCU) were arrested on suspicion of embezzling around $6 million. The shocking news rocked the community, as these individuals weren't just employees—they were also well-known, trusted figures who interacted with locals at church, the supermarket, and the hunting club. Now, members are left questioning their trust in the credit union and wondering whether their money is truly safe. After the initial shock, the community is hoping for justice, and that these individuals will be held accountable for the harm they caused.

So, how did this happen?

To understand the situation, we must take a closer look at SPCU and the fraudulent schemes orchestrated by two of its trusted employees.

Southern Pine Credit Union: Background Information

Southern Pine Credit Union (SPCU) is a non-federal institution that has provided affordable banking alternatives and financial education to its 1,400 members, primarily employees at a local paper mill in Lowndes County, Georgia. As a credit union, SPCU prides itself on returning profits to its members in the form of better rates and enhanced services. The credit union is governed by a five-member board of directors, which includes a chairperson and a vice chairperson. Three of these board members also serve on the audit committee, ensuring financial oversight. Additionally, SPCU is under the regulatory supervision of Georgia's Department of Banking and Finance, as well as the National Credit Union Administration (NCUA), which oversees and insures credit unions.

With a small staff of six to seven employees, including the President and CEO, SPCU manages daily operations. As of its 2022 annual report, the credit union reported assets of approximately $40 million, with 55% of that amount representing loans to members and deposits totaling about $36 million. In terms of financial performance, SPCU experienced declines in net income (19%) and net assets (5%) between 2021 and 2022.

The Fraudulent Schemes

Two long-time SPCU employees—Teresa Paulo, the controller, and Leah Lehman, the president—engaged in overlapping fraudulent activities over several years. Paulo worked at SPCU from October 2011 to June 2020, with an annual income of $87,396, as reported in the 2018 tax filing. Lehman served as president from 1990 to 2020 and earned $123,900, making her the highest-paid employee in the same tax filing.

Both Paulo and Lehman had the authority to initiate loans and were responsible for submitting quarterly reports to the NCUA. They also had access to all employee usernames and passwords for SPCU's systems and software.

Lehman's fraudulent activities began in June 2003, when she created a share-secured loan using the name and social security number of an unsuspecting member. Over the next several years, from February 2012 to May 2020, she repeatedly rebooked and paid off the loan with additional advances, funneling the funds into a joint account. These funds were then used for personal expenses, including purchasing a boat, a hunting club share, and giving gifts to family members. Although the loan was eventually paid off, Lehman continued the scheme with other individuals' identities, taking out loans without their knowledge and using the funds for personal gain.

To conceal her actions, Lehman used falsified credit transactions and manipulated SPCU's computer system. By altering loan due dates, she kept these loans from appearing in the credit union's quarterly NCUA reports. Lehman adjusted the loan accounts, often adding interest or making additional fraudulent loan advances to mask the artificial growth of SPCU's loan portfolio. By the end of May 2020, the drafts to cover the outstanding loan balances had ballooned to around $4.1 million.

Meanwhile, Paulo was running a similar scheme of her own. In October 2011, she also created a share-secured loan in another member's name and, like Lehman, repeatedly rebooked and took out additional advances. She transferred the proceeds into a joint account, using the funds for her own personal expenses and transferring money into her family members' accounts. Paulo used the same deceptive tactics as Lehman, falsifying credit transactions and manipulating the loan due dates to prevent the loans from appearing in SPCU's reports. By the end of May 2020, the drafts needed to settle these loans had grown to about $1.2 million, with only $7,700 in legitimate payments made to reduce the balances.

Summary of the Fraud Schemes

Employee	Fraudulent Activity	Amount Stolen (Approx.)
Leah Lehman (President)	Created share-secured loans in members' names without their knowledge, used funds for personal expenses, manipulated loan dates to prevent detection	$4.1 million
Teresa Paulo (Controller)	Created fraudulent loans in members' names, transferred funds for personal use, falsified transactions to conceal activity	$1.2 million (excluding payments and interest)

This betrayal has left the community in disbelief, and as the investigation continues, members are hoping for justice to be served. The stolen funds represent not only financial damage but also the loss of trust in individuals who were once pillars of the community. In June 2020, the NCUA placed the credit union into conservatorship because of unsafe and unsound practices.

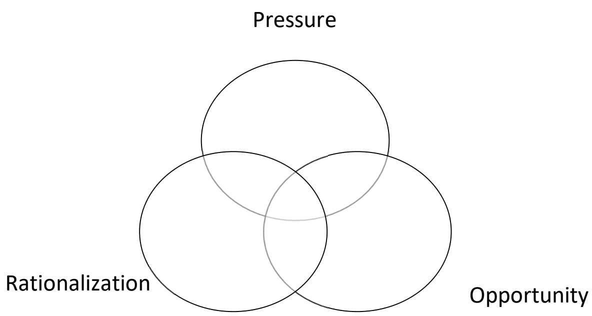
AFTERMATH

Although the exact method of discovery is unclear, the fraud was investigated by both the Federal Bureau of Investigation (FBI) and the Federal Deposit Insurance Corporation's (FDIC) Office of the Inspector General. This investigation led to the arrest of both the controller and president, as well as the termination of their employment with SPCU.

In October 2023, the president pleaded guilty to one count of bank fraud and one count of aggravated identity theft. A month later, the controller also pleaded guilty to the same charges: one count of bank fraud and one count of aggravated identity theft.

ACTION PLAN

Students should be able to provide responses to the following questions.
1. What red flags were identified in the case that suggested potential problems at the credit union prior to the fraud's discovery?
2. Using the fraud triangle below, discuss (a) the opportunities or conditions at SPCU that enable the fraud to occur, (b) the motivation that encouraged the employees to commit the fraud, and (c) the rationalization used by the employees in conducting the fraud.



3. What controls should have been in place to prevent fraud.
4. Do you believe that the controller and president were aware of each other’s scheme? Was the controller motivated to commit fraud based on the president’s activities?
5. Did the board fulfill its fiduciary duties?
6. What is an appropriate penalty for the controller? The president? The credit union?

EPILOGUE

The credit union was released from conservatorship in March 2022 and began operating under new leadership. Later that year, the board engaged Lillie & Company, an independent accounting firm specializing in the audit of credit unions, to conduct an independent audit of its 2021 financial statements.

In September 2024, Paulo, the former controller of SPCU, was sentenced to five years in prison and ordered to repay approximately $1.2 million in restitution after admitting to her involvement in a long-running bank loan and aggravated identity theft scheme. Her sentence included 24 months for aggravated identity theft and 36 months for bank fraud, to be served consecutively, totaling 60 months (about 5 years) in prison.

Additionally, in May 2024, Lehman, the former president of SPCU, was sentenced to 24 months for aggravated identity theft and 48 months for bank fraud, also to be served consecutively, totaling 72 months in prison, followed by two years of supervised release. Lehman was also ordered to pay approximately $4.5 million in restitution to the credit union. Neither defendant is eligible for parole.

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AUTHORS' NOTE

This case was prepared by the authors and is intended for class discussion rather than for determining the effectiveness or ineffectiveness of how the situation was handled. The events described are based on real-world situations reported in various public sources.

AI software was used to review and finalize the document for journal submission.

The teaching notes are not published with the case. Interested faculty should contact the lead author to request a copy.