OFFICE OF AUDIT
REGION 6
FORT WORTH, TX

Yale Court Apartments
Houston, TX

Section 223(f) Multifamily Insurance Program

2014-FW-1005 September 22 , 2014

Issue Date: September 22, 2014

Audit Report Number: 2014-FW-1005

TO: Raynold Richardson
Director, Multifamily Housing Program Center, 6EHM

Craig Clemmensen
Director, Departmental Enforcement Center, CACB

//signed//

FROM: Gerald R. Kirkland
Regional Inspector General for Audit, Fort Worth Region, 6AGA

SUBJECT: The Former Owner of Yale Court Apartments, Houston, TX, Used Project Funds in Violation of the Regulatory Agreement With HUD

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of Yale Court Apartments in Houston, TX.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8M, requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at http://www.hudoig.gov.

If you have any questions or comments about this report, please do not hesitate to call me at (817) 978-9309.

September 22, 2014

The Former Owner of Yale Court Apartments, Houston, TX, Used Project Funds in Violation of the Regulatory Agreement With HUD

Highlights

Audit Report 2014-FW-1005

What We Audited and Why

At the request of the Director of the U.S. Department of Housing and Urban Development's (HUD) Houston, TX, Office of Multifamily Housing Programs, we conducted a review of Yale Court Apartments (project). Our objective was to determine whether the project owner used the project funds in accordance with its regulatory agreement and HUD regulations.

What We Recommend

We recommend that the Director of HUD's Houston, TX, Office of Multifamily Housing Programs flag the form HUD-2530 for all appropriate parties for the regulatory agreement violations in this report. We also recommend that the Director of HUD's Departmental Enforcement Center pursue civil money penalties and administrative sanctions, as appropriate, against the owner, operator, and/or their principals/owners for their part in the regulatory violations cited in this report.

What We Found

The former owner used more than $3.5 million of the project funds for ineligible and unsupported expenses. Specifically, it (1) used $3.2 million for unauthorized distributions, transfers to non-HUD-insured properties, or repayments to the former owner for advances; (2) used several incorrect documents to support more than $88,000 in withdrawals from the repair escrow account; (3) paid more than $16,000 for other ineligible project expenses; (4) overpaid management fees by nearly $16,000; (5) underfunded the tenant security deposit account by more than $9,000; (6) made ineligible loans to employees; and (7) spent more than $160,000 in project funds for items that it could not properly support. Further, the former owner did not maintain accurate financial information and did not submit annual audited financial statements as required. These conditions occurred because the former owner did not implement adequate controls to ensure compliance with the regulatory agreement and disregarded the project's regulatory agreement. The former owner's improper use of project funds reduced the amount available for physical repairs and payment of the mortgage, which resulted in the project being left in poor physical condition and contributed to HUD's nearly $4 million loss when HUD resold the note in August 2012.

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BACKGROUND AND OBJECTIVE

Yale Court Apartments (project no. 114-11246) is a 250-unit apartment complex located at 5050 Yale Street, Houston, TX, and was owned by Shiraz US Yale, LLC. The company consisted of seven members – six persons and a corporation:

Member	Ownership percentage
1. Owner 1 (person)	20.633%
2. Owner 2 (person)	20.633%
3. Owner 3 (person)	17.942%
4. Owner 4 (person)	16.148%
5. Owner 5 (person)	9.644%
6. Optimum RE Investment, LLC	7.500%
7. Managing member (person)	7.500%

According to the company's membership regulations, the managing member was responsible for the property, affairs, and business of the company. No other member had the authority to act for or on behalf of the company, to do any act that would be binding on the company, or to incur any expenditures on behalf of the company, unless approved by the manager. On February 7, 2008, the managing member executed a regulatory agreement with the U.S. Department of Housing and Urban Development (HUD) in which the former owner agreed to be bound by the terms and conditions of the regulatory agreement for a mortgage loan insured by the Federal Housing Administration (FHA). The former owner purchased the project with more than $6.3 million in financing provided by Evanston Financial Corporation and insured by FHA under section 223(f) of the National Housing Act. The managing member also owned, leased, or operated at least 17 additional non-HUD-insured properties and was affiliated with 27 other businesses.

The former owner became delinquent on the project mortgage in September 2009. The mortgage company assigned the mortgage to FHA in July 2011 when the former owner was $169,485 behind on its mortgage payments. FHA paid a claim of more than $6 million to the lender on November 9, 2011, and sold the mortgage note on August 9, 2012, for $2.2 million.

