

In the Matter of:

SECOND CHAPEL HILL HOUSING DEVELOPMENT CORPORATION
and
REV. ROBERT COVERSON,
Respondents

HUDBCA No. 99-C-105-D4
: Docket No. 99-9019-DB (LDP)

Rev. Robert Coverson
Second Chapel Hill Housing
Development Corporation
19160 Evergreen Road
Detroit, MI 48219

Respondent, Pro se

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Findings of Fact and Recommended Decision

By Administrative Judge Jean S. Cooper
October 15, 1999

Statement of Jurisdiction

On April 1, 1999, the HUD Board of Contract Appeals received and docketed the request of Reverend Robert Coverson for a hearing on the Limited Denial of Participation (LDP) imposed on Coverson and Second Chapel Hill Housing Development Corporation (SCH), Respondents, by the Michigan State Office of the U.S. Department of Housing and Urban Development (HUD). The administrative judges of the HUD Board of Contract Appeals are authorized to serve as hearing officers and to issue findings of fact and a recommended decision for consideration by the HUD official who imposed the LDP. 24 C.F.R. §§24.105-24.314(b)(2), and 24.713(b). The findings of fact and recommended decision set forth below are based on the administrative record (AR) in this case, the written submissions of the parties to this proceeding, and the transcript and exhibits admitted at the hearing held in this matter.

Statement of the Case

On February 6, 1999, John J. Niebiezczanski, Acting Director, Single Family Housing Division, HUD Michigan State Office, imposed an LDP on Respondents as participants in HUD's Partners for Affordable Homeownership Program (PAHP). Two reasons were cited for the LDP. First, SCH sold five properties for amounts higher than allowed under HUD's program requirements for PAHP. Second, SCH violated conflict of interest provisions contained in 24 C.F.R. §291.435(b) by contracting with an investor who served on the Board of SCH and a company owned by the investor to finance, rehabilitate, market, and act as broker for the sale of the homes that SCH purchased through PAHP. The causes cited as the legal basis for imposition of the LDP on Respondents are irregularities in a participant's past performance in a HUD program, 24 C.F.R.

§24.705(a)(2), and failure to honor contractual obligations or to proceed in accordance with contract specifications or HUD regulations, 24 C.F.R. §24.705 (a)(4). The LDP was imposed for a period of twelve months. It prohibits Respondents from participating in all housing programs under the jurisdiction of the Assistant Secretary of Housing, Federal Housing Commissioner, in the geographical area of jurisdiction of HUD's Michigan State Office.

By letter dated March 10, 1999, Coverson requested a hearing on the LDP imposed on Respondents. Respondents contend that the LDP is inappropriate because they received no PAHP orientation training from HUD or the HUD guidelines applicable to PAHP until almost a year after the five properties in question had been sold, and they had repeatedly requested both from HUD. Respondents contend that they believed they were operating in accordance with HUD regulations and program requirements at the time, and had no intent to violate either the program requirements or HUD regulations.

The parties mutually agreed to extend the period within which the hearing would begin, pursuant to 24 C.F.R. §24.314 (b)(i). The hearing was held in Detroit, Michigan on June 8-9, 1999. The record was held open after the hearing for the receipt of documents in the possession of Bruce Schlüssel. The parties agreed that, upon receipt of the documents, the HUD Office of Inspector General for Audit (IG) would have 14 days from receipt to evaluate the documents to see whether the unresolved audit findings were satisfied by the submission. If the documents resolved the outstanding audit findings on which this case is based, the Government would negotiate a settlement with Respondents. If not, the parties would present closing arguments by telephone. The documents submitted after the hearing did not resolve the audit findings. However, the IG revised its calculations based on the documents submitted to find that the alleged excess profit on each sale was substantially less than the IG had originally computed. Closing arguments were presented by telephone on August 12, 1999. This recommended decision is based on the evidence in the record considered as a whole.

