

October 13, 1995

Audit Related Memorandum
No. 96-AT-212-1801

MEMORANDUM FOR: Minerva Bravo, Director
Multifamily Housing Division, 4NHM

FROM: Kathryn Kuhl-Inclan
District Inspector General for Audit-Southeast/Caribbean, 4AGA

SUBJECT: Eduardo Carlos Gomez
ECEGE Development & Investment Co., Inc.
Continental Building Management Co., Inc.
and
Executive Homesearch & Realty Services Corporation
San Juan, Puerto Rico

We have completed a review of ECEGE Development & Investment Company, Inc., Continental Building Management Company, Inc., and Executive Homesearch & Realty Services, Inc., relating to ownership and/or management of five HUD-insured projects in Puerto Rico. Our primary objective was to identify instances of equity skimming.

Our review included: (1) interviews with HUD staff, management agents, project employees, and others, (2) review of HUD Caribbean Office project files, (3) review of project records at the management agent's office, (4) review of a subcontractor's records, and (5) a visit to a project. The review was performed from September 1994 to June 1995.

We confirmed that:

Continental Building Management Company, Inc., the former management agent, improperly disbursed \$1,295,065 of project funds during the period from 1989 to 1993 at the direction or on behalf of its owner, Eduardo Carlos Gomez; and

Executive Homesearch, which replaced Continental Building as management agent in the five projects, charged \$19,628 to Jardines de Country Club and \$2,059 to Lissette Apartments for personnel costs of employees who provided services to other projects. Executive Homesearch also prorated an excessive portion of its controller's salary to the 11 projects it administered.

A total of \$1,316,752 should be reimbursed to the applicable projects through: (1) cash repayment by Executive Homesearch for specific amounts identified as ineligible or improper,

(2) cancellation of project payables to Eduardo Carlos Gomez, and (3) enforcement of the repayment agreement with the current general partner of Lissette, Jardines, and San Juan Park I under the modified transfers of physical assets (TPA). We also recommend that you start administrative procedures to debar Eduardo Carlos Gomez, ECEGE, and Continental Building, as well as any other identified parties who fail to comply with your repayment instructions. We are notifying Field Counsel, by copy of this memorandum, of the need for their assistance to debar Gomez, and to enforce compliance with conditions of the modified TPA's or, if necessary, to pursue other legal remedy including civil enforcement.

We discussed our findings and recommendations with Eduardo Carlos Gomez, Executive Homesearch, and Commercial Advisers and considered their comments. In addition, we have provided a copy of this memorandum to each of them. We have also referred certain matters relating to the management of Lissette Apartments to our Office of Investigation.

Please give us a status report within 60 days for each recommendation herein showing: (1) the corrective action taken, (2) the proposed corrective action and the target date for completion, or (3) why action is considered unnecessary. Also, please furnish us copies of any correspondence or directives issued because of the review.

If you or your staff have any questions, please contact Nancy H. Cooper, Assistant District Inspector General for Audit, at (404) 331-3369, or Aurora Rodriguez, Senior Auditor, at (809) 766-5879.

Attachments

- 1 - Schedule of Ineligible Costs
- 2 - Distribution

BACKGROUND

ECEGE Development & Investment Company was a profit motivated corporation organized in January 1979 under the laws of the Commonwealth of Puerto Rico. Its president and director was Eduardo Carlos Gomez. ECEGE was the General Partner of five HUD-insured projects:

Lisette Apartments, Carolina
Jardines de Country Club, Carolina
San Juan Park I, Santurce
San Juan Park II, Santurce
Pentagon Apartments, Santurce

Continental Building Management Company is a for-profit corporation organized in July 1978 under the laws of the Commonwealth of Puerto Rico. Its president and director is also Eduardo Carlos Gomez. This identity-of-interest firm managed the five projects until March 1993 when HUD replaced it with Executive Homesearch & Realty Services, Inc., because of continued management deficiencies.

Executive Homesearch is a for-profit corporation organized in March 1969 under the laws of the Commonwealth of Puerto Rico. Its president and director is Ana C. Pages. Chairman of its Board of Directors is Hector C. Pages.

In October 1993, ECEGE's charter was canceled and its president, Eduardo Carlos Gomez began acting as General Partner of the projects. In May and June 1994 HUD authorized three modified transfers of physical assets (TPA) in which Gomez was replaced with Commercial Advisers, Inc. as General Partner of Lisette Apartments, Jardines de Country Club, and San Juan Park I. The TPA's were conditional upon the payment by the new general partner of monies owed by ECEGE or Gomez. The new General Partner had its IOI firm take over management of the three projects.