Three different management agents managed the project between February 2008 and July 2011. From February 2008 to April 2010, 100 Percent Leased Management, LLC, an identity-of-interest company,[1] was the management agent. It maintained its office and records at 2400 Augusta Drive, Suite 453, Houston, TX. Centra Partners, LLC, located at 3730 FM 1960 West, Suite 300, Houston, TX, managed the project from May 2010 to March 2011. Sumar Realty Corporation, located at 3838 North Sam Houston Parkway, Suite 290, Houston, TX, managed the project from May 2011 to July 2011. After July 2011, 100 Percent Leased Management resumed managing the project.

[1] The identity of interest existed because the project owner's managing member was also the managing member of 100 Percent Leased Management, LLC.

The owner during our field work no longer owns or manages the project. An unrelated company, PEM FSF Yale Court, LLC, and UG Acquisition, LLC, purchased the note in August 2012 and sold it to Tidwell Apartments Houston, LP, in February 2013. The mortgage is no longer insured by FHA.

Between 2009 and 2013, HUD flagged the form HUD-2530 (Previous Participation Certification)[2] for the former owner and the managing member for financial default, failure to file financial statements, mortgage assignment, and unacceptable physical condition of the property.

Our objective was to determine whether the project owner used the project funds in accordance with the regulatory agreement and HUD regulations.

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2 HUD places 2530 flags or indicators in HUD's internal form HUD-2530 system to notify HUD personnel that the flagged parties have unresolved regulatory noncompliance issues if the parties attempt to conduct future business with HUD.

RESULTS OF AUDIT

Finding: The Former Project Owner Used More Than $3.5 Million in Project Funds in Violation of the Regulatory Agreement

From February 2008 through July 2011, the former owner inappropriately paid more than $3.2 million in unauthorized distributions, in transfers to non-HUD-insured properties, and to the former owner for advances; more than $16,000 in payments for other projects' expenses; nearly $16,000 in excess management fees; and more than $160,000 in unsupported disbursements. Further, the former owner underfunded the tenant security deposits by nearly $10,000. Additionally, the former owner used inappropriate documents to support more than $88,000 in withdrawals from the repair escrow account and inappropriately loaned project funds to six employees. As of July 2011, four employees owed the project $12,850. These conditions occurred because the former owner did not implement adequate controls to ensure compliance with the regulatory agreement and disregarded the project's regulatory agreement. The former owner's improper use of project funds reduced the amount available for physical repairs and payment of the mortgage, which resulted in the project being left in poor physical condition and contributed to the project's default on its $6.3 million FHA-insured mortgage, and the loss of nearly $4 million to the FHA insurance fund when FHA sold the mortgage note in August 2012.

The Former Owner Made Unauthorized Distributions, Transfers, and Repayments of Advances

The former owner violated the regulatory agreement when it made 308 transfers, unauthorized distributions, and repayments of advances totaling more than $3.2 million to 30 non-HUD-insured properties or affiliated entities from February 7, 2008, to July 15, 2011.[3] The inappropriate transfers included $900,000 in insurance proceeds that the former owner transferred to a bank in Israel.

Based on a review of bank statements and general ledgers, the former owner transferred more than $2.1 million into the project's account, including advances or additional equity contributions for reasonable and necessary operating expenses to sustain the project. However, bank statements showed that the former owner transferred more than $3.2 million for distributions or repayments of advances to the former owner, none of which HUD authorized. For example,

[3] Section 6(e) of the regulatory agreement prohibits owners from making or receiving and retaining any distribution of assets or any income of any kind of the project except surplus cash and except under certain other conditions without prior HUD approval. Section 13(g) of the regulatory agreement defines a distribution as any withdrawal or taking of cash or other assets of the project for anything other than reasonable expenses incident to the operation and maintenance of the project.

according to one of the management agents, the managing member instructed him to cancel a property mortgage payment and transfer $15,000 into his personal bank account and then to transfer an additional $3,000 into his identity-of-interest management agent's bank account in July 2011. Table 1 is a summary of fund transfers into and out of the project's account by year, while appendix A is a detailed list of the transfers. Since the project was in a non-surplus-cash position from February 2008 through July 2011, HUD prohibited repayments of advances.[4]

