



U.S. Department of Housing and Urban Development  
**Southwest District Office of Inspector General**  
819 Taylor Street, Room 13A09  
Fort Worth, Texas 76102

(817) 978-9309 **FAX** (817) 978-9316  
<http://www.hud.gov/oig/oigindex.html>

September 30, 1999

**99-FW-177-0803**

MEMORANDUM FOR: Saul N. Ramirez, Jr.  
Deputy Secretary, SD

FROM: D. Michael Beard  
District Inspector General for Audit, 6AGA

SUBJECT: Community Builders' Role In Multifamily Property Disposition  
Multifamily Housing Property Disposition Center  
Fort Worth, Texas

During our nationwide review of Community Builders, the Fort Worth Property Disposition staff expressed concerns regarding the involvement of Community Builders in disposing of HUD property. The staff named seven properties. We decided to review those concerns and determine whether Community Builders had inappropriately intervened with the property disposition process. To accomplish the objective, we reviewed documents regarding the disposition of five properties and interviewed applicable HUD staff and local officials. The review covered the respective periods HUD held each property in its inventory. The properties were: Crest A in Dallas, Texas; Pebble Creek in Arlington, Texas; two Jeff- Vander-Lou properties in St. Louis, Missouri; and Kenilworth in Portland, Oregon.

Our review of five properties disclosed that in three cases Community Builders did inappropriately interfere in HUD's disposition of the property. In the three cases, a Community Builder intervened and placed inappropriate pressure on multifamily housing officials. As a result of the Community Builder interference, HUD spent more than \$4.7 million in holding costs or lost sales proceeds. In one instance, HUD sold a property that it had invested \$17 million to a nonprofit for \$10.

Within 60 days please give us, for each recommendation made in this memorandum report, a status report on: (1) corrective action taken; (2) proposed corrective action and date to be completed; or (3) why action is considered unnecessary. Also, please furnish us copies of any correspondence or directives issued because of this review.

## **Background.**

The Fort Worth Property Disposition Center (Center) covers activities for HUD in 29 states. The Center is responsible for enforcing statutory and regulatory requirements governing the foreclosure, disposition, and management of multifamily HUD-owned and Mortgagee-in-Possession properties. During Fiscal Year 1999, the Center sold ten properties. At September 17, 1999, the Center had 22 properties in its inventory. The Center operates under specific criteria designed to protect the interests of the United States, including the Multifamily Housing Property Disposition Reform Act of 1994:

- Subsection 203 (a) which provides for the disposition of multifamily projects in a manner consistent with the National Housing Act, that will protect the financial interest of the Federal Government, and that will, in the least costly fashion among reasonable available alternatives, address certain national goals.
- Subsection 203 (c)(1), provides for the disposition of multifamily housing projects on a negotiated, competitive bid or other basis.

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## **Finding.**

### **Community Builders Interfered in Property Disposition.**

Multifamily housing officials delayed the disposition of one multifamily property in Dallas and two in St. Louis increasing HUD's holding cost and eventually disposed the Dallas property for a nominal price. Community Builders interfered in the normal process pressuring multifamily housing officials into prolonged negotiated sales to nonprofit entities through a city or local housing authority. As a result, HUD incurred \$4.7 million in holding costs or lost sales proceeds. Also, since the two properties in St. Louis are still in HUD's inventory, HUD continues to incur additional holding costs.

#### **Dallas Property.**

In Dallas, the Senior Community Builder<sup>1</sup> interfered with the sale of Crest A. In September 1998, the Senior Community Builder caused the cancellation of a Request for Proposals where an entity not favored by tenants was to purchase the property. The Multifamily HUB Director canceled the Request for Proposals in favor of a negotiated sale through the Dallas Housing Authority to a nonprofit that tenants supported. The sale took an additional 8 months to negotiate. During this time, HUD incurred \$1.9 million in holding cost. The nonprofit purchased the property for \$10; HUD had \$17 million invested in the property. The following paragraphs provide a history of the sale.

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<sup>1</sup> This Senior Community Builder also served as the Secretary's Representative for the Southwest District.

