

UNITED STATES OF AMERICA  
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT  
OFFICE OF ADMINISTRATIVE LAW JUDGE

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In the Matter of .....  
KAREN PRUETT SHELTON ..... HUDALJ 84-990-DB  
Respondent .....  
.....

Edwin E. Wallis, Jr., Esquire  
For the Respondent

Serena M. Williams, Esquire  
For the Department

Before: ALAN W. HEIFETZ  
Administrative Law Judge

INITIAL DETERMINATION

Statement of the Case

This proceeding arose as a result of a proposal by the Department of Housing and Urban Development ("the Department" or "HUD") to debar Karen Pruett Shelton ("Respondent") from participating in all Departmental programs for a period of two (2) years. HUD's action is based on Respondent's conviction following a plea of guilty to violating 18 U.S.C. §§ 1001 and 1002. Respondent was duly notified of the proposed debarment and thereafter filed a timely request for a hearing. Because the proposed action is based on a conviction, the hearing was limited under Department Regulation 24 C.F.R. § 24.5(c)(2) to submission of documentary evidence and written briefs. Upon the record submitted, I make the following findings and conclusions:

Findings of Fact

Respondent began work as a mortgage loan originator for Guaranty Mortgage Company ("Guaranty") on November 1, 1978. Respondent had no prior experience in the real estate industry. In December 1980, Respondent terminated her employment with Guaranty. At the time Respondent terminated her employment, Guaranty was under investigation by HUD. Following her employment with Guaranty, Respondent pursued her profession by enrolling in real estate courses and obtaining a real estate license. In November 1982, Respondent and her husband, Darryl Shelton, opened West Tennessee Mortgage Corporation

("West Tennessee"), later First Security Mortgage Corporation ("First Security").

On November 22, 1983, a Federal Grand Jury returned a thirty-eight (38) count indictment charging Respondent and others with violations of 18 U.S.C. §§ 1001 and 1002. The indictment alleged that from July 1979 to March 1981, Respondent had knowingly and wilfully combined, conspired, confederated and agreed with others to make and cause to be made false statements and representations to HUD in order to facilitate real estate sales. The indictment alleged that such false statements and representations were made by Respondent for the purposes of: inflating sales prices so that HUD would approve and insure larger mortgages than if true sales prices had been submitted; obtaining such insured mortgages with little or no down payment being made by the purchaser, in violation of HUD regulations; and providing nearly one hundred percent financing to real estate purchases, thereby increasing the number of real estate sales from which fees and commissions would be received.

Pursuant to a plea agreement, the indictment against Respondent was dismissed and Respondent pleaded guilty to counts 17 and 28 of the 38 count indictment. Counts 17 and 28 charged Respondent with making false statements and representations to the Department in violation of 18 U.S.C. §§ 1001 and 1002. 1/

On October 29, 1984, Respondent was convicted on counts 17 and 28 in the United States District Court for the Western District of Tennessee, Eastern Division. On counts 17 and 28, Respondent received a suspended sentence and was placed on probation for a two-year period. In addition, Respondent was fined \$3,000.00. All other counts of the indictment were dismissed.

Since October 26, 1984, Respondent has been suspended from participation in HUD programs. 2/

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1/ Counts 17 and 28 of the indictment charged, respectively, that on two separate occasions, the first on or about March 20, 1980, and the second on or about July 31, 1980, Respondent and others falsely stated in a sales contract and offer to purchase the purchase prices of specified properties and misrepresented that earnest money had been received from purchasers.

2/ In a letter dated October 31, 1984, Respondent's husband, as President of First Security, sought clarification from HUD regarding the Department's position on duties still performable by Respondent for his company, First Security, in light of Respondent's suspension from further participation in HUD programs. In this letter, Mr. Shelton stated that due to the indictment, Respondent had disposed of her entire ownership  
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The evidence proffered by the Department in support of its proposal to debar Respondent from further participation in HUD programs consists, primarily, of Respondent's plea of guilty, conviction and subsequent admissions of making false statements contained in both her initial and supplemental responses to the Complaint. The Department's documentary evidence includes copies of Respondent's Indictment as returned by the Federal Grand Jury and the Judgment and Probation Commitment Order filed by the District Court.

