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BARRON'S
Online

White Male Over 40 Sues HUD, and the Department's Big Loan Sale Is in Peril

Jim McTague



A much-touted Clinton Administration effort to reinvent the Department of Housing and Urban Development is nearing collapse. The endeavor called for the mass sale of HUD's multibillion-dollar portfolio of low-income housing loans.

The department may find itself forced to abandon the program, at least for the near future, because of a vitriolic lawsuit by an unhappy contractor who alleges widespread favoritism and bidding irregularities by the HUD bureaucracy. Some HUD officials doubt the program can be cranked up again if it is shut down for a protracted period. President Clinton has praised the program and offered it as a model for asset sales by other government agencies.

The plaintiff, John Ervin of Bethesda, Md., is asking the federal court for the District of Columbia to halt the program pending the outcome of his lawsuit, a list of alleged outrages supported by, among other things, leaked documents and anonymous messages purportedly from a HUD insider that were left on his telephone answering machine. Ervin accuses HUD of "palpable bias against its white male career employees over the age of 40, and against white-male-owned contractors."

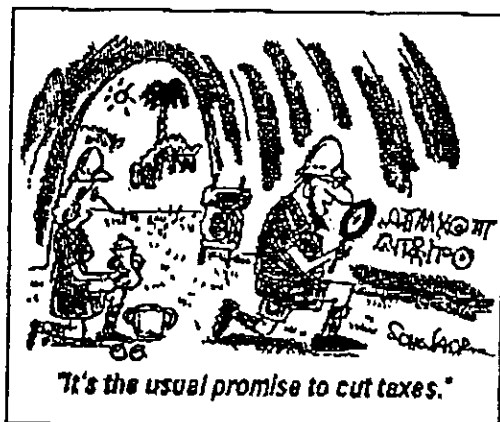
A former female housing official, he says, illegally steered millions of dollars worth of contracts to firms run by close women friends and by minorities. Not only does Ervin assert that his status as a white male is a problem, but he also contends HUD has blackballed his firm because he dared blow the whistle on the supposed old-girl network.

Nicholas Retsinas, HUD's assistant secretary for housing, maintains the suit is without merit and is a consequence of HUD's struggle to privatize a federal program that hasn't served the taxpayers. In other words, HUD argues, people like Ervin who cashed in under the old system are being squeezed by new

players.

Ervin made about \$7 million a year servicing mortgages for HUD, according to his suit. He admitted to *Barron's* that he loses out if those loans are sold to private-sector companies. However, Ervin asserts there are other services he could perform for HUD if only he could get a fair shot at the contracts. Ervin accuses a former HUD deputy secretary, Helen Dunlap, of freezing him out and improperly awarding financial-advisory contracts of almost \$40 million to Hamilton Securities, a small firm headed by a woman, C. Austin Fitts. Fitts was recruited by a former Treasury Secretary, Republican Nicholas Brady, to head the Federal Housing Administration. She was later bounced by Jack Kemp, who was HUD Secretary at the time. Ervin also complains that Dunlap awarded work to a woman, Nancy Andrews, who, on visits to Washington on HUD business, stayed at Dunlap's home and received free office space from HUD. The department says it often supplies space inside its building for its outside contractors and that the practice has been vetted by HUD's ethics police. In his suit, Ervin cites anonymous sources quoting Dunlap as saying, "The only fitting position for a white male is secretary."

Dunlap, who denies any wrongdoing, left HUD in September to become president of the National Low Income Housing Coalition, an advocacy group. Like Retsinas, she declares there is no merit to any of Ervin's charges.



Harley Schwarzen for Barron's

Since the loan sales began last year, HUD has disposed of 1,200, or half, of its multi-family mortgages and 47,000, or 52%, of its single-family mortgages. The agency sells the assets at around 75 cents on the dollar but claims to be saving taxpayers about \$1 billion in the long run because the loans tend to lose value in the hands of the federal government. Purchasers have included GE Capital, BlackRock Capital Finance and Berkeley Federal Bank & Trust.