As of our review, Gomez still owned San Juan Park II and Pentagon Apartments and both were still managed by Executive Homesearch.

FINDINGS

1 - Improper Use of Project Funds

Continental Building, the former management agent of the five HUD-insured projects, improperly disposed of \$1,295,065 of projects funds from 1989 to 1993. The management agent made advances and loans to the former General Partner, ECEGE and to its related parties totaling \$1,179,428, diverted \$5,836 to other projects, and charged the projects \$109,801 in ineligible expenses. Although HUD had previously informed the General Partner that advances and loans to owners and related parties were unauthorized distributions, the Management Agent and General Partner continued the practice, disregarding the provisions of the regulatory agreement as well as HUD's specific instructions. Consequently, the five projects were deprived of funds needed for their operation and maintenance.

Criteria

Project operations are governed by regulatory agreements executed by the mortgagor and HUD. Paragraph 8 of the agreements state that, "Owners shall not without the prior written approval of the Secretary:

"(b)...pay out any funds except from surplus cash, except for reasonable operating expenses and necessary repairs.

"(e) Make, or receive and retain, any distribution of assets or any income of any kind of the project except surplus cash...."

Projects in which Gomez/ECEGE is no longer the General Partner

The audited financial statements for 1989 through 1993 show that Continental Building made advances to its identity-of-interest General Partner, ECEGE, and other related parties, diverted project funds to other projects through loans and advances, and charged ineligible expenses to the projects as follows:

Project	Advances to Related Parties	Advances and Loans to Other Projects	Ineligible Expenses	Total
Lisette Apartments	\$540,243	\$2,270		\$542,513
Jardines de Country Club	338,559			338,559
San Juan Park I	31,407	3,566	109,801	144,774

Total	\$910,209	\$5,836	\$109,801	\$1,025,846
-------	-----------	---------	-----------	-------------

Based on these and other deficiencies, and at the request of the other project owners, HUD removed ECEGE as the General Partner of the three projects in May 1994. One of the conditions imposed by HUD for approval of the TPA's was that the new General Partner, Commercial Advisers, agreed to reimburse the projects for amounts owed by Gomez. The amount was tentatively set at \$981,043 which included \$542,513 to Lissette Apartments, \$338,559 to Jardines de Country Club, and \$99,971 to San Juan Park I project. The \$981,043 did not include \$44,803 for the San Juan Park I (\$31,407 in advances plus \$3,566 for diversion plus \$9,830 of the \$109,801 ineligible), because at the time the payment plan was discussed the 1993 financial statements for this project had not been reviewed. HUD informed Commercial Advisers, Inc., that the amount in the San Juan Park I project could vary depending on results of the 1993 audited financial statements. As of our review, Commercial Advisers appeared reluctant to fulfill its part of the agreement.

Projects in which Gomez/ECEGE is still the General Partner

Continental Building Management also made advances and loans to its identity-of-interest General Partner, ECEGE, amounting to \$269,219 from San Juan Park II and Pentagon Apartments as follows:

Project	Advances to General Partner and Other Related Parties
San Juan Park II	\$154,356
Pentagon Apartments	114,863
Total	\$269,219

Most of the advances and loans to ECEGE, its related parties, and other projects were made from 1989 to 1993 and were still reflected in the 1993 audited financial statements of the projects as "Accounts Receivable from Related Parties."

Despite HUD's requests, the unauthorized distributions were not returned to the projects, and the practice continued. In our opinion, Gomez, Continental Building, and ECEGE willfully disregarded the provisions of paragraphs 8(b) and 8(e) of the regulatory agreement.

Recommendations:

We recommend that you:

- 1A Begin procedures to debar Eduardo Carlos Gomez, ECEGE, and Continental Building from doing business with the Federal Government.
- 1B Require Eduardo Carlos Gomez to reinstate \$154,356 to the San Juan Park II project and \$114,863 to the Pentagon Apartments by reversing the project payable to him.
- 1C Require Executive Homeseach to reimburse \$3,566 to the San Juan Park I project from Pentagon Apartments.
- 1D Seek HUD Field Counsel's assistance to enforce the payment plan with Commercial Advisers, Inc., for \$981,043, or to pursue other legal remedy.
- 1E Require Commercial Advisers, Inc., to reimburse \$41,237 to the San Juan Park I project. Add this amount to the payment plan.