Table 1: Fund transfers to and from other entities

Year	Transfer of project funds to other entities	Transfer of funds from other entities	Net transfers out (transfers out less transfers in)
2008	$ 672,667	$ 406,756	$265,911
2008	900,000*		900,000
2009	868,149	659,012	209,137
2010	723,438	903,490	(180,052)
2011	81,153	191,010	(109,857)
Totals	**$ 3,245,407**	**$ 2,160,268**	**$ 1,085,139**

* Transferred to a bank in Israel by the managing member of Optimum

The project's 2008 audited financial statements showed that the project had surplus cash of $1.1 million. However, the independent auditor incorrectly calculated the surplus cash for 2008 when he included excess insurance proceeds from hurricane damage. Further, the financial statements were not issued until January 6, 2010, and would not have been an excuse for fund transfers in 2008 and 2009. According to HUD, surplus cash is calculated based on project operations.[5] Based on our calculation of surplus cash, the project was in a non-surplus-cash position during 2008. Also, the former owner had been delinquent on the project's mortgage since September 2009. Finally, there was no surplus cash in 2009 or 2010. Therefore, the project was in a non-surplus-cash position from the time the former owner purchased it in February 2008 through July 2011. Thus, the former owner was not authorized to make any distributions or repay any owner advances.

HUD sent the former owner several letters, dated June 30, 2009, February 26, 2010, April 27, 2010, and August 26, 2010, advising the former owner not to misuse the funds while the mortgage was in default. The independent auditor notified the former owner through the project's fiscal year 2008 audit report that distributions or repayment of advances could not be made if the project did not have surplus cash.

[4] Section 2-11 of HUD Handbook 4370.2, REV-1, Financial Operations and Accounting Procedures for Insured Multifamily Projects

[5] Section 7 of the regulatory agreement

However, the former owner disregarded this regulatory agreement requirement and continued to make distributions and repayments of advances.

The Former Owner Transferred $900,000 to a Bank in Israel

Due to damage sustained from Hurricane Ike in 2008, the project received $2.9 million in insurance proceeds. The former owner, specifically the managing member of Optimum,[6] instructed the project's bank to wire transfer $900,000 of the insurance proceeds from the project's bank account to a bank in Israel to repay a loan advanced to the project and to return $700,000 of owner equity. The project's general ledgers as of July 2011 showed that there was $527,473 in the Israeli bank after the former owner repaid a $350,000 non-HUD loan and accrued interest of $22,527 in December 2009. However, the former owner should not have transferred the project funds because the project had been delinquent on its mortgage since September 2009 and it was in a non-surplus-cash position.

The project owner was able to obtain the insurance proceeds without HUD's and the lender's endorsements. Contrary to sections 8(a) and (b) of form HUD-92447, Property Insurance Requirements, the insurance checks did not include HUD and the lender as payees.

Further, section 7 of the regulatory agreement required that money derived from any insurance on the property be applied in accordance with the terms of the mortgage. According to the deed of trust, insurance proceeds were to be paid to the note holder, which was Evanston Financial at that time.[7] The deed of trust allowed Evanston Financial to, at its option, apply excess insurance proceeds to the debt or release them for repairing or rebuilding the project. There was no evidence that Evanston Financial either applied excess proceeds to the debt or released them for repairing or rebuilding the project.

The Former Owner Used Inappropriate Supporting Documents To Withdraw Funds

The former owner used inappropriate documents, including a contract, an invoice, and a check, to support $88,560 in withdrawals from the repair escrow account.

The managing member requested a meeting with HUD staff on May 18, 2009, to discuss the reimbursements of draw requests since several noncritical repairs had not been completely addressed before the property suffered the effects of Hurricane Ike on September 13, 2008. At that time, it became impossible to distinguish between what required reimbursement from insurance proceeds and

6 According to the former owner's membership regulations, other than the managing member, its members, which included Optimum, had no managerial power unless explicitly authorized by a majority vote of the members.

7 Paragraph 7 of the deed of trust

what would be covered by the repair escrow. HUD staff explained to the managing member in the meeting that any invoice dated before Hurricane Ike that had been paid and had not been submitted in previous draws would be reimbursed and any invoice dated after Hurricane Ike would be considered storm damage and would not be eligible for repair escrow proceeds.

The managing member then submitted documents that were created after the fact to support withdrawing $88,560 from the property's escrow account on May 20, 2009. These documents included a general contract, an invoice, and a check made payable to a construction company as proof of payment. The general contract was dated August 18, 2008, before Hurricane Ike, but was signed and notarized on August 18, 2009, after Hurricane Ike and after the submission date. The owner of the construction company confirmed and provided evidence showing that the invoice was not his and claimed to have not done the work and not received the money. The back-dated check made payable to the construction company was voided and not cashed, although the money was removed from the escrow account and deposited in the project account.