Hamilton has laid most of the groundwork for those asset sales. Ervin complains that a \$1 million financial advisory contract Hamilton successfully bid for in 1992 subsequently was amended, and that by 1994 the value of the pact had reached \$18 million. HUD finally put the contract out for new bids, selecting three additional advisers - Merrill Lynch, CS First Boston and Cushman & Wakefield. He charges that Dunlap stacked the deck so he wouldn't win. Then Dunlap contrived to have Hamilton selected as a "super" adviser, overseeing the other firms, for \$25 million a year.

In his suit, Ervin also complains that HUD is engaged in a cover-up to keep him from unearthing proof of the gigantic conspiracy he alleges and has failed to answer 60 requests for information that he has made under the Freedom of Information Act. HUD says it's trying to meet the request, but it has been slowed by the volume of his requests. The department contends Ervin has requested thousands of pages, using the FOIA in lieu of the normal lawsuit discovery process.

Prior to Dunlap's arrival, Ervin was a consistent beneficiary of HUD

contracts. Between 1989 and 1994, he won more than \$25 million in HUD contracts. His firm, Erwin & Associates, grew from a staff of five to more than 40 people. The head count has fallen back to fewer than 25 employees. HUD, Ervin admits, was the sole source of his livelihood.

Farmer Mac Sues, Fears Loss of Capital

The Federal Agricultural Mortgage Corp., or Farmer Mac, a congressionally chartered mortgage company whose shares trade on Nasdaq, also is enmeshed in a high-stakes lawsuit.

Farmer Mac is suing the Western Farm Credit Bank of Sacramento, Calif., a former business partner, for breach of contract. The suit was filed last month in federal court in Washington. Farmer Mac has three classes of stock. Only the 1.2 million Class C nonvoting shares are available to the public, however. The 990,000 shares of Class A voting stock are owned by financial institutions that don't belong to the government-sponsored Farm Credit System. Institutions that do belong to the system are issued Class B stock, of which there are 593,000 outstanding shares.

In a letter to Louisiana Republican Richard Baker, who chairs the House Subcommittee on Capital Markets, Securities and Government Sponsored Enterprises, Farmer Mac admitted that a courtroom defeat would result in a loss of capital. The company already is undercapitalized by \$10 million and is operating on a temporary waiver from Congress.

Farmer Mac is a hayseed version of Fannie Mae, or the Federal National Mortgage Association. Its mission is to provide a secondary market for farm and rural housing mortgages. Trouble is, there aren't enough of such loans being originated to keep Farmer Mac in business. Congress has expanded the agency's lending authority to allow it to buy rural home mortgages, but it is too early to tell if that business will take off.

Western is a regional farm credit bank. Last November it agreed to find loans for Farmer Mac. Western and Farmer Mac got into a fight about the sales price for one pool of about \$40 million in loans, and Western unilaterally terminated the contract. Farmer Mac is suing for an unspecified amount. Western is expected to file a countersuit shortly.



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PM-HUD Firing,370

Financial firm fired after HUD discovers \$3.8 million error

By JENNIFER ROTHACKER

Associated Press Writer

WASHINGTON (AP) — A computing error the government says cost it \$3.8 million has led to the firing of the financial services firm accused of making the mistake.

The Department of Housing and Urban Development has ordered Hamilton Securities Advisory Services Inc. to reimburse the money and suggested it may order further retribution pending an investigation.

The Washington, D.C.-based firm defended its work for HUD, and claimed the department owed it \$1.6 million for work successfully completed.

HUD hired Hamilton in 1993 as a financial adviser for a mortgage note auction program that earns HUD millions of dollars a year.

When a property owner defaults on a mortgage insured by the Federal Housing Administration, HUD becomes the owner of the mortgage. The auction program takes the mortgages out of HUD's hands by selling them to the private sector.

Because HUD does not have the expertise to value notes, it hired financial advisers, including Hamilton, to optimize the government's profits.

An investigation ordered by HUD Secretary Andrew Cuomo to ferret out abuse and fraud throughout HUD concluded that Hamilton "failed to provide accurate financial advisory services to the mortgage note sales program" since its contract started in 1992, HUD said in a news release.