Respondent has at all times admitted that she made the false statements and misrepresentations alleged in Counts 17 and 28. However, Respondent states in her initial response to the Complaint that her "activities occurred when [she] was a recently

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interest in First Security and had, in June 1984, resigned from her position as Vice President of First Security. Respondent's husband stated that Respondent had never been on the payroll or drawn any form of compensation since the incorporation of First Security in September 1982. Furthermore, since her resignation in June 1984, Respondent's duties were restricted to bookkeeping and computer operations. According to her husband, Respondent had not been active in the "loan production phase" of the company's operation. Mr. Shelton expressed his belief that replacing Respondent in her bookkeeping and computer program functions would affect the economic viability of First Security's operation and noted that U.S. District Court Judge McRae had stated during his disposition of the case that he had no problem with Respondent remaining in the mortgage banking business. In a letter dated November 1, 1984, Respondent sought clarification from HUD regarding the status of her suspension. No direct Departmental response was proffered to the October 31, 1984 and November 1, 1984 letters. Based on a memorandum dated December 18, 1984, from the Director of the Participation and Compliance Division to the Manager of the Memphis Office, the Department seemingly took the internal position that the then pending debarment proceeding would clarify the issues raised in the October 31, 1981 letter submitted by Respondent's husband. It was also noted that a further response to the letter would be coordinated with the Office of Lender Certification and Monitoring due to the provisions of 24 C.F.R. §§ 25.9(m) and (n). No such response was introduced into the record.

The Department thus far has, in the face of a direct inquiry on behalf of Respondent, failed to address the propriety or impropriety of Respondent's continued performance of bookkeeping and computer operation functions at First Security. Consequently, I find that Respondent may continue to perform in such a capacity so long as her functions comply with the terms of any debarment order resulting from this proceeding and related Departmental rules and regulations.

hired employee in the mortgage lending business and further occurred at a time when [she] had no prior experience in HUD rules and regulations." Respondent states that such activities were "done without criminal intent." Respondent also states that she plead guilty in District Court on the advice of her attorney so as to avoid further attorney fees and related trial costs even though she "maintained her innocence" throughout the proceeding. Respondent cites the disposition of the case by Judge McRae as further mitigating evidence. <sup>3/</sup> Respondent also points out that she terminated her employment with Guaranty in December 1980 and thereafter remained uninvolved in HUD programs until the opening of West Tennessee (later First Security) in November 1982. Respondent states that she resigned her position with First Security in June 1984 as a result of the indictment. Respondent states that "this would make a total of 30 months in which I was not involved in HUD programs since the investigation began in November of 1980."

In support of her attempt to mitigate her criminal conviction, Respondent submitted with her initial response a copy of a letter to the federal probation officer. This letter was submitted by Respondent pursuant to the probation officer's filing of his pre-sentencing report. The letter summarized the loan application process as well as the events leading up to the investigation of Guaranty and her termination of employment with the company. Respondent stated that since leaving Guaranty and opening First Security with her husband, she has taken the steps necessary to more fully comply with HUD rules and regulations. Respondent also asserted that while at Guaranty, she took over 700 loan applications and that of the transactions described in the indictment, she received "average pay" of "approximately \$137.00 per loan." Respondent closed the letter by stating that "I did not realize, or at the very worst, disregarded the fact that the infractions that were occurring were wrong," and that the infractions were "very common during this period of time." Respondent expressed remorse for her conduct as she has throughout her submissions in this proceeding.

Respondent offered additional support for her attempt to mitigate the criminal conviction in her reply brief. Respondent states that since filing her initial response she has learned that the attorney, also indicted and given a suspended sentence, had neither been debarred nor suspended from the practice of law in Tennessee. Respondent also states that the real estate agents also indicted had been suspended by the Tennessee Real Estate Commission for six months. Respondent points to these lengths of

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<sup>3/</sup> Respondent states in her initial response that Judge McRae "imposed no sentence other than a \$3,000.00 fine" and that the fine has been paid. Respondent's depiction of Judge McRae's disposition of the case is inaccurate. Respondent's sentence was suspended and Respondent received not only a \$3,000.00 fine, but also was placed on probation for a period of two years.

punishment as received by her co-defendants, coupled with her "voluntary disassociation" with HUD activities while these matters were pending and all other matters raised in her initial response, as mitigating factors justifying a debarment of less than two years.