The Former Owner Paid The Expenses Of Other Projects

The former owner made 13 disbursements totaling $16,292 from the project's petty cash fund and used its debit card and checking account for expenses[8] that benefited other non-HUD-insured properties. These ineligible expenses are listed in table 2 and include payments for utilities, accounting fees, labor costs, and eviction fees.

Table 2: Ineligible expenses paid for other properties

Source	Date	Project	Purpose	Amount
Petty cash	09/22/2008	Arbor Oak	Eviction fee	$650
Petty cash	09/26/2008	Arbor Oak	Contract labor	3,658
Petty cash	09/26/2008	Arbor Oak	Maintenance	192
Petty cash	10/01/2008	Yishlam, Inc.	Contract labor	8,059
Debit card	05/20/2008	Meadow Rose	Electric bill	567
Debit card	06/19/2008	Meadow Rose	Electric bill	458
Debit card	09/03/2008	Meadow Rose	Electric bill	781
Debit card	10/16/2008	Meadow Rose	Electric bill	9
Debit card	07/17/2008	Meadow Rose	Electric bill	301
Debit card	08/18/2008	Meadow Rose	Electric bill	321
Debit card	11/13/2008	Meadow Rose	Electric bill	9
Debit card	04/25/2008	Meadow Rose	Electric bill	387
Check # 3174	04/15/2011	Various projects	Accounting fee	900
Total				**$16,292**

8 Section 6(b) of the regulatory agreement prohibits paying out any funds except for reasonable operating expenses or necessary repairs unless it is from surplus cash.

Further, timesheet and payroll records showed that the project manager and maintenance staff worked at other properties while their entire salaries were paid from project funds. Both the project manager and the maintenance person estimated that they spent 80 percent of their time at the project and 20 percent at two other projects. There was no indication in the general ledger that the other properties reimbursed the project for their salaries. Since the timesheets did not show how many hours each employee worked for the other properties, we could not reliably estimate the amount of funds that the other projects should have reimbursed to the project.

The Former Owner Overpaid Management Fees

The former owner overpaid $15,935 in management fees to 100 Percent Leased Management, LLC, an identity-of-interest management agent, at a time when Centra Partners, a non-identity-of-interest management agent, managed the project. According to Centra Partners' certification, the fees should have been 3.5 percent of project income.[9] However, 100 Percent Leased Management, LLC was paid 5 percent of rental and miscellaneous income collected. 100 Percent Leased Management, LLC passed 3.5 percent to Centra Partners and kept the remaining 1.5 percent. As a result, the former owner overpaid $15,935 in management fees to 100 Percent Leased Management, LLC from May 6, 2010, to March 11, 2011.

The Former Owner Made Unsupported Disbursements

The former owner could not adequately support that 57 of 74 disbursements totaling more than $163,000[10] were for the project. Although the project is located in Houston, TX, the unsupported disbursements included payments to the City of Galveston, purchases from a Home Depot in Galveston, hotel costs in San Antonio and Washington, DC, and other expenses, which lacked support to show that they were for the project. Further, some disbursements appeared to be for meals and entertainment, such as project payments to a delicatessen, a Houston spa, and a

9 HUD Handbook 4381.5, REV-2, paragraph 3-2(b), relating to allowable management fees from project funds, states that fees should be derived from project income (residential, commercial, and miscellaneous). Sections 2-2 and 3-1 state that the management agent is subject to HUD approval and the management fees may be paid only to the person or entity approved by HUD to manage the project.

10 Section 6(b) of the regulatory agreement states that without prior HUD approval, the owner must not assign, transfer, dispose of, or encumber any personal property of the project, including rents, and must not pay out any funds except for reasonable operating expenses and necessary repairs. HUD Handbook 4370.2, REV-1, paragraph 2-6E, requires that all disbursements from the regulatory operating account be supported by approved invoices or bills or other supporting documentation.

Galveston water park. See appendix B for a list of the 57 unsupported disbursements.

