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**MEMORANDUM NO.**  
2004-CH-1802

May 12, 2004

**MEMORANDUM FOR:** Preston A. Pace, Jr., Director of Columbus Multifamily Housing  
Hub, 5EHMLA  
Margarita Maisonet, Director of Departmental Enforcement  
Center, CV  
John W. Herold, Associate General Counsel for Program  
Enforcement, CE

  
**FROM:** Heath Wolfe, Regional Inspector General for Audit, 5AGA

**SUBJECT:** HAPI Management Incorporated  
Multifamily Equity Skimming  
Beverly Hills, California

### **INTRODUCTION**

We completed a review of the books and records of HAPI Management Incorporated. We performed the review to determine whether HAPI used Project funds in compliance with the Regulatory Agreements and HUD's requirements. HAPI Management Incorporated inappropriately used \$409,388 from three Projects.

### **BACKGROUND**

HAPI Management Incorporated, an identity-of-interest company, managed Ashland Manor Apartments, King Towers, and South Park Apartments Projects. Apartment Investment and Management Company (AIMCO) owns both HAPI Management Incorporated and the three Projects. Apartment Investment and Management Company, a publicly traded company, is the largest owner/operator of apartment properties in the United States. The Company owns and manages over 1,740 properties located in 47 states.

## **METHODOLOGY AND SCOPE**

Our review covered the period between January 1, 1998 and December 31, 2000. The review period was extended as necessary. We interviewed HUD's staff and Apartment Investment and Management Company's employees. We reviewed the Projects' files including: general ledgers; canceled checks; invoices; Regulatory Agreements; and Audited Financial Statements for Fiscal Years 1998 to 2002. We also reviewed: HUD Handbook 4370.2 REV-1 CHG-1; 24 CFR Part 24; Title 12 of the United States Code Section 1735f-15; and Title 31 of the United States Code Section 3801.

## **RESULTS OF REVIEW**

HAPI Management Incorporated inappropriately used \$409,388 of Ashland Manor, King Towers, and South Park Projects' funds between January 1, 1998 and December 31, 2002. The inappropriate expenses included \$130,367 for disbursements to HAPI Management Incorporated and \$279,021 for unsupported expenses. We provided Apartment Investment and Management Company and HUD's staff a schedule of the inappropriate expenses. The Projects were in a non-surplus cash position and/or not in compliance with all outstanding notices of requirements for proper maintenance when the funds were used. As a result, fewer funds were available for the Projects' normal operations and the Projects were in poor physical condition causing the residents to live in substandard conditions that were hazardous to their health and safety.

Additionally, HAPI Management Incorporated did not disclose to HUD that Ashland Manor and King Towers Projects' funds were used to repay advances to HAPI and an owner distribution. The former Assistant Secretary of the General Partner for Ashland Manor Limited Partnership and the former Vice President/Director of Property Management for HAPI certified in Ashland Manor Project's Fiscal Year 1999 Audited Financial Statement that no unauthorized distributions of Project revenue were made. Additionally, the former Executive Vice President of the General Partner for King Towers Limited Partnership and the former Vice President/Director of Property Management for HAPI certified in King Towers Project's Fiscal Year 1999 Audited Financial Statement that no unauthorized distributions of Project revenue were made. The repayment of advances to HAPI and the owner distribution while the Projects were in a non-surplus cash position and/or not in compliance with all outstanding notices of requirements for proper maintenance is an unauthorized distribution. This lack of disclosure violates the Program Fraud Civil Remedies Act of 1986, which subjects owners and management agents to monetary penalties.

As a result of our review, HUD's Director of the Columbus Field Office of Multifamily Housing Hub agreed to pursue collection of the ineligible and unsupported costs. Additionally, HUD's Director agreed to set up a Reserve Capital Account that restricts the Projects' access to funds

without HUD's permission for any amounts reimbursed for the ineligible or unsupported costs. Further, the Director said he would pursue civil and appropriate administrative actions against the parties involved, if warranted.

### **Federal Requirements**

Ashland Manor Apartments Limited Partnership's Regulatory Agreement, paragraph 2, states disbursements from the Replacement Reserve Fund, whether for the purpose of effecting replacement of structural elements and mechanical equipment of the Project or for any other purpose, may be received only after receiving the consent in writing from the Federal Housing Administration's Commissioner. The Regulatory Agreement also states the Owners must maintain the mortgaged premises, accommodations, grounds, and equipment in good repair and condition.

Paragraph 6 of the Projects' Regulatory Agreements states the Owners may not, without prior written approval of the Federal Housing Administration's Commissioner: (b) assign, transfer, dispose of, or encumber any personal property of the Projects, including rents, or pay out any funds, other than from surplus cash, except for reasonable operating expenses and necessary repairs; (e) make, or receive and retain, any distributions of assets or any income of any kind of the Projects, except from surplus cash and except under certain conditions, including the requirements to comply with all outstanding notices for proper maintenance of the Projects.

Paragraph 13(j) of the Projects' Regulatory Agreements defines distribution as any withdrawal or taking of cash or any assets of the Projects excluding payments for reasonable expenses incident to the operation and maintenance of the Projects.

HUD Handbook 4370.2 REV-1 CHG-1, page 2-6, requires all disbursements must be supported by approved invoices/bills or other supporting documentation.