HUD did not specify how the company failed, but The Washington Times reported Monday that Hamilton made "erroneous instructions" for a computer model used to optimize a dozen sales of these mortgages. HUD has not suggested that Hamilton intentionally made the mistakes.

The failure resulted in a \$3.8 million loss for HUD, the department said.

HUD wrote C. Austin Fitz, chief executive of Hamilton, on Friday, demanding reimbursement and terminating the company's contract.

In a release issued Monday, Hamilton defended its work for HUD, arguing that it has given taxpayers an "extraordinary return" of

billions of dollars through its work in the auction program.

HUD said it is reviewing all work performed by Hamilton and may make additional claims.

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Firing of Outside Financial Adviser Only Adds to Political Furor for HUD

Department Left to Deal With \$4 Million Error, Charges of Favoritism

By Judith Havemann
Washington Post Staff Writer
Tuesday, October 28, 1997; Page A19
The Washington Post

When the Department of Housing and Urban Development abruptly fired its main outside financial adviser Oct. 17, it intensified a political furor over what is ordinarily the most commonplace of government activities: contracting out for expertise in the private sector.

HUD said the firm, Hamilton Securities Advisory Services, which ran a computerized review of complicated bids for HUD loan sales, had made a technical error with serious consequences. "Had Hamilton not made an error, [the government] would have been \$4 million richer," said a senior HUD official who declined to be named. "I think \$4 million is a lot of money."

The company, which had been hired by HUD's previous management, responded that the firing was motivated by the campaign of the department's new leadership to appear tough on waste, fraud and abuse. Leslie H. Lepow, Hamilton's attorney, said the error amounted to a mere .05 percent of the money Hamilton helped bring in to the federal treasury.

"The company did make a mistake," Lepow said. "We immediately brought it to the department's attention. The effect was minimal . . . and we think that politics are what is driving this."

The uproar over Hamilton opens a window on an obscure but hugely important part of Washington's economy. Federal government contracting to local firms accounts for \$20 billion in the region's \$170 billion economy.

Hamilton Securities, headed by former federal housing commissioner C. Austin Fitts, was hired by HUD four years ago to provide financial advice on HUD's sale of

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115,000 "troubled" mortgages to the private sector. The Federal Housing Administration had insured the mortgages under a long-established program to help low- and moderate-income Americans buy homes. When thousands of owners began to fall behind in their payments about a decade ago, HUD had few resources to go after them.

The loan sales program was designed to take the mortgages off HUD's hands by selling them to investors more deft at collecting the delinquent monthly payments. HUD hired Hamilton and three of the nation's largest financial firms to help it oversee the program.

Today, the loan sales program has yielded \$9.5 billion, about \$2.1 billion in "profit," Hamilton says. At the same time, the program and the company's role in it have become embroiled in civil and criminal litigation, been the subject of more than 200 freedom of information requests and submerged the department under thousands of subpoenaed documents.

A lawsuit filed more than a year ago by a Bethesda contractor, Ervin and Associates, charges that Hamilton was awarded the contract because of illegal favoritism, and that the firm's handling of the entire bid sale is tainted.

Ervin and Associates' annual business with HUD fell from \$7 million to less than \$100,000 in recent years. In court papers, John Ervin, the company's president, charged the department with contract fraud, bid rigging, insider dealing and retaliation against him. He said that a former HUD official who was in charge of the loan sale program was prejudiced against white men.

Ervin alleged that HUD had shown favoritism to Hamilton, which is a female-headed firm, by steering contracts to it. And Hamilton's acknowledgment of an error, according to Ervin spokesman Daniel M. Hawke, is a "preemptive strike" to explain away "conduct that is really much more sinister."

Hamilton's attorneys deny the charges. "There was no favoritism, no bid rigging, and no fraud," Lepow said.

But to Ervin, the situation seems plain. "The firing of Hamilton has everything to do with the Ervin case," Hawke said. "There are two reasons for this: There is a new secretary of HUD [Andrew M. Cuomo] who is interested in cleaning up things that have gone wrong in the agency, and secondly . . . we have forced the agency to dig into our allegations."