The Former Owner Underfunded the Tenant Security Deposit Account

The former owner did not fully fund the project's tenant security deposit account as required.[11] The former owner acquired the project in February 2008 and certified on February 7, 2008, that the tenant security deposit was fully funded. However, it did not open a tenant security deposit bank account until April 15, 2010, and did not fully fund it. From February 2008 through April 15, 2010, the former owner deposited and refunded tenant security deposits using the project's operating bank account. According to the project's general ledger, the security deposit should have been more than $34,000 as of July 2011. According to the management agent in July 2011, the security deposit should have been nearly $10,000. We accepted the management agent's estimate of the necessary balance over the general ledger estimate because the management agent prepared the tenant security deposit liabilities based on the tenant files, which we considered to be more reliable than the general ledger. However, the maximum balance that was ever in the tenant security deposit bank account was $7,087. The managing member transferred $7,000 to his identity-of-interest management agent on March 18, 2011, and following the transfer, there was only $87 in the tenant security deposit bank account.

The General Ledger Showed Outstanding Loans to Employees

According to the general ledger, the former owner inappropriately loaned project funds to six employees. The ledger also showed that some of the employees had repaid some of the loans through their payroll. However, as of July 2011, four employees owed the project $12,850. [12]

The Property Was in Poor Physical Condition and Its Obligations Remained Unpaid

The former owner did not maintain the project in good repair and condition as required by section 7 of the regulatory agreement. HUD's Real Estate Assessment Center performed physical inspections of the property on February 12, 2010, and

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11 Section 6(g) of the regulatory agreement states that any funds collected as security deposits must be kept separate from all other funds of the project in a trust account, the amount of which must at all times equal or exceed the total of all outstanding obligations under the account.

12 Section 6(b) of the regulatory agreement prohibits paying out any funds except for reasonable operating expenses or necessary repairs unless it is from surplus cash.

July 15, 2011. The property failed the inspections and received a score of 57c and 51c, respectively. The "c" indicated health and safety deficiencies. Further, the Real Estate Assessment Center reports identified serious physical deficiencies, such as obstructed or missing accessible route and damaged soffits, fascia, walls, and vents.

According to one management agent, as of June 2011, the project had not paid its electric bills since January 2011 and owed more than $60,000. The management agent also said that vendors, including the mortgage company, did not accept checks from the project or its identity-of-interest management agent because of a history of insufficiently funded checks. The project had more than $200,000 in unpaid bills, not including the $169,485 in delinquent mortgage payments, as of July 2011. At various times during May and June 2011, cable, gas, trash removal, phones, and Internet services, as well as a rent roll system, had been terminated for varying lengths of time. Further, HUD's management review in September 2011 disclosed that the project had been without water for about 3 weeks.

The Former Owner Did Not Maintain Accurate Financial Information

The project's books and records were incomplete and inaccurate.[13] Transactions were not always recorded in the check registers or general ledgers. Further, the independent auditor stated that he could not complete the 2009 audited financial statements because of incomplete books and records. The former owner submitted the project's 2008 audited financial statements to HUD but had not submitted the 2009 and 2010 audited financial statements as required.[14]

Conclusion

The former owner failed to maintain accurate financial records and further violated the regulatory agreement by not submitting annual audited financial statements for 2009 and 2010. As a result, HUD and other stakeholders could not properly assess the project's true financial condition.

The former owner disregarded the project's regulatory agreement and diverted or misused $3.2 million of the project funds and insurance proceeds when the project was in a non-surplus-cash position. Further, the former owner did not fully fund tenant security deposits and made loans to employees from project funds.

[13] Sections 9(c) and 9(d) of the regulatory agreement require the owner to keep the books and accounts of the project operations in condition for a proper audit and in accordance with HUD requirements. HUD Handbook 4370.2, REV-1, paragraph 2-3B, requires that financial records be complete, accurate, and updated monthly.

[14] Section 9(e) of the regulatory agreement requires the owner to submit audited annual financial statements within 60 days following the end of each fiscal year. HUD extended the time to submit them to 90 days in 24 CFR 5.801(c)(2).

Additionally, the former owner used several inappropriate documents to support more than $88,000 in withdrawals from the repair escrow account. As a result, the project was in poor physical and financial condition, and HUD suffered a loss of nearly $4 million when it resold the note.

Since the auditee no longer owns the project, there are no recommendations in this report to address the causes. Rather, the recommendations are designed to prevent the auditee from causing similar problems at other FHA-financed projects and for pursuing any possible recoveries from the auditee for the loss that FHA suffered when it resold the note.

Recommendations

We recommend that the Director of HUD's Houston, TX, Office of Multifamily Programs

1A. Expand the 2530 flags on all the former project owners and managing members to include the regulatory agreement violations noted in this report.