### Discussion

Debarment is a sanction which may be invoked by HUD as a measure for protecting the public by insuring that only those qualified as "responsible" be allowed to participate in HUD programs. 24 C.F.R. § 24.0; Stanko Packing Co. v. Bergland, 489 F. Supp. 947, 949 (D.D.C. 1980); Roemer v. Hoffman, 419 F. Supp. 130, 131 (D.D.C. 1976). "Responsibility" is a term of art in government contract law which speaks to the projected business risk of a contractor or grantee, including his integrity, honesty, and ability to perform. See Roemer v. Hoffman, *supra*; 49 Comp. Gen. 139 (1969); 39 Comp. Gen. 468 (1959). The primary test for debarment is present responsibility, although a finding of a present lack of responsibility can be based on past acts. Schlesinger v. Gates, 249 F.2d 111 (D.C. Cir. 1957); Roemer v. Hoffman, *supra*. Integrity is central to a contractor's responsibility in performing a business duty toward the government. 39 Comp. Gen. 468 (1959).

The concept of responsibility is manifestly relevant to a mortgage loan originator who knowingly makes false statements to misrepresent the actual sales price and receipt of earnest money in order to provide nearly one hundred percent financing to purchasers, thereby increasing the number of sales from which fees and commissions would be received.

Respondent does not dispute that she is a "contractor or grantee" within the meaning of 24 C.F.R. § 24.4(f). Nor does she dispute that the conviction precipitating this debarment action is governed by the regulatory authority relied upon by the Department. <sup>4/</sup> Rather, Respondent argues that the existence

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<sup>4/</sup> The Department relies upon the cause stated in 24 C.F.R. § 24.6(a)(4)(5) and (6) as regulatory authority for the proposed debarment. Under that provision, HUD may debar a "contractor or grantee" for any of the following causes:

- (4) Any other cause of such serious compelling nature affecting responsibility, as may be determined by the appropriate Assistant Secretary, to warrant debarment.
  - \* \* \*
  - (5) Violation of any laws, regulation, or procedure relating to the application for financial assistance, insurance, or guarantee or to the
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of "cause" does not compel debarment where mitigating circumstances militate against imposition of the sanction. This is correct. However, I am not persuaded that it is in the best interests of either HUD or the public to conclude that debarment in this case is unwarranted. Respondent's contention that the events leading up to her conviction occurred at a time when she was a "recently hired employee of the mortgage lending business" and when she had "no prior experience in HUD rules and regulations" does not alter the fact that Respondent fraudulently misrepresented property purchase prices and receipt of earnest money deposits in a sales contract and in an offer to purchase. Respondent was under an obligation to deal honestly and forthrightly with the Department. To meet this obligation, Respondent, as a loan originator, was required to perform all her duties meticulously. This she failed to do. Respondent's ignorance of Departmental policies and procedures does not excuse her wilful and knowing acts of falsification and misrepresentation.

Debarment is not a penalty but a way for the government to execute its statutory obligations effectively to protect the public. Gonzales v. Freeman, 344 F.2d 570 (D.C. Cir. 1964). The deterrent effect of debarment cannot be overlooked as a means to assure that end. If governmental regulations are to have any validity, adherence to their requirements must be assured. To ignore or make light of their breach is to condone such conduct and to encourage its repetition. Furthermore, Respondent's

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performance of obligations incurred pursuant to a grant of financial assistance, or conditional or final commitment to insure or guarantee.

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- (6) Making or procuring to be made any false statement for the purpose of influencing in any way the action of the Department.

In its notice of proposed debarment and subsequent submissions, the Department does not specifically rely on 24 C.F.R. § 24.6(a)(1) as regulatory authority, although it purports to base its proposed debarment on Respondent's October 29, 1984 conviction. 24 C.F.R. § 24(a)(1) provides as cause for debarment a "conviction for commission of a criminal offense as an incident to obtaining or attempting to obtain a public or private contract ... or in the performance of such contract ... ." This provision constitutes clear grounds for debarment in this proceeding since the Department explicitly relies not only on the circumstances surrounding Respondent's conviction but on the conviction itself. I assume failure to include such cause is due to Departmental oversight.

conduct may have resulted in direct harm to other mortgage loan applicants seeking participation in the federal program. By falsifying the figures upon which the Department bases its determinations, it is possible that Respondent's actions resulted in a denial of assistance to more needy buyers who would otherwise have received the financing wrongfully made available to Respondent's customers.

Accordingly, I conclude that debarment is appropriate and necessary in this case to insure that the seriousness with which HUD views Respondent's conduct will not be misconstrued by her, or by any others doing business with the Department, and that the public will thereby be protected.

