



U.S. Department of Housing and Urban Development
Office of Inspector General for Audit
Great Plains Region, 7AGA
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MEMORANDUM NO: 2003-KC-1804

December 1, 2003

MEMORANDUM FOR: Herman Ransom, Director, Office of Multifamily Housing, 7AHM

Roger E. Niesen

FROM: Roger E. Niesen, Regional Inspector for Audit, 7AGA

SUBJECT: Meadowbrook Manor of Topeka
Section 232 Nursing Home Review
Topeka, Kansas

INTRODUCTION

We have completed a review of Meadowbrook Manor of Topeka, a Section 232 Nursing Home. We conducted this review as a follow-on of a nationwide review of HUD's monitoring of the Section 232 Program. The overall objective of our review was to determine whether the lessee arrangements at the property were appropriate, and whether project officials used project funds for unallowable purposes. Due to unanticipated circumstances, we terminated this review prior to accomplishing our entire objective. During the work we performed, we did not identify any reportable conditions. During our review, this property was foreclosed upon, and was subsequently sold by HUD without insurance.

METHODOLOGY AND SCOPE

We reviewed and evaluated the ownership entity's records, the records of the lessee, and performed a limited review of the records of the management agent, including the Regulatory Agreements and Lease Agreements for the property. We also reviewed HUD's rules and regulations regarding the Section 232 Program, as well as applicable Codes of Federal Regulations. We interviewed HUD Multifamily staff, and employees of the ownership entity and management agent. We did not examine or evaluate the detailed financial records and supporting documentation that would evidence the results of project operations or the sources and uses of project funds. Our audit period was January 1, 1999 through December 31, 2000.

BACKGROUND

The owners of Meadowbrook Manor of Topeka, a limited partnership, leased the property to HCPIII Kansas, Inc., which was formed by the ownership solely to avoid Kansas licensing issues. This corporation exists in name only, and had no financial activity during our audit period.

Meadowbrook Manor's Regulatory Agreement with HUD limited the use of project funds by the owners, and made the owners ultimately responsible for making the mortgage payments on time. HCPIII Kansas, Inc.'s Regulatory Agreement with HUD required the lessee to make payments to the owner to pay all mortgage payments, Reserve for Replacement payments, and necessary maintenance expenses. The Regulatory Agreement did not include further restrictions on how property funds could be used by the lessee; however, the lease agreement states that it is subject and subordinate to the Regulatory Agreement between the owner and HUD.

HCPIII Kansas, Inc. then subleased the property to a subsidiary of Lenox Healthcare, Inc., as the operator and management agent. On November 3, 1999, Lenox and its subsidiaries filed a voluntary petition for relief under the Bankruptcy Code. Lenox fell behind in their payments to the owners to cover the mortgage; therefore, the owners stopped making the mortgage payments. Lenox began making payments to the owners again in June 2000 and continued through July 2001; however, in July 2001, Lenox again filed for bankruptcy. Due to missed mortgage payments, the loan was assigned to HUD on July 13, 2001.

RESULTS OF REVIEW

We reviewed the ownership entity's records and the lessee's records and found no reportable conditions. After a partial review of the management agent's records, we decided to terminate the audit without further reviewing the agent's records due to the following:

- HUD foreclosed on this property during our review, and subsequently sold it without insurance in the summer of 2002.
- We completed our review of the owner's activities and found no exceptions.
- Based on a previous nationwide internal review of HUD's monitoring of the Section 232 Program, HUD has initiated actions to identify and correct program control weaknesses in the Section 232 program. HUD has drafted changes to the Regulatory Agreement and is currently in the process of getting the new Agreement cleared for use.