We recommend that the Director, Departmental Enforcement Center,

1B. Pursue civil money penalties and administrative sanctions, as appropriate, against the owner, operator, and/or their principals/owners for their part in the regulatory violations cited in this report.

SCOPE AND METHODOLOGY

We conducted the review at the offices of 100 Percent Leased Management, LLC, the project, and the local HUD office in Houston, TX. Our review period was February 7, 2008, to July 15, 2011. To accomplish our objective, we

- Reviewed background information and the criteria that controlled the insured multifamily housing project.
- Reviewed various reports and documents to determine the financial and physical unit conditions at the project. The reports and documents included available independent public accountant reports for fiscal year 2008, information contained in HUD's Real Estate Management System, and documents maintained by the multifamily project manager assigned to monitor the project.
- Reviewed funds transferred into and out of the project's bank accounts and contacted the independent public accountant and obtained his audit working papers supporting the findings in the project's 2008 audited financial statements.
- Performed a walk-through inspection of the exterior of the project and reviewed HUD inspection reports to determine the project's overall physical condition.
- Reviewed tenant security deposit accounts.
- Reviewed the loan payment history and reserve for replacement and escrow accounts for the audit period.
- Reviewed insurance deposits and contacted the appropriate insurance agent for information to determine whether insurance proceeds were properly accounted for.
- Reviewed disbursements and deposits in the accounting records and supporting documentation to determine whether they appeared appropriate. We reviewed and tested a nonstatistical sample of 74 disbursements totaling $224,955 from a total of more than $8.7 million disbursed, excluding fund transfers, during the audit period. The selected sample included various vendors, accounts, and transactions that were, based on our professional judgment, likely to have a high risk of error. The conclusions reached in this report relate only to the sample items tested and have not been projected to the universe of approximately 1,900 disbursements.
- Reviewed the project's electronic format check registers and general ledgers. We assessed the computerized data and found that the transfers and disbursements were not always recorded in the check registers and general ledgers. The audit results, therefore, are also based on our review of source documentation, including check vouchers, invoices, and bank records.
- Interviewed the former managing member, management agent staff from all three management agent companies, a contractor, the project manager, and HUD officials.

We performed the audit from July 2011 to January 2012. FHA sold the note on August 9, 2012. The report documents what we found while the project was FHA insured and the former owner was obligated by the regulatory agreement. We conducted the audit in accordance with generally accepted government auditing standards, except as noted below. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective(s). We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

We did not comply with the auditing standard for early communication of control deficiencies resulting in noncompliance with provisions of laws, regulations, contracts, or grant agreements, or abuse because we suspended the audit from January 2012 to September 2013 at the request of our Office of Investigation and the U.S. Department of Justice. We then updated our review work to incorporate changes in the project's status and revise our recommendations.

INTERNAL CONTROLS

Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objective:

- Controls over compliance with laws and regulations and
- Controls over disbursements.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiency

Based on our review, we believe that the following item is a significant deficiency:

- The project owner did not implement adequate policies and procedures to ensure compliance with the regulatory agreements and HUD regulations (finding).

APPENDIXES

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

The Director, Office of Multifamily Programs in Houston agreed with the report and the recommendations and elected not to submit written comments.

Appendix B

FUND TRANSFERS INTO AND OUT OF THE PROJECT

February 7 to December 31 2008, transfers

Payee or payor	Transfer out of Yale Court	Transfer into Yale Court	Net transfer out of Yale Court
100% Leased Management, LLC	$110,000	$35,000	$75,000
Aqua Bella, LLC	6,900		6,900
Arbor Oak Apartments	34,250		34,250
Evia Israel, LLC	200		200
Kasif, Inc.	56,625	14,770	41,855
One Rose Meadow Apartments	1,400		1,400
Yishlam, Inc.	26,000	28,000	(2,000)
Carriage House	200,000	90,000	110,000
Houstate	5,000	5,000	0
Optimum RE Investments Equity	70,986	20,986	50,000
Shiraz Inwood Oaks	65,000	50,000	15,000
Shiraz US Galveston	83,000	163,000	(80,000)
Shodim, LLC	13,306		13,306
Bank Leumi	900,000		900,000
Totals	**$1,572,667**	**$406,756**	**$1,165,911**