After the Dallas Housing Authority chose not to exercise its right of first refusal, HUD arranged to sell the Crest A property at a foreclosure sale in June 1997. The Crest A Tenant Alliance (Alliance) protested the sale and pressured HUD to take the property into its inventory. On July 12, 1998, HUD issued a Request for Proposal (RFP). Based upon a higher graded proposal, HUD awarded the property to a joint venture between Sheltering A Nation and Operation Relief Community Development Corporation. This selection outraged the Alliance and they asserted HUD had acted in bad faith. The Alliance solicited help from the more powerful Texas Tenants' Union (Union). Together, they inundated HUD officials with letters, filed a hotline complaint with the OIG, and threatened civil litigation. In response to the uproar and because she agreed with the Alliance's assertions, the Senior Community Builder set up a meeting with the Alliance and the Union. The Senior Community Builder believes that HUD should always work with the residents, admitted she had many talks with the Center staff regarding their level of sensitivity to residents and resident issues, and that she and the Center staff have fundamental differences of opinion regarding resident issues. In one instance, the Senior Community Builder attempted to establish property disposition policy and in another instance, she attempted to remove required contract language that protects the federal government's interest. These actions constituted interference with the Public Trust Officer function and, in our opinion, an abuse of her position. The documentation we reviewed disclosed she had an adversarial attitude toward the Center's staff.

### **HUD rescinds the RFP.**

Because of the Alliance's and Union's lawsuit threats, allegations of impropriety in the RFP process<sup>2</sup>, and Community Builder influence, the Multifamily HUB Director rescinded the RFP. Shortly thereafter, HUD arranged to pass Crest A through the Dallas Housing Authority to a nonprofit entity, Dallas City Homes (a lower graded proposal in the original RFP and an entity the Alliance supported). HUD has no justification for either the rescission or the change in disposition method. This improper RFP rescission exposes HUD to possible litigation.<sup>3</sup>

### **Interference in Property Disposition Policy.**

Following a meeting between parties, the Alliance and the Union sent a letter to the Senior Community Builder and the Center Director expressing their understanding of what transpired. In a draft response, the Center staff rebutted the Union's understanding citing a requirement to adhere to federal regulations and property disposition policy. Unbeknownst to Center staff, the Senior Community Builder added language to the Center's draft response citing her understanding of the policy. When Center staff became aware of the additional language, they forwarded the draft to a property disposition official in headquarters who agreed that there were technical problems with the Senior Community Builder's language. Nonetheless, the Senior Community Builder continued to argue with Center staff on policy language saying the Center's changes to her modifications wiped out commitments made in the meeting with the Alliance and the Union. She added she would not concur with the letter as modified. The

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<sup>2</sup> HUD neither investigated nor referred the allegations for investigation.

<sup>3</sup> The OIG reviewed the RFP and proposals noting no impropriety in the RFP rating process.

Senior Community Builder told the Inspector General's office she did not mind policy fights. She stated her changes did not reflect any differentiation from policy; they were only clarifications of what she heard HUD commit to in the meeting with the Union.

### **Interference in Contract Language.**

Due to financial and contract language problems, the parties delayed the sale of the Crest A property. The purchaser requested that HUD subordinate the equity kicker rider in the sales contract. An equity kicker rider is a provision on all contracts involving properties provided grants or sold for a nominal value. The rider prevents purchasers from realizing windfall profits if they resell the property (the Department had \$17 million invested into the Crest A). The Senior Community Builder questioned the need for the rider.

The Senior Community Builder is a well-known Dallas attorney. Prior to joining HUD, she was opposing counsel in two significant cases involving HUD. She is an experienced lawyer and has had prior dealings with HUD and Dallas housing. Thus, HUD regulations and housing law should not be completely unfamiliar to her. However, during interviews, she said she had problems with the RFP and proposal scorings and was trying to understand what is regulatory and what is at the discretion of Center officials. For example, in an electronic message dated April 26, 1999, the Center Director wrote to his supervisors and staff saying the nonprofit entity's attorney requested that HUD subordinate the equity kicker rider on the sales contract. The Director went on to explain that HUD would not subordinate the clause because there was a grant attached and HUD had invested a lot of rehabilitation money into the property. The HUB Director forwarded the message to the Senior Community Builder, who then questioned first what an equity kicker rider was and second why it was needed. The Center Director informed the Senior Community Builder of the significance of the rider.