Findings of Fact

1. PAHP is a HUD program that allows non-profit organizations and public agencies to buy HUD-owned homes at a 30 percent discount from the HUD appraised value of the homes, and to repair and sell those homes to qualified low-income buyers. HUD restricts the sale price that a non-profit organization can charge the home buyer to the net development cost plus ten percent of the net development cost. The purpose of the program is to expand home ownership opportunities for qualified low-income buyers. (AR Tabs 13, 17, 27.)
2. SCH is a non-profit Michigan corporation. Coverson is the president of SCH. In 1994, SCH applied to HUD to be approved as a participant in PAHP. As part of the application process, SCH had to provide evidence of its tax exempt status, a list of its Board members, including their names and titles; evidence of SCH's administrative and financial capability to develop and carry out the purposes of the PAHP, and evidence of its experience as a lower income housing provider. Organizations lacking this experience, such as SCH, would be restricted to buying ten properties, and would have to complete rehabilitation and resale of five of these properties prior to purchasing additional properties under PAHP. (AR Tabs 13, 21, 28, 29.)

3. Bruce Schlusssel was the treasurer and a member of the Board of SCH at the time when SCH applied to participate in PAHP, and was listed by SCH as such in its application package. Schlusssel is the owner of Gannon Real Estate Company (Gannon). He is also the president of Bralen, Inc., a real estate development company. Schlusssel was known as a real estate developer by at least one of the HUD employees who participated in reviewing and approving SCH's application. Schlusssel was listed on the officer's list submitted by SCH to HUD as "formerly mortgage broker" and "Licensed Builder." (AR Tabs 24, 28; Exhibit R-31; Transcript Tr. 53-54, 111, 426-427.)
4. To establish its administrative and financial ability to perform acceptably in PAHP, SCH also submitted to HUD a copy of a Letter of Understanding dated February 6, 1995, between Bralen, Inc. and SCH. The Letter of Understanding provided that Bralen, Inc. would provide all acquisition funds for SCH to purchase properties through PAHP, to be reimbursed in full at closing plus 12% interest on acquisition funds. It also provided that Bralen, Inc. would provide funds for all repairs necessary, and contract all labor necessary for those repairs. Bralen, Inc. would be reimbursed in full for repair costs "plus 35% for management fee." The marketing of the repaired properties would be done by Gannon. Gannon would be paid \$6,000 at the closing of each property as a sales commission. This amount was subsequently reduced to \$2,000 per property after SCH had already been approved to participate in PAHP and had already sold some of the repaired houses. Coverson had offered to pay such a high sales commission so that Gannon's sales force would have an incentive to market the houses aggressively and sell them quickly. A typical sales commission for sale of real estate in Detroit is 6-7% of the sale price of a property. The Letter of Understanding was signed by Schlusssel, as president of Bralen, Inc. and by Coverson for SCH. (AR Tab 26; R-23; Tr. 116, 323, 428.)
5. On February 9, 1995, SCH was approved by HUD to participate in PAHP. HUD raised no questions about Schlusssel's role as a Board member of SCH, nor did it question the arrangements set out in the Letter of Understanding. (AR Tabs 16,21; R-22.)
6. In March, 1995, SCH's bid was accepted on five PAHP properties, and sales contracts were entered into for the purchase of the five properties located at 8586 Brace, 9560 Plainview, 14559 Vaughan, and 8083 Prest, all in Detroit, Michigan. The sales of the five properties closed on April 17, 1995. Subsequently, SCH purchased five more properties from HUD through the PAHP, including a property located at 13597 Westwood, Detroit. (AR, Tab 28; G-10.)
7. Once a property is sold to a PAHP participant, the requirements applicable to resale of the property bought through the PAHP program are specifically listed in a Model Land Use Restriction Addendum that is incorporated by reference into the sales contract between HUD and the PAHP participant for each property sold. Each Addendum is signed by the representative of the PAHP participant purchasing the property and by a HUD representative. The Addendum provides in pertinent part as follows:
 1. Unless an exception is granted in writing by the Seller:

- a. the initial purchaser shall resell the property only to a person who intends to occupy the property as his or her principal residence and whose income is at or below 115 percent of the median income in the area, when adjusted for family size, or a State, government entity, tribe, or agency thereof, or a private nonprofit organization as defined in 24 C.F.R. 291.405.
- b. the initial purchaser shall not resell the property for an amount in excess of the net development cost plus ten percent of the net development cost. Net development cost is the total cost of the project, including items such as acquisition cost, architectural fees, permits and survey expenses, insurance, and taxes, and excluding overhead and any developer's fee.
- c. the property may not be occupied by or resold to any of the purchaser's officers, directors, elected or appointed officials, employees, or the spouse, child, stepchild, parent, stepparent, or business associate of any of the above.