January 1 to December 31, 2009, transfers

Payee or payor	Transfer out of Yale Court	Transfer into Yale Court	Net transfer out of Yale Court
100% Leased Management, LLC	$51,800		$51,800
Arbor Oak Apartments	420,600	137,750	282,850
Houston Coloventure, LLC	21,881	50,000	(28,119)
Managing Member Optimum	29,000	113,029	(84,029)
BlueBay Amberwood	33,500		33,500
Bluebay Yale	69,800	900	68,900
Shiraz Inwood Oaks, LLC	113,594	256,221	(142,627)
Yishlam, Inc.	47,600	3,700	43,900
One Rose Meadow Apartments	14,200	7,000	7,200
Kasif, Inc.	10,691	59,290	(48,599)
Prosperity Avenue Apartments	2,145		2,145
Evia Israel, LLC	6,300		6,300
Coral Isle, Inc.	3,600		3,600
Shiraz Galveston	800	17,122	(16,322)
Optimum RE Investments, LLC	798		798
Foreclosure International Dallas, LLC	5,000	5,000	0
Unknown – Other accounts	19,840		19,840
Shiraz Galveston***1935		9,000	(9,000)
BlueBay Colonial Square Apartments (Galveston)	17,000		17,000
Totals	**$868,149**	**$659,012**	**$209,137**

January 1 to December 31, 2010, transfers

Payee or payor	Transfer out of Yale Court	Transfer into Yale Court	Net transfer out of Yale Court
2828Q – Account ***8496	$300	$1,000	($700)
100% Leased Management, LLC	71,700	58,055	13,645
2828Q – Account ***7439	4,360	0	4,360
5008 Avenue S	3,030	2,000	1,030
A/R Blue Bay Construction	5,000	5,000	0
Amberwood Apartments	8,905	1,700	7,205
Aqua Bella, LLC	31	6,900	(6,869)
Arbor Oak Apartments	276,710	252,495	24,215
Dor Estates, LLC	14,000	14,000	0
Evia Israel, LLC	10,722	6,600	4,122
Houston Coloventure, LLC	2,970	1,300	1,670
Kasif, Inc.	43,075	43,870	(795)
One Rose Meadow Apartments	8,310	15,601	(7,291)
Employee - Loan	1,050		1,050
Oak Villa Apartments	8,200	5,200	3,000
Managing Member Shiraz US Yale LLC	5,000	15,500	(10,500)
Optimum Global Investments, LLC	3,640		3,640
Park Valley Apartments	58,494		58,494
Prosperity Ave, LLC	360		360
Shiraz Galveston	4,960	303,088	(298,128)
Shiraz Inwood	50,042	98,800	(48,758)
Spanish Trail	1,900	1,900	0
Managing Member Optimum	84,029		84,029
Transfer withdrawal per Tzur Email	16,650	5,650	11,000
Yishlam, Inc.	16,800	50,700	(33,900)
Note Payable Oak Villa Apts	15,500	1,000	14,500
Unknown - Other accounts	7,700	13,130	5,430
Totals	**$723,438**	**$903,490**	**($180,052)**

January 1 to July 15, 2011, transfers

Payee or payor	Transfer out of Yale Court	Transfer into Yale Court	Net transfer out of Yale Court
100% Leased Management, LLC	$3,000	$3,410	($410)
A/R Blue Bay Construction	20,000	23,000	(3,000)
Arbor Oak Apartments	1,300	0	1,300
One Rose Meadow Apartments	2,000		2,000
Managing Member Shiraz US Yale, LLC	15,000		15,000
Prosperity Ave, LLC		36,400	(36,400)
Shiraz Inwood	39,503	128,200	(88,697)
Other accounts	350		350
Totals	**$81,153**	**$191,010**	**($109,857)**

Total transfers 2008 - 2011

Year	Transfer out of Yale Court	Transfer into Yale Court	Net transfer out of Yale Court
2008	$1,572,667	$406,756	$1,165,911
2009	868,149	659,012	209,137
2010	723,438	903,490	(180,052)
2011	81,153	191,010	(109,857)
Totals	**$3,245,407**	**$2,160,268**	**$1,085,139**