Inspector General staff asked the Senior Community Builder why she would question contract language protecting the Department's interest. After being told HUD could not remove the rider, she stated she no longer pursued it. Considering her background as an attorney, she should have known this or at the very least, understood its importance to HUD. Further, she apparently would not have backed off if the Center could have removed the rider. Thus, she would have approved the potential for windfall profits; an action not in HUD's interest.

### **Saint Louis Properties.**

The St. Louis Senior Community Builder interfered in the sale of the Jeff- Vander-Lou (JVL) #15 and #18 properties. In St. Louis on September 2, 1998, the Senior Community Builder convened a meeting of key housing players in the area. This was 5 months after the City, under the "Right of First Refusal," had stated it had no interest in purchasing the JVL properties. At that time, the Center's staff were preparing to sell the properties on the open market. Participants at the Senior Community Builder's meeting expressed concern about the availability of affordable large-family rental units. At the meeting, they agreed a smaller group would convene to work out a plan for housing in the area. They concluded one of the keys to success of any plan would be the ability to combine and control all JVL properties as

a single entity. This would include JVL #15 and #18, which HUD had for sale. The meeting participants requested that HUD delay its planned sale for a few months to allow the participants time to plan. The Kansas City Multifamily Housing HUB Director requested postponement of the open market sales, who in good faith, along with the Center staff were trying to work with the Community Builder. At the urging of the Community Builder, the Center Director canceled market sales in favor of working something out with the City.

As a result of the Community Builder's interference, HUD has postponed the sale for a year. HUD has not yet disposed of the properties. They remain in HUD's inventory – the resulting holding cost is \$2.8 million and will continue to grow as long as HUD holds this property. Various parties have attempted to arrange a sale to a nonprofit for a nominal price. The Multifamily HUB Director is not in an enviable position. He had recently attempted again to sell the properties, but received a letter from the Deputy Mayor. The Deputy Mayor said the proposed sale had total support of the appropriate elected officials, which included Congressmen Clay and Gephardt and Senator Ashcroft. The Deputy Mayor strongly recommended the director's approval of sale to the City and subsequently to the nonprofit. At about the same time the newspaper reported the HUB Director as the one "killing the deal" to revitalize and rehabilitate JVL. Negotiations continue.

### **Officials' Actions Delayed Disposition of Properties.**

The Center held the Crest A property in inventory for an additional 8 months awaiting a negotiated sale to a nonprofit entity through the City of Dallas Housing Authority. On September 30, 1998, by letter, the Center notified the three entities that submitted proposals that the RFP on the Crest A property was canceled even though they had notified these entities of the winning proposal on September 25, 1998. The HUB Director in Fort Worth canceled it purportedly because of strong overtones of pre-decision. He canceled it without an investigation and without convening another panel to determine whether the selection was biased. Instead, he decided it was in the best interest of HUD to negotiate a sale to the Dallas Housing Authority for an eventual sale to a nonprofit entity acceptable to the Crest A Tenants Alliance. The acceptable nonprofit had come in second under the RFP.

The Center set closing for March 31, 1999. However, the nonprofit had problems getting the financing for closing. Consequently closing did not occur until May 31, 1999, and only after the Center Director threatened to proceed with an alternative plan.

HUD has had the JVL properties #15 and #18 in inventory for over a year awaiting a negotiated sale to a nonprofit through the City of St. Louis. Center officials have scheduled and canceled open market sales twice since September 3, 1998, in favor of a negotiated sale to the City. On September 22, 1998, the Director of the Kansas City Multifamily Housing HUB postponed the first sale for 60 days. Despite Community Builder optimism and reports of progress, the negotiation continues. On August 20, 1999, the HUB Director again recommended that sale negotiations should continue. As of September 14, 1999, the parties still had obstacles to resolve.

