



U. S. Department of Housing and Urban Development
Office of Inspector General for Audit, Midwest
77 West Jackson Boulevard, Room 2646
Chicago, Illinois 60604-3507

AUDIT RELATED MEMORANDUM
98-CH-211-1802

November 20, 1997

MEMORANDUM FOR: Beverly Bishop, Director, Office of Housing,
Illinois State Office
Edward Hinsberger, Director of Multifamily
Housing, Illinois State Office

FROM: Dale L. Chouteau, District Inspector General for Audit,
Midwest

SUBJECT: Dearborn Place Apartments
Multifamily Equity Skimming
Chicago, Illinois

We completed an audit of the books and records of Dearborn Place Apartments. We conducted the audit because the Project's financial statements indicated that the Project's funds may have been inappropriately used. Dearborn Place Apartments is a multifamily project located in Chicago, Illinois. The mortgage was insured under Section 221(d)(4) of the National Housing Act. The Project defaulted on the mortgage on July 1, 1990 and the mortgage was assigned to HUD on October 6, 1992. The Project has 185 units and is not subsidized.

Dearborn Place Apartments is owned by Dearborn Delaware Associates, an Illinois Limited Partnership, and is managed by an identity-of-interest management firm, Near North Properties, Inc. James R. Loewenberg is the President and 95 percent owner of Near North Properties Inc. James R. Loewenberg owns or controls approximately 30 percent of Dearborn Delaware Associates. The former management firm also shared an identity-of-interest with the owners. The Project's books and records are located at 875 North Dearborn Street, Suite 350, Chicago, Illinois.

The audit objectives were to determine whether the Project owner and management agents used Project funds in accordance with the Regulatory and other agreements and applicable HUD policies and procedures. The audit covered the period of January 1, 1994 through June 30, 1996. We extended the audit period as necessary. We performed the audit between September 1996 and January 1997.

We Concluded that Dearborn Delaware Associates and its management agents:

- Improperly used \$840,333 of Project operating funds to make payments on bank loans. The payments were made while the project was in default, and in a non-surplus cash position. The loans were paid because the former identity-of-interest management agent believed these were eligible project expenses. As a result, the project was deprived of needed revenues for reasonable and necessary operating expenditures.
- As a result of rent concessions and writeoffs of rent due, the former identity-of-interest management agent paid the Project \$189,204 less than the market rate rent between November 1988 and December 1995. The former management agent did not enforce on itself the Landlord's Remedies as outlined in the lease. Consequently, the Project was deprived of needed revenues for reasonable and necessary operating expenditures.
- Improperly used \$220,000 of funds relating to HUD's partial payment of claim. Specifically, funds escrowed for building improvements were used for legal expenses, architectural expenses, loan repayments, and other miscellaneous partnership expenses. The management agent considered all these expenses to be eligible Project expenses. As a result of the inappropriate payments, HUD lacks assurance that Project operating funds and mortgage proceeds were used for their intended purposes.
- Used Project operating funds totaling \$109,316 to pay ineligible and unsupported expenditures. Specifically, \$66,685 was used to pay ineligible or unsupported legal fees; \$26,365 was used to pay for ineligible consulting; and \$16,266 was used to pay other miscellaneous ineligible expenditures. As a result, the Project was deprived of needed revenues and HUD lacked assurance that Project funds were used only for reasonable and necessary operating expenses.
- Did not remit monthly remaining net cash to HUD as payment on its HUD-held second mortgage. A total of \$27,230 was not remitted as required. As a result of the payments not being made, HUD did not receive funds to apply against the HUD-held mortgage.

We provided our draft findings to the Project owner and management agent during the audit. We held an exit conference on February 12, 1997. The Project Owner and management agent provided written comments to our draft findings and recommendations. Subsequently, we referred this case to the Assistant U.S. Attorney for the Northern District of Illinois for pursuit of civil action under the provisions of Section 1715z-4a Title 12, U.S.C. After additional discussions, the Project Owner agreed to remit \$1,386,083 for the audit findings and \$34,500 for the costs of the audit. On November 12, 1997, the owner paid HUD three cashiers checks totalling \$1,420,583. The \$1,420,583 represents a payment in full to HUD for the audit findings.

Should your staff have any questions, please have them contact me at (312) 353-7832.

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