2. This Addendum survives the expiration, if any, by operation of law or otherwise, of the FHA Sales Contract, and shall terminate five years from the date contained herein.

8. Coverson signed a Model Land Use Restriction Addendum on behalf of SCH at the closing for each property that SCH purchased from HUD through the PAHP. Bruce Schlusell signed the sales contracts as broker, and all but one of the contracts indicated that Gannon Real Estate Company was the broker's business name. Coverson signed each sales contract on behalf of SCH as its President. Coverson did not see the text of the Model Land Use Restriction Addendum until the closing for the first five properties. (AR Tab 28; Tr. 461-462.)
9. Coverson wanted to repair and sell five properties very quickly because HUD would not permit SCH to buy an unlimited number of PAHP properties until it had approved the way that SCH performed on the first five. The arrangement set out in the Letter of Understanding was designed to move the process rapidly to make it worthwhile for Bralen, Inc., and Gannon to take responsibility for the repairing and selling of the properties. The Letter of Understanding was amended on April 7, 1995, to replace the 35% management fee with an equal division of the profits between Bralen and SCH. The commission paid to Gannon was also reduced from \$6,000 to \$2,000 per property through the amended agreement. Alan Bednarsh, an official with Bralen, Inc., took responsibility for the repair and improvements on the properties. Coverson checked the work as it progressed to see if it was acceptable, and was satisfied with the work being done. The subcontractors hired to do the repairs and improvements were paid by Bralen, Inc., or Gannon, and all office subcontractor invoices were kept together by the bookkeeper for Gannon and Bralen, Inc., Fred Bennett, until just before closing, when they were provided to SCH. Coverson was concerned that some of the invoices being given to SCH appeared to lack documentation and were not the invoices received directly from subcontractors, but he was unable to obtain better documentation of the costs of development. (AR Tab 26; R-23; Tr. 331-332, 351-353, 356-357, 405-406, 408, 455-457, 479-480, 485.)
10. The first five properties repaired and sold by SCH were located at 8083 Prest, 8486 Brace, 9560 Plainview, 14559 Vaughan, and 13597 Westwood, all

in Detroit, Michigan. The sale closings for Plainview and Vaughan were on July 20, 1995. Brace closed on July 21, 1995, Prest closed on August 28, 1995, and Westwood closed on October 13, 1995. I have fully credited the check ledgers, expense lists and invoices filed by Respondents to document the net cost of development for each of the properties. I have also fully credited Respondents with the settlement costs and broker's fees that were paid to Gannon for each sale. The only items that I subtracted from the calculation of allowable net development costs were advances to SCH and to Bralen, Inc., because those advances were for profit, which is not an allowable development expense. I find that even if I credit Respondents' documentation in this manner, SCH made a profit in excess of ten percent on every property except Plainview, which had particularly high settlement and broker's fee expenses. SCH made the most excess profit on the sales of the last two properties to close, Westwood and Prest. (Respondents' Post hearing Exhibits; (unnumbered) 8-G; Government's Amended IG Findings based on Respondent's Post-hearing Exhibits.)

11. The sale price of each of the first five properties sold by SCH were based on the appraised value of the repaired property, not the net development cost plus ten percent. Coverson thought this was allowable because the appraised values were calculated by HUD-approved appraisers. Coverson had been told by Cynthia Nardecchia, the HUD employee who administered the PAHP, about the ten percent limitation but he did not fully grasp what it meant. Coverson had repeatedly requested a formal training session on the program's requirements. SCH had been notified by HUD in writing that such training would be provided by HUD, but no formal training was ever provided by HUD to SCH. Nardecchia decided that she would answer the questions posed to her by SCH and meet with Coverson to go over the program requirements informally, but she would not provide formal training. I find that Nardecchia did discuss program requirements with Coverson, including the ten percent profit limitation, but she gave him no written materials to guide SCH until July 27, 1995, after SCH had already sold three of the repaired properties. On July 27, 1995, Coverson was finally given a photocopy of a few pages from Nardecchia's copy of HUD Handbook 4310.5, which gave little or no guidance on any program requirements applicable to the post-purchase period when properties were to be repaired and resold. Furthermore, the ten percent profit limitation was a new program requirement when SCH applied to participate in PAHP, and the vehicle for bringing the limitation to the attention of participants in writing was only through the Model Land Use Restriction Addendum. There were no other documents that contained post-purchase program requirements, other than the Addendum, which was the main reason why Nardecchia could not satisfy Coverson's request for written guidance. She could only give it orally. Nardecchia was unable to tell Coverson what a "developer's fee" was, even though that phrase is contained in the paragraph on the profit limitation in the Model Land Use Restriction Addendum. She was also unaware of any HUD program requirement or regulation that would prevent Schluskel from being on SCH's Board and also getting paid for work on the PAHP properties purchased by SCH. Nardecchia believed that there were no HUD regulations that applied to PAHP, and told Coverson so. (Tr. 57-59, 91, 97-98, 103, 113, 127, 132, 137-140, 142-145, 432-433, 510.)
12. HUD Notice H94-74 was a document that applied to HUD's Single Family Property Disposition Program Sales Procedures. It was reissued as HUD Notice 95-89 (the Notice), without changes. It is primarily an in-house