Prolonged negotiations to sell a salable property to a city for \$10 is against HUD’s Negotiated Sales regulations, Title 24 Code of Federal Regulations Section 290.13. It provides for a negotiated sale when a competitive offering will not generate offers of equal merit from qualified purchasers, which is not the case for the JVL #15 and #18 properties. A similar property JVL #19 sold on the open market for \$410,000 on June 5, 1998, with a rider that provides for affordable housing for 30 years.

**Delayed negotiated sales to nonprofit entities have cost HUD millions.**

HUD could have sold the properties as planned and recouped some of its money and avoided significant holding cost. Altogether, HUD could have recouped and saved over \$4.7 million as follows.

*Costs to HUD for Crest A:*

Holding cost from RFP cancellation to date of closing:	\$1,930,186	
Less: Sales Price	\$ 10	
Closing Extension Fees	<u>20,000<sup>4</sup></u>	<u>20,010</u>
Net Cost		\$1,910,176

*Costs to HUD for JVL #15 & #18:*

Holding cost from cancellation of first sale through September 14, 1999	\$2,196,217	
Sales proceeds not realized	<u>636,379</u>	
Net Cost		<u>2,832,596</u>
Total Cost		<u>\$4,742,772</u>

**Headquarters clarifies Community Builder role.**

During the course of our audit, the Assistant Secretary for Housing, the Director of the Departmental Enforcement Center, and the Assistant Deputy Secretary for Field Policy and Management issued a joint memorandum clarifying the Community Builder role in multifamily housing projects (see Attachment 1). The memorandum noted certain Community Builders had misinterpreted or overstepped their role. The memorandum also stated: “In highly sensitive cases (e.g., involving OGC [Office of General Counsel] or OIG [Office of Inspector General]), the CB [Community Builder] may be advised to refrain from any communication, or will be limited to discussion of only very specific aspects of the case.” The memorandum did not address existing Service Agreements between Community Builders and Property Disposition. In those Service Agreements, Community Builders are allowed to comment on property

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<sup>4</sup> An extension fee of \$10,000 resulted from nonprofit entity’s inability to close by the established date of March 31, 1999. The nonprofit incurred an additional \$10,000 for an extension to May 31, 1999.

disposition. Also, Community Builders can exercise influence over career employees through their input on annual performance appraisals.

## **Recommendations:**

We recommend that HUD:

- 1A. Sell the JVL properties on the open market as the regulations provide.
- 1B. Establish a protocol for involvement in the disposition of properties. The protocol should ensure all members of HUD's team work together to accomplish HUD's mission while protecting its financial interest. However, HUD should eliminate the Service Agreements between Community Builders and Property Disposition.
- 1C. Take steps to ensure HUB directors do not act without a plan of disposition that is consistent with the National Housing Act, will protect the financial interest of HUD, and will in the least costly fashion among reasonable alternatives, address the goals of HUD. Further, any deviation from such plan should be documented and approved.
- 1D. Take steps to ensure Community Builders cannot exert undue influence over the business decisions of Public Trust Officers.
- 1E. Take appropriate disciplinary action against those Community Builders who have interfered in the Property Disposition process.

US. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT  
WASHINGTON, D.C. 20410

SEP 10 1999

MEMORANDUM FOR: Secretary's Representatives  
Senior Community Builders  
Departmental Enforcement Center,  
Headquarters Division Directors  
Departmental Enforcement Center,  
Satellite Office Directors  
Multifamily Hub/ Program Center Directors  
Property Disposition Center Directors  
Headquarters Multifamily Office Directors

SUBJECT: Clarifying Community Builder Roles in Troubled FHA Multifamily Housing Projects

In order for HUD to promptly and properly address troubled multifamily projects, it is essential that we act and speak with one voice, as "One HUD". As HUD is currently structured, the Office of Housing remains responsible for the asset management functions for these projects at all times. The Departmental Enforcement Center (DEC), working closely with Housing staff, is currently involved with several hundred of these projects.

