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**DEPARTMENT OF
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TO: Mike Spano, Mayor
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All City Council Members

FROM: Kitley S. Covill, Inspector General 

SUBJECT: City of Yonkers Commercial Loan Program

DATE: January 23, 2013

As part of the review of loans given by the City of Yonkers (City) to various business entities in Yonkers, the Department of the Inspector General (IG) reviewed the Commercial Loan portfolio. Currently the City has eleven commercial loans outstanding; four of those loans are current, one entity recently became delinquent on its loan and six loans are in default. At the start of the IG review not all of the entities that were in default were being sued, but as of the date of this report all of the entities in default are now either being sued or in the process of being sued by the City for repayment of what is currently owed.

A chart containing the current status of the Commercial Loan portfolio utilizing information from the Department of Planning and Corporation Counsel is attached to this report as Exhibit A. All of the commercial loans were made by the prior Administrations' Office of Economic Development.

A City of Yonkers Office of Economic Development, Commercial Loan Policies & Procedures manual specifies everything that should be reviewed prior to making a commercial loan. One of the essential components for lending money, as stated in the manual, is: "every loan must have two ways out. The first way out is cash flow. The second way out is collateral. In all cases however, collateral must be adequate to secure the obligation. The Office of Economic Development (OED) will secure a loan with a general security agreement, a

perfected lien on all assets, and the personal guarantees of all principals who own 20% or more of the stock or play a key role in management". Our review considered the manual requirements, specifically in relation to several of the loans that are currently in default.

The IG notes that all of these commercial loans were for small businesses that were starting or maintaining a business in a challenged economic area of the City. As such, the loans were risky and were given to encourage viable small businesses. It is not surprising that a number of the business entities have had financial challenges and are having trouble repaying the City.

Findings:

The IG reviewed several of the commercial loans using the files kept by the Department of Planning (DOP)¹. Our review revealed that there are several parts to a commercial loan: the application and financial review of the borrower and the proposal for use of the loan proceeds, the commitment and loan terms for issuance of the loan, the closing and disbursement of the loan, and the servicing of the loan with the City's bank.

These several parts were completely disconnected in the file, and were handled by different people. The files were somewhat organized, but incomplete. The files were often missing crucial documentation including signed copies of the Promissory Note, conflicting terms for commitment of the loan as opposed to what appeared in the closing documents and even confusing language regarding repayment.

The files also included haphazard communications concerning loan status and litigation. Often it was not clear from the official DOP file who handled the closing and what arrangements were made to set up the payment to the City's bank. In one case, when a City employee inquired as to the status of the loan, the bank employee handling the payments noted that the principle wasn't due for ten years. This information was incorrect as principle payments were to have commenced one or two years after the loan was disbursed.²

Our review revealed that the City usually, although not always, followed the protocols as outlined in the Policies and Procedures Manual for making a commercial loan. Prior to making the loans, the City obtained the documentation required by the Policies and Procedures Manual although the City often relied upon informal personal financial statements and did not obtain confirming documentation of those statements.

¹ The Office of Economic Development was folded into the Department of Planning in early 2012.

² The Promissory Note states the loan is for ten years, interest only is payable for the first two years, and the principle is amortized over nine years.

The City always obtained joint and several personal guarantees³ although without a thorough examination of the personal financial statements for the guarantors, there was little likelihood that every guarantee would be worthwhile for suit and collection purposes. From our review it appears that the City collateral for these loans was not always as outlined at the time of commitment. For example in one loan the commitment required the City's loan to be placed in second position after the primary lender, but apparently the City's loan ended up being placed in fourth position, and this placement was known prior to the loan closing and disbursement. In other loans the collateral was for restaurant fixtures, furniture, a lease assignment or other business assets.

It appears that some of the commercial loans remained in default with often no collection effort for years. Of the one lawsuit that was commenced before 2012, it is unclear from the City's files what collection efforts were made, even when judgments against the guarantors were obtained.

Recommendations

- All commercial loans must be given only after the requirements contained in the City's Office of Economic Development Policies & Procedures manual are completely satisfied.
- Collateral for all loans must be more thoroughly scrutinized before any loan is disbursed.
- Commercial loan repayments should be closely monitored and appropriate collection action begun in a timely manner.
- DOP files should be organized and copies of all documents executed at closing must be provided to the City.
- Any time documents are requested by Corporation Counsel, outside counsel, or other entities, originals must be kept in the official DOP file.
- The DOP employee managing the commercial loan portfolio should receive periodic updates from attorneys representing the City as to the litigation status for each defaulted loan and work closely with the attorneys when a commercial loan recipient falls behind in payment.
- The City needs to track the loans, as the bank that processes the payments may not have accurate information regarding the loan requirements for repayment of principle and interest.
- The City's Corporation Counsel must ensure that the loan documents, particularly the Promissory Note, are in order before the loan is given, even if the City is being represented by outside counsel at the closing of the loan.

³ A joint and several personal guarantee is necessary to cover the entire loan. Thus, if one guarantor is judgment proof, the remaining guarantors are liable for the entire amount owed.

2012 Commercial Loan Status Report

Commercial Loans

Loan #	Borrower	Loan				Current		Status	Legal Action Taken
		Amount	Contract	Maturation	Rate/Term	Balance			
208	Tyrone House	\$50,000.00	07/01/04	07/01/14	4.00%/10 yrs.	\$6,795.26	Current	N/A	
313	C-telli Food Corp.	\$48,000.00	11/01/03	01/01/07	5.00%/3 yrs. 2 mos.	\$11,174.30	Default	Sued 2012	
316	Action Press/Peterson	\$14,248.00	09/01/04	09/01/09	4.25%/5 yrs.	\$2,016.91	Default	Sued 2013	
318	Infinity IV LLC/Letends IV	\$100,000.00	02/08/05	03/01/15	5.00%/10 yrs. 1 mo.	\$65,890.76	Default	Judgment Obtained	
320	The Pizza Place, Inc.	\$90,000.00	04/13/05	04/01/15	7.50%/10 yrs.	\$54,297.95	Default	Sued 2013	
321	Zendom, Inc./D/B/A Chartreuse Bistro	\$97,417.46	09/01/05	08/01/10	6.25%/4 yrs. 11 mos.	\$82,546.29	Default	Legal Papers Prepared	
330	Retro Fitness Funding Yonkers LLC	\$300,000.00	12/10/09	12/31/19	Floating rate of prime + .25% per annum	\$221,293.83	Current	N/A	
331	Body & Soul Essentials, Inc. (D/B/A Wholesome Goodness)	\$150,000.00	05/01/10	04/30/20	Floating rate at prime capped at 6%	\$149,964.33	Default	Legal Papers Prepared	
332	Carolyn Ray, Inc.	\$35,000.00	08/10/10	07/31/16	0%/5 Years	\$25,083.22	Current	N/A	
333	Wedding Center Plus Depot, Inc.	\$35,000.00	07/06/10	06/30/16	0%/5 Years	\$24,066.58	Current	N/A	
334	T. G. F. J. Corp.	\$35,000.00	07/06/10	06/30/16	0%/5 Years	\$25,012.49	Delinquent	Working With Borrower (Recent Delinquency)	
GRAND TOTAL						\$954,665.46		\$668,141.92	