Some of the allegations are the subject of a 15-month-long criminal investigation by the HUD inspector general, which is continuing. Meanwhile, Ervin's lawsuit is pending in federal district court. The Justice Department, in papers filed earlier this month, asked for a delay "so that the

parties could explore the possibility of a settlement."

HUD said it decided to fire Hamilton now, after waiting nearly a year, because the error alone was not sufficient reason to terminate the contract.

"There are four factors, which when combined rise to a level of termination," said Federal Housing Commissioner Nicolas Retsinas in a statement released by HUD. "They are: reduced capacity of Hamilton Securities, the imminent completion of the note sales program; passage of [new] legislation; and past performance errors by Hamilton."

The error committed by Hamilton related to its "optimization" computer program to determine the winning bidders for the loans

In an effort to maximize interest in the loan sale, the government allowed bidders to bid on packages of loans. Because of the complicated nature of the bids, involving hundreds of properties and many bidders, a computer model was used to sort out the best combination.

Sources said Hamilton told the bidders to state their minimum bid using one accounting method, but the computer was programmed to recognize another. The contractor translated the bidder's terminology into computer terminology, which was sufficiently different that the government received \$3.8 million less than it would have on overall mortgage sales of \$9.5 billion.

HUD has demanded that Hamilton voluntarily repay the \$3.8 million and the company, strapped for funds because of the firing, has offered to discuss a settlement.

About \$2.5 billion in loans remain to be sold, a departmental official said. "Until FHA has a new financial adviser," said Retsinas, the Federal Housing Administration commissioner, "the department cannot conduct pending note sales and insure that the sales generate maximum returns for the taxpayer."

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HUD Fires Financial Adviser

By Jennifer Rothacker
Associated Press Writer
Monday, October 20, 1997; 7:27 p.m. EDT

WASHINGTON (AP) -- The federal housing department fired one of its top financial advisers after discovering the company made an error that resulted in a \$3.8 million loss.

Hamilton Securities Advisory Services Inc. said Monday it was "extremely proud of its work" for the Department of Housing and Urban Development and hoped to reach an amicable resolution.

Hamilton was hired to be a chief financial adviser for a mortgage note sales auction program that earns HUD millions of dollars a year.

When a property owner defaults on a mortgage insured by the Federal Housing Administration, HUD then becomes owner of the mortgage. The auction program takes these mortgages out of HUD's hands by selling them to the private sector.

Because HUD does not have the expertise to value notes, it hired financial advisers -- including Hamilton -- to optimize the government's profits.

An investigation ordered by HUD Secretary Andrew Cuomo to ferret out abuse and fraud throughout all of HUD concluded that Hamilton "failed to provide accurate financial advisory services to the mortgage note sales program" since its contract started in 1992, HUD said in a news release.

HUD did not specify how the company failed, but The Washington Times reported Monday that Hamilton made "erroneous instructions" for a computer model used to optimize a dozen sales of these mortgages. HUD has not suggested that Hamilton intentionally made the mistakes.

That failure resulted in a \$3.8 million loss for HUD, the department said.

HUD wrote C. Austin Fitz, chief executive of Hamilton, on Friday, demanding reimbursement and terminating the company's contract.

units—far below the requirements of such a fast-growing state with so many low-wage jobs.

Nonprofit organizations offer even more hope. New York's East Harlem helps illustrate why. On East 105th Street, a solid rectangular apartment building with newly planted trees houses 101 elderly people. A few blocks away, on East 106th Street, fresh paint and new windows mark the apartment building as recently rehabilitated. More new paint and a sign, "Affordable Housing for New Yorkers," decorate a narrow building on 117th Street. The three buildings are the handiwork of Hope Community, which gets its funding from a complicated mix of HUD's Home Program, Community Development Block Grants, low-income-housing tax credits, city money and other sources. Executive Director Mark Alexander describes an endless maze of arcane regulations—some imposed by Congress to prevent waste and abuse. Whatever their intent, Alexander says it took him three years to win approval to build a housing project for the elderly. "The housing industry needs a few programs that are consistent and stable," he says, "so we can learn how to use them."