document for the use of HUD employees with responsibilities for the programs covered by the Notice. PAHP was one of the discount sales programs covered by the Notice, but only limited parts of the Notice apply to PAHP. The Notice includes a list of the types of documentation and information needed by HUD to "pre-qualify" a non-profit organization to participate in a HUD discount sales program. It also contains a Single Family Property Disposition Processing Flow Chart which includes, as part of it, the applicable discounts and time periods for bidding on a HUD property in a discount sales program. There are no program requirements or rules, as such, contained in the Notice. There is no direct reference in the Notice to the ten percent profit limitation in the PAHP. Rather, a Model Land Use Restriction Addendum is included as Attachment 5 to the Notice, without explanation. Henry Plowden, a HUD employee who had no responsibility for the PAHP by the time that SCH was approved to participate in it, believed that he had given a copy of the HUD Notice to Coverson during the period when SCH had not yet been approved to participate. I find Plowden's testimony to have been sufficiently confused as to when events occurred and why, that I cannot credit his testimony on this fact. Plowden may have given Coverson a list of the types of information that SCH would need to provide to HUD to be approved as a PAHP participant, but no program requirements applicable to buying, repairing or selling a PAHP property are included in that list. The only section or document in the entire Notice that applies in any way to the period after a participant has purchased a PAHP property is the Land Use Restriction Addendum, attached to the Notice as Exhibit 5. However, Coverson never saw the Model Land Use Restriction Addendum until April 22, 1995, at the closing for the first five properties that SCH purchased from HUD. (AR Tab 29; G-3' Tr. 56, 58-59, 91, 113.)

13. After SCH sold the first five repaired properties, Coverson requested permission from HUD to allow SCH to purchase more PAHP properties. William Gambill, the Acting Chief of the HUD Property Disposition Division in Detroit, worked with the PAHP as part of his duties. He reviewed most of the PAHP participants for compliance with the requirements in the Land Use Restriction Addendum. In November and December, 1995, Gambill looked at documentation that he was provided by HUD and by SCH to see whether SCH was in compliance with PAHP requirements. Gambill became concerned when he saw what appeared to be evidence of "irregularities" in SCH's program performance. He sent the SCH files to the IG for assistance in his review. (AR Tab 24; G-13; Tr. 64-65, 68, 70, 74, 78.)
14. Starting in September, 1995, the IG began a review of PAHP to evaluate the program's effectiveness in Detroit. PAHP participants would be audited on-site as part of the review. David Brazier, an IG auditor, was assigned to review SCH's participation in PAHP. Brazier spent one day going over records at SCH and interviewing personnel, including Coverson, but he was not able to return to SCH to continue the review on-site. Brazier went over the files that SCH provided to Gambill in December, 1995, so that Brazier could complete his review. Brazier made note of the fact that Coverson told Brazier that he was "unaware" of the ten percent profit limitation. The IG sent a letter to Coverson, dated April 30, 1996, with Brazier's draft audit findings. Brazier questioned all of the "receipts" or invoices from Gannon or Bralen, Inc., and subtracted the amounts reflected on those invoices from the allowable costs of development. Brazier only accepted third-party invoices from subcontractors who actually performed the various repairs as proof of