2 - Improper Distribution of Salaries

Executive Homesearch, a former Management Agent of Jardines de Country Club and Lissette Apartments, charged \$19,628 and \$2,059, respectively, for salaries and payroll taxes of employees who provided services to other projects. The management agent claimed that the service performed at other projects was temporary and due to emergencies. Therefore, it did not consider a proration necessary. Also, the management agent overcharged 40 percent of the salary of its controller to the 11 projects it administered. These charges were improper because the controller was performing supervisory duties which is a cost of the management agent, not the projects. As a result of these deficiencies, the projects have been deprived of funds needed for operation and maintenance.

Criteria

The operations of the projects are governed by regulatory agreements executed by the mortgagor and HUD. Paragraph 8(b) of the agreements states, "Owners shall not without the prior written approval of the Secretary ...pay out any funds except from surplus cash, except for reasonable operating expenses and necessary repairs."

Charges to Jardines de Country Club

Executive Homesearch charged the salaries and payroll taxes of the project administrator, a handyman, and a gardener to Jardines de Country Club project while they were providing services to the Pentagon Apartments project. The Jardines project manager provided a written statement to Commercial Advisers, Inc., the new general partner, indicating that she and two other project employees performed work at the Pentagon Apartments while their salaries were charged to Jardines. We interviewed the three employees involved who confirmed the statement. The improper charges for salaries and payroll taxes amounted to \$19,628.

Charges to Lissette Apartment Project

Executive Homesearch charged salaries and payroll taxes of five employees to the Lissette Apartments project when, in fact, they were working at three other projects and at the home of Eduardo Carlos Gomez, the former General Partner. This information was provided by the project administrator and confirmed by us through interviews with the employees. The salaries and payroll taxes improperly charged to Lissette Apartments amounted to \$2,059 and were incurred as follows:

Service Provided To:	Salaries and Payroll Taxes
San Juan Park I	\$1,273
San Juan Park II	380
Santa Juanita	239
Eduardo Carlos Gomez, former General Partner	167
Total	\$2,059

Excessive Allocation of Controller's Salary

From its offices in Santurce, Puerto Rico, Executive Homesearch provided centralized accounting services to all projects it managed including the five HUD insured projects we reviewed. From April 1993 to March 1994, the agent's controller provided direct accounting services to all projects. After March 1994, however, she provided mostly supervision of the projects. Based on our interview with the controller, we estimated that 70 percent of her tasks involved supervision and 30 percent involved direct accounting service to the projects. The management agent prorated her salary costs at just the reverse; 70 percent to the projects and 30 percent to the management agent. This resulted in an overcharge of 40 percent of her salary to all projects and undue profit to the agent. Lissette Apartments, Jardines de Country Club, and San Juan Park I projects were managed by Executive Homesearch until August 1994. Executive Homesearch still managed San Juan Park II and the Pentagon Apartments as of our review. These projects were deprived of funds needed for operation and maintenance.

Recommendations:

We recommend that you require:

- 2A Executive Homesearch to repay \$19,628 to Jardines de Country Club and \$619 to Lissette Apartments, and to charge employee expenses to the projects for which the work was performed.
- 2B Commercial Advisers to reimburse \$167 to Lissette Apartments and transfer \$1,273 from San Juan Park I to Lissette Apartments.
- 2C Executive Homesearch to adjust the allocation of its controller's salary from April 1994 to the present and reimburse each project accordingly.

SCHEDULE OF INELIGIBLE COSTS

<u>Recommendation</u>	<u>Ineligible Costs</u> ¹
1B	\$ 269,219
1C	3,566
1D	981,043
1E	41,237
2A	20,247
2B	<u>1,440</u>
Total	<u>\$ 1,316,752</u>

¹Ineligible amounts obviously violate law, contract, HUD or local agency policies or regulations.

Distribution

Secretary's Representative, 4AS
Director, Multifamily Housing Division, 4NHM
Field Comptroller, 4AF
Director, Accounting Division, 4AFF
Field Audit Liaison Officer, 4AFI
Assistant General Counsel, 4AC
State Coordinator, Caribbean Office, 4NS
Assistant to the Deputy Secretary for Field Management, SDF (Room 7106)
Chief Financial Officer, F (Room 10166) (2)
Deputy Chief Financial Officer for Operations, FO (Room 10166) (2)
Director, Office of Internal Control and Audit Resolution, FOI (Room 10176) (2)
Housing - Federal Housing Comptroller, HF
 ATTN: Audit Liaison Officer (Room 4122)
Associate Director, US GAO, 820 1st St. NE Union Plaza,
 Bldg. 2, Suite 150, Washington, DC 20002
Executive Homeseach & Realty Services
Eduardo Carlos Gomez
Commercial Advisers