Limited resources. Even so, there's only so much a more streamlined federal housing agency can accomplish working through local governments and nonprofits. Daniel Leibsohn, president of the Low Income Housing Fund in San Francisco, has provided loans for nearly 15,000 units of nonprofit low-income housing since 1984. "I think nonprofits could do more housing, but only up to a point with existing resources," he says. "I think it's a longer-term project of trying to build up nonprofits."

There are no magic fixes, but any solution involves more money. Leibsohn would provide more attractive subsidies in order to involve more private developers. They could receive support to build turnkey projects, for example, to be handed over to tenants or nonprofits to manage. Kathryn Wylde, who recently left her longtime position as president of the New York City Housing Partnership, which created and renovated 15,000 units in New York City, believes that the federal government has to play a continued role but that the agency must be fixed first. "The tax base of New York City can't begin to address the needs of the people here," Wylde says. "We have to have federal participation and federal funding for these needs."

BY PENNY LOEB WITH WARREN COHEN IN CHICAGO, EDWARD T. POUND, TIMOTHY M. ITO AND DANA COLEMAN

U.S. NEWS

Of contacts and confidence

Asking questions about billion-dollar deals

In 1994, officials at the Department of Housing and Urban Development launched an ambitious new program to sell off billions of dollars in troubled real-estate mortgages to private investors. The HUD-insured loans, on which borrowers had defaulted, were proving a drag on efforts to streamline the agency. The way the officials figured it, everybody would win. HUD would rid itself of unwanted baggage. Proceeds generated from the sales would be used against the deficit or for housing initiatives. And private investors would make a buck, reselling the mortgages at higher prices or foreclosing on deadbeats who hadn't made a mortgage payment in years.

In most ways the system has seemed to work as planned. Investors, with Wall Street firms taking the lead, eagerly

snapped up the troubled paper in 15 separate sales, the last one this past September. HUD removed 79,700 problem mortgages from its books, and the agency says it netted even more money than expected: \$1.3 billion for taxpayers.

Questions. The program has had a troubling underside, however. Based on a federal lawsuit filed by a top consultant at HUD and complaints from senior agency employees, the housing agency's inspector general has opened a criminal investigation into allegations that the \$11 billion mortgage-sale program may have been tainted by contracting fraud and instances of insider dealing. Now in its fifth month, the inquiry has resulted in the issuance of subpoenas and extensive interviews of senior HUD officials. People close to the matter say no conclusions have been reached about



ADVISER. C. Austin Fitts directed the Federal Housing Administration before going to work as a HUD adviser with partner Russell Davis. Some officials have raised questions about ties between HUD and her firm.

■ U.S. NEWS

whether laws were violated. But according to documents and these sources, the inquiry is focused on two questions:

■ Did certain Wall Street investment firms somehow gain an inside track to win loan packages? Most sales were conducted with sealed bids.

■ Did HUD officials break or bend procurement laws in awarding rich contracts to consulting firms retained to help manage the program?

At the center of the inquiry are two women who played key roles in developing the program. One is C. Austin Fitts, who served as federal housing commis-

small company to retain Hamilton. The firm, Williams, Adley & Co., paid Fitts's company \$6.6 million but denies it was forced to hire her firm.

Through her attorney, Dunlap denies pressuring Williams, Adley and says the firm itself proposed hiring Hamilton. The attorney also says that Dunlap never favored either Hamilton or Wall Street firms. In a statement, Dunlap, who resigned from HUD last month to take a job with a national housing organization, said: "Throughout my tenure at HUD, I acted in the best interests of the department."

