UNITED STATES OF AMERICA

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

BOARD OF CONTRACT APPEALS

Washington, D.C.

In the Matter of:	HUDBCA No. 83-807-D33
	(Activity No. 83-889-DB)
PHILLIP E. HALCOMB,	
Petitioner	

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DETERMINATION

Statement of the Case

This is an appeal from a Temporary Denial of Participation ("TDP") imposed on Phillip Halcomb, Petitioner, by the San Francisco Regional Office of the U.S. Department of Housing and Urban Development ("HUD") pursuant to 24 C.F.R. §24.18. The TDP was imposed on Petitioner because he had allowed seven HUD-insured loans in his name to proceed to foreclosure while the units were rented and the rents were current. A February 2, 1983, letter from Regional Administrator William Sloan notified Petitioner that the TDP was of a twelve-month duration, and was limited to a denial of participation in HUD's mortgage insurance programs within the geographic jurisdiction of Region IX. The TDP was modified on June 3, 1983, after an informal hearing and reconsideration of the sanction in accordance with 24 C.F.R. §24.18(a)(5), reducing the duration of the initial order from twelve to four months. The TDP terminated on June 3, 1983.

Petitioner requested a hearing pursuant to 24 C.F.R. §24.7 to determine (1) whether the imposition of the TDP was warranted,

and (2) whether the TDP was properly modified. The Government moved to dismiss the request for a hearing as moot. The motion was denied and a hearing was held on August 16, 1983, to determine the rights of the parties.

Findings of Fact

1. Petitioner Phillip Halcomb is a real estate developer in Santa Cruz, California, who has familiarity with and experience in HUD programs (Tr. 89-90).

2. In June, 1980, Petitioner began a Planned Unit Development ("PUD") in Gardnersville, Nevada, known as Sequoia Village. It was Petitioner's intention to construct 160 units on this property, only 76 of which were ultimately built. Construction of the PUD was financed with mortgages insured by HUD-FHA through the 203(b) program under the National Housing Act. (Tr. 90-91.)

3. Between June and August of 1980, Petitioner had "pre-sold" 70 units prior to the time any models were built. As a result of escalating interest rates on mortgages during this period, only eight of these "sales" actually went to closing. In response to the lost sales, Boise Cascade, supplier of the prefabricated units, demanded that Petitioner only purchase the units on a letter of credit basis with rental proceeds from the units used to pay them off. Petitioner accepted the financing terms offered by Boise Cascade because he assumed that "one escrow per month" (one sale of a unit) would effectively carry the project for a three-year period. However, he was unable to even close one sale per month. (Tr. 91-93, 97-98.)

4. Petitioner made the mortgage payments due in June and July of 1980. However, Petitioner failed to make any of the subsequent payments due over a ten-month period. The mortgagee, State Savings and Loan of Stockton, California, refused a request by Petitioner to accept partial payments on the mortgages. Petitioner decided that since rental proceeds were insufficient to satisfy both mortgage payments and maintenance expenses, he would pay only the latter in an effort to ensure the project's viability. (Tr. 99-100.)

5. Despite his failure and alleged inability to make the monthly mortgage payments as they came due, Petitioner purchased another 30 prefabricated units from Interstate Homes in December, 1980, in addition to those that were already purchased from Boise Cascade. The agreement provided for an assignment of purchase proceeds as the units were sold. (Tr. 115-116.)

6. When Petitioner purchased the additional 30 units late in 1980, interest rates were escalating. He testified that he believed he had purchased them under a HUD program which provided long-term financing relief for builders attempting to sell off

existing inventory. He admitted that he obtained the information about the HUD program from Mission Bay Mortgage Company, not from HUD. There is no evidence that the 30 units purchased in 1980 were covered by a HUD long-term financing relief program. (Tr. 101-103.)

7. Petitioner testified that he believed he had purchased seven of the units under a high-risk "builder bailout" program outlined in HUD Notice 80-46 and Mortgagee Letter 80-20. I find that the purchase of the seven units was not made under the builder bailout program because that program had terminated prior to the time Petitioner made his purchases. (Petitioner's Ex. 1; Jt. Ex. 3; Tr. 101-102.)

8. William Peisker, Chief of the Property Disposition Section of HUD's Las Vegas Service Office, learned of Petitioner's missed mortgage payments when looking at a default monitoring system printout in July, 1982, which listed six mortgages as being in default. After calling the mortgagee, State Savings and Loan, Peisker was informed that several properties verged on foreclosure. Peisker called a rental agent at Sequoia Village to determine whether the properties were occupied. He was told that all properties were rented and the rents were current. (Tr. 17-19.)

9. Another mortgage went into default between the time Peisker originally learned of the mortgage non-payment and early 1983. On February 2, 1983, a 12-month TDP in all HUD mortgage insurance programs within the geographic jurisdiction of Region VII was imposed against Petitioner for allowing seven HUD-insured loans in his name to proceed to foreclosure. (Jt. Ex. 1.)

10. Petitioner requested an informal hearing on the TDP, which was conducted on February 22, 1983. On June 3, 1983, the Regional Administrator issued a letter modifying the TDP to terminate on June 3, 1983, four months from February 2, 1983. The modification of the TDP was made for two reasons: HUD had not yet actually sustained a monetary loss, and Petitioner agreed to repurchase fourteen of the units. Petitioner would not have been able to secure financing to repurchase the units if the TDP were not lifted. (Tr. 31, 33-36; Jt. Ex. 2, 3.)