development costs. Many of the invoices disregarded by Brazier showed costs of repairs that had been performed on the properties, but the invoice was from Gannon or Bralen, Inc., not the subcontractor. In addition, Brazier found the advances to SCH and Bralen to be ineligible net development cost under the terms of the Land Use Restriction Addendum. Brazier also reduced the allowable broker's fees to 6-7% of the sale price that was customary in Detroit, because he viewed the broker's fees, particularly the \$6,000 broker's fees, as excessive, and also because the arrangement between SCH, Bralen, Inc., and Gannon was not an "arm's length transaction." Based on Brazier's application of strict accounting requirements to the audit of SCH's records, the calculation of allowable net development costs was greatly reduced by Brazier from the actual amounts legitimately spent. The result was that Brazier concluded the SCH had sold each of the five properties for prices far in excess of the allowable ten percent profit under the PAHP program requirements and the Model Land Use Restriction Addendum. Brazier also concluded that the relationship between SCH, Bralen, Inc., and Gannon presented a conflict of interest as defined at 24 C.F.R. §291.435 because Schlüssel was an officer and Board member of SCH at the time when his two owned or controlled companies, Bralen, Inc., and Gannon, were being compensated for financing, repairing and marketing the properties that SCH purchased through PAHP. Respondents did not respond to Brazier's draft audit findings. (G-1, G-4, G-6, G-8 through 12; Tr. 205-207, 218-219, 221, 228, 232-233, 234, 245, 247, 261-262.)

15. Brazier's supervisor was Muhaimed Akhtar. Akhtar reviewed Brazier's audit work papers and concurred with the conclusions in the draft audit. Akhtar believed that SCH was on notice of the ten percent profit limit because Coverson signed the Land Use Restriction Addendum for each property. When Respondents did not make any response to the draft audit findings within ten days, Akhtar called Coverson to find out whether there would be a response. Coverson informed Akhtar that SCH would not respond. The final audit report dated May 31, 1996, was issued by the IG. The audit report found that three of the nine PAHP participants audited, including SCH, made excess profits and were not in compliance with the program requirements. The audit report noted that all of the three non-complying participants told the IG auditors that they were not aware of the program requirements, although a representative of each had signed the Model Land Use Restriction Addendum at the closing when each property was purchased from HUD. The audit report concluded that, because of the excess profits made on the sale of repaired PAHP properties, home buyers paid more for their homes than HUD and PAHP intended. The audit report specifically concluded that SCH made unallowable profits of \$80,488. Of that amount, \$9,000 was for unallowable advances of profits made to SCH, and on one property to SCH and Bralen, Inc.; and \$57,054 was for "unsupported costs," which referred to the invoices Brazier would not credit. The audit report further stated that the sale prices for the properties that SCH repaired and sold were based on the appraised values after repairs, rather than on the net development cost plus ten percent. The audit report also concluded that SCH violated 24 C.F.R. §291.435 because Schlüssel had a conflict of interest serving as SCH's treasurer and board member. The audit report recommended that the Director of the Office of Housing of the Michigan State Office should require SCH to provide invoices to support the "unsupported" expenditures of \$57,054 or prepay on the applicable mortgages the amount that cannot be supported, as well as prepay the applicable mortgages for \$23,434 in excess profits and ineligible

expenses claimed, and "excessive broker's fees" of \$8,692. The audit also recommended that SCH immediately eliminate the conflict of interest. If the recommendations were not resolved satisfactorily, the audit report recommended that SCH be removed from participation in PAHP, and that the Director of the Office of Housing initiate administrative penalties. (AR 13; G-1, G-6; Tr. 270-271, 273-274, 277, 280, 283, 290.)

16. SCH complied with only one of the audit report recommendations. Schlüssel resigned as SCH's treasurer and Board member. On February 21, 1997, HUD was still giving SCH the opportunity to comply with the audit report recommendations by prepaying on the applicable mortgages the unallowable and unsupported costs and excess profits. SCH did not comply with the audit report recommendations on prepayment of the mortgages. By letter dated August 4, 1997, SCH was removed from participation in PAHP, effective August 1, 1997. The letter also stated that administrative sanctions would be taken against SCH, its officers and board members, and that affirmative litigation on the monetary findings would also be initiated. The letter was signed by Robert J. Turner, Director, Office of Housing of HUD's Michigan State Office. (AR Tabs 7,8; R-3; Tr. 441-442, 444.)
17. By letter dated February 16, 1999, Respondents were notified of the LDP imposed on them by the HUD Michigan State Office. Respondents requested a hearing on the LDP pursuant to 24 C.F.R. § 24.713. (AR Tabs 2,6.)