Fitts, 45, a former Wall Street investment banker, says her firm was never

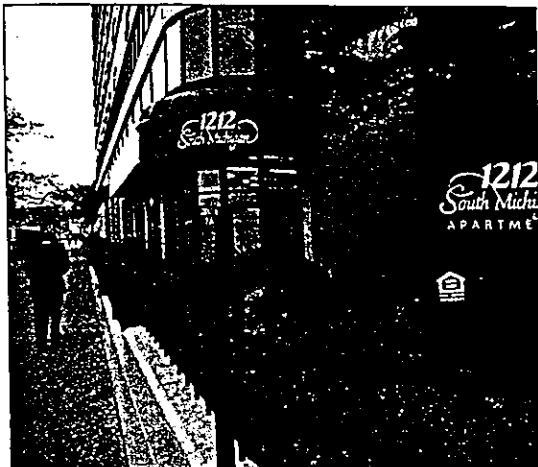
dals, Cisneros says he has started his own investigation of the FHA's procurement practices, including the "appropriateness" of past contract awards to Hamilton and to other program consultants. He says outside financial experts will conduct the review and determine what reforms are needed.

A good plan. The note-sale program was developed to address a growing problem. The agency has to pay claims to lenders when borrowers default on HUD-insured mortgages. By 1993, HUD owned mortgages on 2,400 multifamily housing projects and 90,000 single family homes. HUD officials say selling off the mortgages made sense because the agency was wasting valuable resources to service the loans.

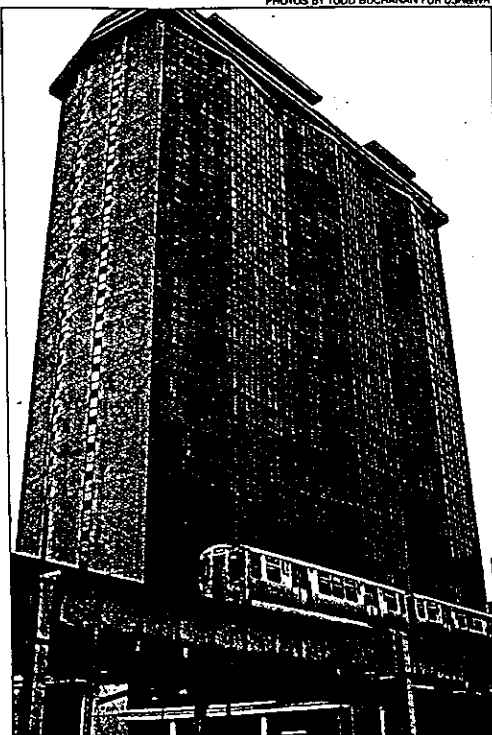
Clearly born of good impulses, the program was nevertheless a constant source of controversy. Inside HUD, senior employees began complaining more than a year ago that top agency managers were skirting procurement rules and paying excessive fees to Hamilton Securities. Top HUD officials apparently took no actions on the complaints. This past summer, there were more allegations—and they were much more sensational. A financial consultant named John Ervin, once one of HUD's top contractors and a competitor of Hamilton, filed a lawsuit in federal court charging widespread abuse in the

management of the note-sale program. Ervin's original and amended complaints are packed with allegations, some of which, he says, came from HUD employees.

Ervin's allegations, if true, are damning. He accuses HUD managers—specifically Helen Dunlap—of "contracting corruption and favoritism." Dunlap twisted procurement laws, Ervin says, to funnel millions of dollars in consulting business to Hamilton. Ervin says that HUD, in collusion with Hamilton, "stacked the deck against small investors," structuring the note sales so that the "big boys" on Wall Street would win most of the business. He cited as examples Goldman Sachs & Co., "a very large contributor" to the Democratic Party, and BlackRock Capital Fi-



ASSETS AND LIABILITIES. *The mortgage-sales program was born of a good impulse, to allow HUD to shed troubled loans like the ones on these buildings in Chicago while generating new revenue. The program has largely worked well, but questions have been raised about alleged insider dealings.*



sioner a few years back and whose financial advisory firm is paid \$868,000 a month by HUD to help the agency manage the program and advise the agency on other issues. The other is Helen Dunlap, an advocate for low-income housing from California who took a top job at HUD in the fall of 1993. She directed the note-sale program. The two became friends and were part of the "New Girls Network"—a name others gave to an informal group of officials and consultants that wielded a lot of clout at HUD.