24 CFR Part 24.110 permits HUD to take administrative sanctions against employees or recipients under HUD assistance agreements that violate HUD's requirements. The sanctions include debarment, suspension, or limited denial of participation that are authorized by 24 CFR Parts 24.300, 24.400, or 24.700, respectively.

HUD may impose administrative sanctions based upon the following conditions:

- Failure to honor contractual obligations or to proceed in accordance with contract specifications or HUD regulations (limited denial of participation);
- Deficiencies in ongoing construction projects (limited denial of participation);

- Violation of any law, regulation, or procedure relating to the application for financial assistance, insurance or guarantee, or to the performance of obligations incurred pursuant to a grant of financial assistance or pursuant to a conditional or final commitment to insure or guarantee (limited denial of participation);
- Violation of the terms of a public agreement or transaction so serious as to affect the integrity of an agency program such as a history of failure to perform or unsatisfactory performance of one or more public agreements or transactions (debarment);
- Any other cause so serious or compelling in nature that it affects the present responsibility of a person (debarment); or
- Material violation of a statutory or regulatory provision or program requirements applicable to a public agreement or transaction including applications for grants, financial assistance, insurance or guarantees, or to the performance of requirements under a grant, assistance award, or conditional or final commitment to insure or guarantee (debarment).

Title 12, United States Code Section 1735f-15, Civil Money Penalties Against Multifamily Mortgagors allows the Secretary to impose a civil money penalty of up to \$25,000 per violation against a mortgagor, with five or more living units and a HUD-insured mortgage. A penalty may be imposed for any knowing and material violation of the Regulatory Agreement by the mortgagor, such as paying out any funds for expenses that were not reasonable and necessary project operating expenses or making distributions to owners while the project is in a non-surplus cash position.

Title 31, United States Code Section 3801, Program Fraud Civil Remedies Act of 1986, provides Federal agencies which are the victims of false, fictitious, and fraudulent claims and statements with an administrative remedy to recompense such agencies for losses resulting from such claims and statements, to permit administrative proceedings to be brought against persons who make, present, or submit such claims and statements, and to deter the making, presenting, and submitting of such claims and statements in the future.

### **Recommendations**

We recommend that HUD's Director of Multifamily Housing Hub, Columbus Field Office, ensure HAPI Management Incorporated and/or Ashland Manor Apartments, King Towers, and South Park Apartments Limited Partnerships:

- A. Reimburses a Reserve Capital Account \$130,367 for Ashland Manor and King Towers Projects for the ineligible payments cited in this finding from non-Project funds.
- B. Provides documentation for the \$279,021 of unsupported payments cited in this memorandum. If documentation cannot be provided, then HAPI Management Incorporated

and/or Ashland Manor Apartments, King Towers, and South Park Apartments Limited Partnerships should reimburse a Reserve Capital Account for the appropriate amount that cannot be supported from non-Project funds.

We also recommend that HUD’s Director of Departmental Enforcement Center and/or HUD’s Associate General Counsel for Program Enforcement:

- C. Pursues administrative sanctions against HAPI Management Incorporated and Ashland Manor, King Towers, and South Park Apartments Limited Partnerships for the inappropriate and unsupported payments cited in this memorandum.
- D. Imposes civil money penalties against HAPI Management Incorporated and Ashland Manor, King Towers, and South Park Apartments Limited Partnerships for the inappropriate and unsupported payments cited in this memorandum that violated the Projects’ Regulatory Agreements.
- E. Pursues action under the Program Fraud Civil Remedies Act against the formers Assistant Secretary of the General Partner for Ashland Manor Limited Partnership, Vice President/Director of Property Management for HAPI Management, and Executive Vice President of the General Partner for King Towers Limited Partnership for falsely certifying in Ashland Manor and King Towers’ 1999 Audited Financial Statements that no unauthorized distributions of Project revenue were made.

**SCHEDULE OF QUESTIONED COSTS**

<u>Recommendation</u> <u>Number</u>	<u>Type of Questioned Costs</u>	
	<u>Ineligible 1/</u>	<u>Unsupported 2/</u>
A	\$130,367	
B		\$279,021
Total	<u>\$130,367</u>	<u>\$279,021</u>

1/ Ineligible costs are costs charged to a HUD-financed or insured program or activity that the auditor believes are not allowable by law, contract, or Federal, State, or local policies or regulations.

2/ Unsupported costs are costs charged to a HUD-financed or insured program or activity and eligibility cannot be determined at the time of the audit. The costs are not supported by adequate documentation or there is a need for a legal or administrative determination on the eligibility of the cost. Unsupported costs require a future decision by HUD program officials. This decision, in addition to obtaining supporting

documentation, might involve a legal interpretation or clarification of Departmental policies and procedures.

In accordance with HUD Handbook 2000.06 REV-3, within 60 days please provide us, for each recommendation without a management decision, a status report on: (1) the corrective action taken; (2) the proposed corrective action and the date to be completed; or (3) why action is considered unnecessary. Additional status reports are required at 90 days and 120 days after report issuance for any recommendation without a management decision. Also, please furnish us copies of any correspondence or directives issued because of the audit.

If you or your staff has any questions, please contact Ronald Farrell, Assistant Regional Inspector General for Audit, at (614) 469-5737 extension 8279 or me at (312) 353-7832.