Recommended Decision

An LDP is a discretionary administrative sanction that is imposed in the best interest of the Government. 24 C.F.R. § 24.700. Underlying the Government's authority not to do business with a person is the requirement that agencies only do business with "responsible" persons and entities. 24 C.F.R. §24.115. The term "responsible" as used in the context of administrative sanctions such as LDPs, debarments and suspensions, is a term of art which includes not only the ability to perform satisfactorily, but the honesty and integrity of the participant. 48 Comp. Gen. 769 (1969)

The test for whether a sanction is warranted is present responsibility, although lack of present responsibility may be inferred from past acts. Schlesinger v. Gates, 249 F. 2d 111 (D.C. Cir. 1957); Stanko Packing v. Bergland, 489 F.Supp. 947, 949 (D.D.C. 1980). The Government bears the evidentiary burden of demonstrating by adequate evidence that cause for Respondents' LDP exists, that the LDP is in the public interest, and was not imposed for punitive purposes. 24 C.F.R. § 24.705. Adequate evidence is defined in the regulations applicable to an LDP as "information sufficient to support a belief that a particular act or omission had occurred." 24 C.F.R. §24.105(a). It is likened to the probable cause necessary for an arrest, search warrant, or a preliminary hearing. Home Bros. v. Laird, 463 F. 2d 1268, 1271 (D.C. Cir. 1971). It is not a rigorous level of proof.

Both SCH and Coverson are participants in a primary covered transaction through the PAHP. 24 C.F.R. § 24.105. Coverson, as the president of SCH, is also a "principal," as defined at 24 C.F.R. § 24.105. As such, both are subject to administrative sanction by HUD if cause exists for a sanction and it is in the best interest of the public and the Government to sanction them. 24 C.F.R. §24.110(a) and §24.115.

The PAHP has few program requirements applicable to the resale of a property by an initial purchaser after the property purchased from HUD has been rehabilitated. Those program requirements are contained in the Model Land Use Restriction Addendum to each sale contract. Respondents complied with all of the program requirements listed in the Model Land Use Restriction Addendum except one. They violated the requirement that they shall not resell a property for an amount in excess of the net development cost plus ten percent. Net development cost is defined in the Model Land Use Restriction Addendum as the total cost of the project, including items such as acquisition cost, architectural fees, permits and survey expenses, insurance, taxes, but excluding overhead and any developer's fee. "Developer's fee" is not defined, but in the context of the Addendum provision, it logically applies to the profit that the PAHP participant is allowed to make on the sale of each property.

Even if every invoice is credited as adequately documenting a necessary development cost, the profit made on the sale of four of the five properties by SCH exceeded the net development cost plus ten percent of the properties. To the extent that Bralen, Inc., Gannon, or SCH was advanced any part of the profit, or developer's fee, those advanced payments were correctly eliminated by the IG auditors as an unallowable developer's fee or profit.

The IG auditors refused to credit the entire amount of the broker's fee paid to Gannon to the extent that those fees exceeded the normal and customary broker's fee of 6-7% in the Detroit area. There is no PAHP requirement that a broker's fee may not exceed that which is ordinary and customary. Coverson originally offered such a generous fee as an incentive for Gannon's brokers to sell the properties as soon as possible. Coverson believed that it was necessary to sell the first five properties very rapidly so that HUD would allow SCH to purchase more properties in the program. The very high broker's fee was included in the net development costs to SCH, thus raising the price at which a property could be sold. This may have defeated the spirit of the PAHP, but it is not in violation of any of its program requirements.

The Letter of Understanding, both as originally written and later as amended, set out the agreement between SCH and Bralen, Inc., to purchase, repair and market the properties bought by SCH through PAHP. The arrangement between SCH, Bralen, Inc., and Gannon was known to HUD when it approved the participation of SCH in the PAHP. The use of a general contractor may have been unusual in the PAHP program, but it is not a violation of a PAHP program requirement. What caused this to be a problem was that Bruce Schlüssel served on SCH's board.