Appendix C

UNSUPPORTED DISBURSEMENT SAMPLES

Payment method	Date	Payee	Purpose	Amount
Debit card	06/04/2008	AFLAC Insurance - Houstate	Health insurance	$ 205
Debit card	11/10/2008	Alamo Rental Car - Houston	Rental car	1,195
Debit card	11/10/2008	Alamo Rental Car - Houston	Rental car	143
Debit card	08/14/2008	Amazon.com	Furniture and equipment	730
Wire transfer	09/23/2009	Amsalem Business Travel	Travel expenses	6,978
Check #2063	08/12/2009	BITUM	Fix asphalt	4,000
Check #2083	09/03/2009	BMB, INC.	Property insurance	28,302
Debit card	2/11/2009	City of Galveston	Unknown	1,960
Check #3142	03/11/2011	David Dahan Plumbing	Plumbing	4,614
Debit card	04/05/2010	Delta Airlines - Atlanta, GA	Airfare	556
Debit card	04/05/2010	Delta Airlines - Atlanta, GA	Airfare	556
Check #1941	06/04/2009	HD Supply Facilities Maintenance	Unknown	9,077
Check #2250	11/22/2009	HD Supply Facilities Maintenance	Appliances	11,263
Debit card	03/02/2009	Highland Products Group	Unknown	367
Debit card	02/02/2009	Hilton Hotel - Washington DC	Hotel	274
Debit card	02/02/2009	Hilton Hotel - Washington DC	Hotel	274
Debit card	08/03/2009	Home Depot 6574 - Galveston	Materials	101
Debit card	05/03/2010	Home Depot 6574 - Galveston	Unknown	290
Wire transfer	04/20/2011	Home Depot 6574 - Galveston	Unknown	128
Debit card	04/09/2010	Hotel Contessa - San Antonio	Hotel	605
Debit card	4/21/2010	Hotel Contessa - San Antonio	Hotel	55
Debit card	4/23/2009	Hotels.com	Unknown	63
Debit card	07/10/2008	Kenny and Ziggy’s Deli - Houston	Meals	142
Debit card	07/10/2008	Kenny and Ziggy’s Deli - Houston	Meals	93
Debit card	09/01/2009	Moody Gardens Spa - Galveston	Spa	234
Wire transfer	09/14/2009	Moody Gardens, Inc. - Galveston	Bonus	527
Wire transfer	09/14/2009	Moody Gardens, Inc. - Galveston	Bonus	527
Wire transfer	09/15/2009	Moody Gardens, Inc. - Galveston	Bonus	240
Check #3062	08/06/2010	Namco Manufacturing, Inc.	Sewer machine	1,500

Check #2350	01/18/2010	Oak Villa/Arbor Oaks, LLC	Reimburse for burner	156
Wire transfer	06/24/2010	Oak Villa/Arbor Oaks, LLC	Reimburse for pool supplies	416
Debit card	01/23/2009	Unknown person or company	Unknown	2,054
Debit card	01/07/2009	Olshan Lumber Company	Unknown	2,392
Check #1451	10/6/2008	Optimum Arbor Oak	Reimbursed for purchase order #1241	8,486
Wire transfer	01/13/09	unknown	Unknown	17,539
Debit card	10/06/2010	SBI Finance	Insurance	5,349
Debit card	12/08/2010	SBI Finance	Insurance	5,349
Debit card	02/07/2011	SBI Finance	Insurance	5,349
Check #3088	8/31/2010	SBI Finance	Insurance	10,483
Check #2087	09/02/2009	Schlitterhahn (water park)	Three tickets for the project manager for waterpark	127
Debit card	07/20/2009	Schlitterhahn - Galveston	Meals and entertainment	346
Check #1835	03/26/2009	Shiraz Inwood Oak	Unknown	7,337
Wire transfer	07/07/2011	Shiraz Inwood Oak	Unknown	1,370
Check #2303	12/22/2009	SICOLA Corporation	Landscaping & lawn maintenance	3,464
Check#2084	09/03/2009	Project manager	Bonus + commission	2,638
Debit card	06/04/2008	T- Mobile – Managing member Shiraz Yale, LLC	Telephone expenses	2,142
Wire transfer	07/03/2009	Managing member of Optimum	Airfare	1,500
Check #1160	07/29/2009	Managing member of Optimum	Hotel	1,853
Check #1175	07/30/2009	Managing member of Optimum	Hotel	371
Wire transfer	05/06/2011	Managing member of Optimum	Hotel	459
Check #3259	01/25/2011	Tax Recourse, LLC	Unknown	4,159
Debit card	9/26/2008	Trellis Spa - Houston	Spa	240
Check #2059	08/10/2009	WCA of Texas Houston Hauling	Trash	3,104
Debit card	07/13/2009	Yahoo Hotjobs	Advertising	337
Check #3202	05/06/2011	Unknown person	Unknown	1,000
Check #3112	10/21/2010	Unknown person	Reimburse for soil	215
Check #3248	03/10/2011	Unknown person	Reimburse for materials	255
			Total	**$163,489**