The Department has sought a two-year period of debarment based on Respondent's conviction. Respondent explicitly states that she is not arguing against the debarment. Instead, Respondent has suggested a number of factors which she considers to be mitigating circumstances, thereby justifying a debarment of less than two years. Respondent specifically requests that consideration be given to a debarment period of six months.

As already stated, Respondent's lack of experience as a loan originator and consequent ignorance of Departmental rules and regulations do not excuse her intentional acts of falsification and misrepresentation. That Respondent pled guilty in District Court on the advice of her attorney is irrelevant. Respondent has admitted throughout this proceeding that she committed the alleged acts of falsification and misrepresentation.

Furthermore, contrary to Respondent's assertion, the disposition of her case by Judge McRae militates against, not for, reducing the period of debarment requested by the Department. <sup>5/</sup> Respondent's sentence was suspended, but she also was placed on probation for two years and was ordered to pay a \$3,000.00 fine.

Respondent's assertion that since the November 1980 investigation, she has not been involved with HUD programs for a total of 30 months does not constitute a mitigating circumstance. As stated in the Department's brief, the two-year debarment is based on Respondent's conviction and the events surrounding that conviction. In fact, this 30 month period of nonparticipation in HUD programs, assumedly in recognition of her lack of knowledge of HUD rules and regulations, was self-imposed by Respondent only after she had committed the acts for which she was later investigated, indicted and convicted.

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<sup>5/</sup> See, *supra*, n.3.

Respondent also asserts that since leaving Guaranty and opening First Security with her husband she has taken the steps necessary to more fully comply with HUD rules and regulations. While Respondent's efforts are commendable, they do not mitigate the overwhelming justification for a two-year debarment. Respondent's newly acquired familiarity with Departmental rules and regulations fulfills a preexisting obligation. If Respondent had performed this most basic duty when it first arose, this proceeding would never have been required. Furthermore, unlike Respondent, I do not find the dollar amounts she earned on the transactions described in the indictment (listed by Respondent as approximately \$137.00 per loan) to be inconsequential. Even if one were to conclude that the financial gain to Respondent was minimal, it cannot be ignored that Respondent's gain was wilfully and knowingly obtained at the expense of both the Government and other deserving purchasers and mortgage companies arguably deprived of participation in the federal program. Respondent's statement that she did not realize or, at the very worst, disregarded the fact that the infractions were occurring because they were "common" militates not against but in favor of a two-year debarment.

Finally, Respondent's assertion that the lengths of "punishment" received by her "co-defendants" serve as a mitigating factor in this debarment proceeding is erroneous on two grounds. First, the sanctions imposed or not imposed on Respondent's co-defendants, either within or outside the Department, bear no relation to a determination of Respondent's present responsibility. This debarment proceeding is an inquiry limited solely to Respondent's integrity, honesty and ability to perform. The present responsibility of others who may have acted in complicity is not at issue. Second, even if it were appropriate to inquire into actions taken by the Department against Respondent's co-defendants, <sup>6/</sup> non-Departmental sanctions would be irrelevant. The purpose of debarment is not to punish but to protect the public interest. Thus, because non-Departmental administrative or judicial proceedings and Departmental debarment proceedings serve related but distinct purposes, the sanctions imposed may but need not be identical.

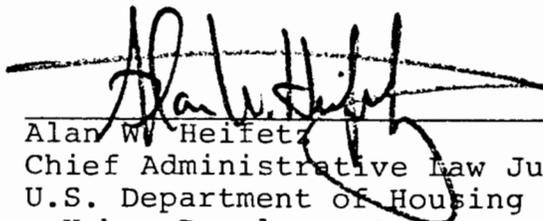
Respondent has been suspended from participating in Departmental programs since October 26, 1984. In view of Respondent's failure to show mitigating circumstances justifying a debarment of less than two years, I find that protection of the public and the government's interest will be served by a two-year period of debarment from the date of Respondent's suspension.

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<sup>6/</sup> The only instance in which an inquiry into the Department's sanctioning of co-conspirators would be appropriate would be where it was alleged that the Department was subjecting similarly situated persons to disparate treatment in its debarment proceedings. There is no evidence whatsoever in this record to suggest such an inquiry.

Conclusion

Upon consideration of the public interest and the entire record in this matter, I conclude and determine that good cause exists to debar Respondent, Karen Pruett Shelton, from doing business with HUD for a period of two years from October 26, 1984 to October 26, 1986.



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Chief Administrative Law Judge  
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Dated: March 15, 1985