Respondents were repeatedly told by Nardecchia that there were no regulations applicable to PAHP. This was not accurate information. Part 291 of the Code of Federal Regulation addresses the disposition of HUD-acquired single family property. 24 C.F.R. § 291.110 provides for direct sale of properties to private non-profit organizations and governmental entities at a discounted sale price. The PAHP falls within this category.

24 C.F.R. § 291.435(b), entitled "Conflicts of Interest," sets out a regulatory requirement that applies to all purchasers and lessees under Part 291 of the HUD regulations. It provides as follows:

- (b) Conflicts of interest. No person who is an employee, agent, consultant, officer, or elected or appointed official of the lessee or purchaser of property under this subpart, or who is in a position to participate in

a decisionmaking process or gain inside information with regard to the lease or purchase of the property, may obtain a personal or financial interest or benefit from the lease or purchase of the property, or have an interest in any contract, sub-contract, or agreement with respect thereto, or the proceeds thereunder, either for himself or herself or for those with whom he or she has family or business ties, during his or her tenure or for one year thereafter.

Because Bruce Schlusel, the president of Bralen, Inc. and owner of Gannon, was on the Board of SCH, and obtained a financial benefit and interest in the properties purchased by SCH through the PAHP, he was in violation of 24 C.F.R. §291.435(b). However, once that violation was pointed out to SCH by the IG auditors, Schlusel resigned his position at SCH, and this violation was corrected to the satisfaction of HUD. SCH responded appropriately when it was notified that Schlusel could not serve on SCH's Board. Neither Respondent should be sanctioned for a violation that was corrected upon notice of it, particularly since the HUD personnel administering the program also did not know about the regulation, and Nardecchia questioned its applicability even at the hearing. I find that it does apply to PAHP participants, but under the peculiar circumstances of this case, I find no public purpose in holding Respondents responsible for that which they were told did not exist, and corrected upon notice.

There is adequate evidence that SCH failed to honor the contractual obligation of the ten percent profit limitation in the Model Land Use Restriction Addendum attached to each contract at closing when the properties were sold by HUD to SCH, and which were also contained in the HUD Notice as an attachment. Respondents also failed to correct that violation by not prepaying the excess profit to the mortgages. Therefore, SCH has not cured its violation, even if the excess profit it made was far less monetarily than the IG auditors had originally computed. This is a ground for the LDP. 24 C.F.R. § 705 (a)(4). SCH was also responsible for the irregularities in its past performance in the PAHP. 24 C.F.R. § 705 (a)(2). As the president of SCH, Coverson is as responsible for these irregularities as SCH. The ten percent profit limitation was no secret. It was contained in every Model Land Use Restriction Addendum signed by Coverson. Nardecchia also focused on it in her discussions with Coverson. When SCH decided to use Gannon and Bralen, Inc. to fund its participation, to contract for the repairs, and to market the properties after repairs, SCH relinquished most of its control over how things were done. It is noteworthy that SCH could not ever get all of the receipts for the work that was done. SCH was the PAHP-approved participant, not Bralen, Inc., or Gannon, but the way in which Bralen, Inc., and Gannon handled receipts and calculated the sale price of the properties put SCH in violation of the ten percent profit limitation. SCH should not have ceded its control and authority to the extent that it did. To have done so was not responsible conduct. Because the sale price was determined by appraisal, rather than by adding together the actual net development costs plus ten percent, it would have been pure accident if SCH was in compliance with the ten percent profit limitation because it was not the reference point for the sale price of any of the five properties.

I do not believe the SCH or Coverson set out to deliberately violate any of the PAHP program requirements. However, by not paying close attention to how the sale price had to be set and by ceding so much control to Bralen, Inc. and Gannon, they were bound to be in violation of the profit limitation, and by

their violation, whether intended or not, the homebuyers paid higher prices than necessary, which defeated the purpose of the PAHP. For this reason, I find that the LDP was warranted. Because the contract violation and the resulting irregularity have not been corrected to date, there is no basis on which I can find Respondents to be presently responsible. I therefore recommend that the LDP not be terminated before the twelve month period of the sanction has elapsed.

CONCLUSION

For the foregoing reasons, I find that the Limited Denial of Participation imposed on Respondents was supported by adequate evidence and the causes for its imposition have not been corrected. Therefore, I recommend that the LDP not be terminated at this time.

Jean S. Cooper
Administrative Judge