11. Petitioner has failed to repurchase the 14 units in accordance with the agreement which was the basis on which the TDP had been reduced to four months. (Tr. 139-140.)

Discussion

Department regulations provide that a TDP may be invoked upon adequate evidence of irregularities in a contractor's or grantee's past performance in a Department program or upon a showing that an insurance applicant would pose an unsatisfactory

risk to HUD. 24 C.F.R. §24.18(a)(2)(i),(ii). Petitioner is a "contractor or grantee" within the meaning of the regulation applicable to the TDP sanction because he is a participant in a program in which HUD is an insurer. 24 C.F.R. §24.4(f).

The June 3, 1983, modification notice terminated the TDP imposed on Petitioner. The modification did not, however, address the propriety of the originally-imposed TDP. Petitioner requested a hearing to remove the "stigma" brought about by HUD's actions, so that he will not be obligated to report the imposition of the TDP on future applications for Government assistance and contracts. The only issues presented are whether the imposition of the sanction was warranted and whether the sanction was properly modified. Petitioner contends that the entire TDP should have been expunged from his record.

The Government maintains that the TDP was warranted because Petitioner posed an unsatisfactory risk as a 203(b) HUD mortgage insurance applicant. It viewed his failure to make any mortgage payments over ten months on seven properties when rents were current as adequate evidence of an unsatisfactory underwriting risk to HUD. Only after monitoring Petitioner's mortgage payments, and making inquiries into the circumstances surrounding the defaults, did the Department impose the TDP. Following an informal hearing during which Petitioner presented his explanation for allowing the defaults, HUD terminated the TDP primarily because Petitioner agreed to repurchase 14 of the units. It was determined that it was in the best interest of the Government to encourage such a repurchase.

Petitioner advances factors in mitigation of his actions and asserts that the initial application of the TDP was inappropriate. First, Petitioner faults HUD for imposing a TDP before fully investigating the circumstances surrounding his inability to make the mortgage payments. Petitioner argues HUD should have been aware that he might not be able to meet his mortgage payments as a result of worsening economic conditions and burgeoning interest rates. Petitioner places particular emphasis on the risky nature of the HUD builder bailout program, in which he maintains he was a participant.

Petitioner further posits that in not making mortgage payments on the seven properties, he was exercising a business judgment, reasoning that the viability of the project was better safeguarded if maintenance payments were made on the entire project rather than satisfying the mortgage payments in question.

I find Petitioner's assertions that the TDP was unwarranted to be without merit. With respect to the bailout program provisions relied upon by Petitioner, the program terminated prior to the time he took out his mortgages. Petitioner decided not to pay the mortgage notes on seven properties, put those financial and contractual obligations last in line behind a

growing number of creditors, all the while incurring further obligations through purchases of additional units. Petitioner's excuse for that pattern of behavior was that the mortgagee would not accept partial payments. The incurrence of all of the additional debts which were paid made it all but a certainty that Petitioner would not have enough money left each month to make more than a "partial" payment on the mortgage debt. I find that Petitioner's business conduct was inexcusable. It posed a serious underwriting risk to HUD, a risk that apparently left Petitioner unconcerned. I find that the imposition of the TDP was well justified. Certainly the abysmal record of Petitioner's failure to pay its obligations on the mortgage not only justified the initial imposition of the TDP, but militate against an expungement of the sanction.

The remaining issue to be resolved is whether the TDP was properly modified when on June 3, 1983, HUD reduced the term of the TDP from twelve to four months. Following the informal hearing and assurances by Petitioner that he would repurchase 14 units which had gone or were about to go to foreclosure, HUD determined that the interests of the Government would be served by modifying the original TDP. The modification was prompted by HUD's knowledge that the agreement to refinance the units required the removal of the sanction on Petitioner in order for him to obtain financing.

Petitioner maintains that he and HUD officials had informally agreed to a "rescission" of the TDP and not merely a modification of the sanction during the course of their negotiations on a repurchase agreement. Petitioner uses the term rescission to mean expungement. This understanding was not shared by HUD. The modification notice from Assistant Secretary Philip Abrams states that the "modification by HUD in no way condones [Petitioner's] action in allowing the seven loans to go to foreclosure."

I find HUD's decision to impose the TDP and then to modify it, but not expunge it, was proper and in accordance with 24 C.F.R. §24.18(a)(5)(iii). This case is in no way appropriate for expungement of the sanction. The modification of the sanction was taken in the best interests of the Government as an enabling action to promote the repurchase of the units by Petitioner. The only element of the sanction that was improper was its scope. It should have been limited to the Section 203(b) program, rather than to all HUD mortgage insurance programs. Michael J. Papa, HUDBCA No. 83-770-D14, May 25, 1983. However, there is no evidence that the Petitioner has been prejudiced by the absence of such a limitation, nor was the issue raised by Petitioner.

Conclusion

For the foregoing reasons, both the imposition and subsequent modification of the Temporary Denial of Participation

of Phillip E. Halcomb were proper, except as to the scope of the sanction, which should have been limited to participation in the Section 203(b) program. Petitioner's request for an expungement of the sanction is denied.

JEAN S. COOPER
Administrative Judge

Dated: December 29, 1983