It has come to our attention that in their effort to provide responsive customer service, Community Builders (CBs) in certain areas have misinterpreted or overstepped their role in dealing with HUD's identified troubled multifamily projects.

Handling these troubled multifamily projects must be a team effort at all times. To this end, it cannot be stressed too strongly that, prior to responding to any inquiries, issues, etc. regarding any multifamily project, the Community Builder MUST first consult with the Multifamily Hub/Program Center Director to determine whether it is a troubled MF project and how to respond. If Housing advises the CB that the DEC is involved in the troubled project, then Housing and the Community Builder must communicate with the appropriate DEC Satellite Office. These three organizations will jointly determine the response and the role of the Community Builder, if any, in addressing the issue. In highly sensitive cases (e.g. involving OGC or OIG), the CB may be advised to refrain from any communication, or will be limited to discussion of only very specific aspects of the case.

At no time is it proper for the Community Builder to schedule meetings, respond to or initiate contacts directly with an owner, owner's representative, owner's agent, the media, tenants, Members of Congress or their staffs, etc. regarding a troubled multifamily project without the explicit prior agreement of the Director of the Multifamily Hub/Program Center and, where the DEC is involved, the DEC Satellite Office Director. Keep in mind that any separate communications between the Community Builders and any of these parties could compromise proposed or ongoing negotiations between the Departmental Enforcement Center and the owner. At all times, HUD must present itself to the public as speaking with one voice on troubled multifamily projects.





When a multifamily project has been referred to one of the Office of Housing's two Property Disposition (PD) Centers for foreclosure or taking over a project as mortgagee-in-possession or owner, responsibility for the property moves to the PD Center. In such cases, Community Builders remain an essential part of the FRJD team, but will need to work closely and coordinate with the Director of the appropriate PD Center.

The policy outlined above must be adhered to immediately. More detailed guidance is being developed by a working group to be established by the Office of Housing, Departmental Enforcement Center, and the Office of Field Policy and Management.

If you have any questions, please contact Marc Harris, Office of Housing (202) 708-0614, ext. 2680; Jane Hildt, DEC Operations Division (202) 708-9395, ext. 3567 or Barry Riebman, Office of Field Policy and Management (202) 708-1123.

Note that the Departmental Enforcement Center Satellite Offices are located in New York, Atlanta, Chicago, Fort Worth, and Los Angeles; the Property Disposition Centers are located in Atlanta and Fort Worth.

William Apgar, Assistant Secretary  
for Housing/Federal Housing Commissioner

Edward J. Kraus, Director  
Departmental Enforcement Center

Mary E. Madden, Assistant Deputy Secretary  
for Field Policy and Management

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 Ira Peppercorn, Director, Office of MF Asst Restructuring, Y, 4000 Portals Bldg., D.C. 20024  
 Mary Madden, Assistant Deputy Secretary for Field Policy & Mgmt, SDF (Room 7108) (2)  
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Washington, DC 20548 **Attn: Judy England-Joseph**  
Henry A. Waxman, Ranking Member, Comm. on Govt Reform,  
House of Rep., Washington, D.C. 20515  
The Honorable Fred Thompson, Chairman, Comm. on Govt Affairs,  
U.S. Senate, Washington, D.C. 20510  
The Honorable Joseph Lieberman, Ranking Member, Comm. on Govt Affairs,  
U.S. Senate, Washington, D.C. 20510  
Cindy Fogleman, Subcomm. on Gen. Oversight & Invest., Room 212,  
O'Neill House Ofc. Bldg., Washington, D.C. 20515  
The Honorable Dan Burton, Chairman, Committee on Govt Reform,  
House of Representatives, Washington, D.C. 20515  
Deputy Staff Director, Counsel, Subcommittee on Criminal Justice, Drug Policy & Human  
Resources, B373 Rayburn House Ofc. Bldg., Washington, D.C. 20515 (2)  
Steve Redburn, Chief, Housing Branch, Office of Management and Budget  
725 17<sup>th</sup> Street, NW, Room 9226, New Exec. Ofc. Bldg., Washington, D.C. 20503  
Inspector General, G