Pressure? In the case of Dunlap, several agency employees allege that she improperly directed lucrative business to Fitts's company, the Hamilton Securities Group Inc. In one case, a senior HUD employee says, Dunlap and another agency official "pressured" a

shown favoritism by Dunlap or other HUD officials. She also says her company never steered any note-sale business to Wall Street firms.

Inspector General Susan Gaffney declined to discuss her inquiry. But *U.S. News* has learned that her investigators recently seized Dunlap's records at HUD, and Fitts's company was served with subpoenas last August for some 50,000 documents. They included thousands of electronic-mail communications between Hamilton, HUD officials and firms that bid on the mortgage sales.

HUD Secretary Henry Cisneros defends the note-sale program, which is run by the Federal Housing Administration. "I believe our policy of note sales," he says, "was the right one." However, mindful of the agency's history of scan-

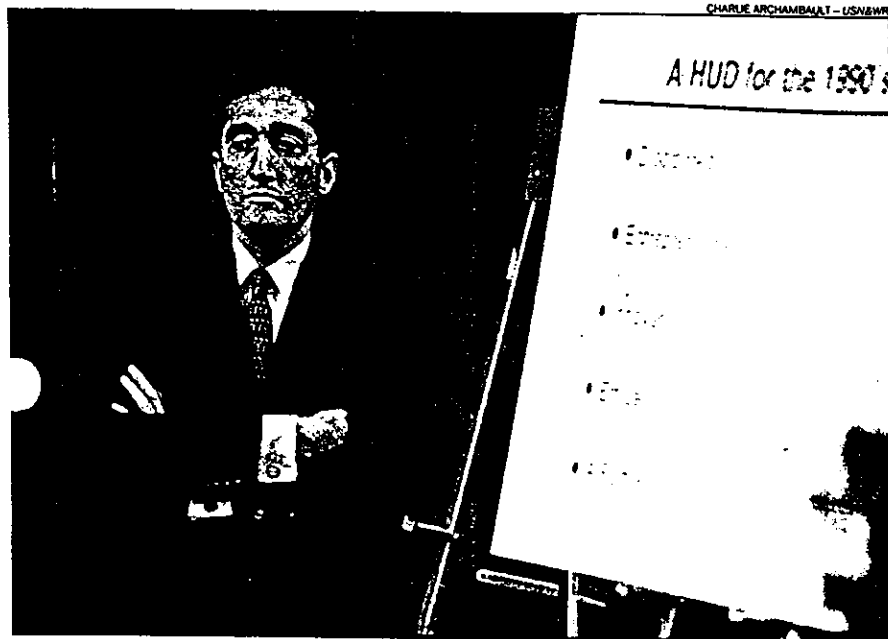
■ U.S. NEWS

nance LP, a respected financial powerhouse. Goldman and BlackRock deny any impropriety.

Ervin, who did not sue Hamilton, says he was "blackballed" at HUD after repeatedly complaining. Agency officials call Ervin "a disgruntled contractor" and say his allegations must be viewed with skepticism because his company, which managed HUD assets, lost out whenever mortgages were sold off.

Investigators are carefully tracking the allegations in Ervin's lawsuit and have

and had "access to confidential information" on the mortgage sales. Though she didn't identify the bidders, people familiar with the letter say she was referring to BlackRock Capital, among others. Burstein also cited a meeting at HUD in which, she wrote, Hamilton officials "discussed the marketing of assets in a portfolio in front of a representative" of BlackRock, "which was bidding on that particular portfolio." At one point, Burstein added, Hamilton's representative "suddenly spoke, laughing, 'We have to watch what we say; remember there's a bidder in the room.'"



THE SECRETARY. Henry Cisneros says he has worked hard to correct past abuses at the housing agency. The loan-sale program, he says, is just one example of innovation and produced big savings for the taxpayers.

questioned at least two companies that worked with Hamilton in developing the note-sale program. Both were asked about Hamilton's dealings with BlackRock Capital. One of the companies is Asset Strategies Group, a financial advisory firm that fell out with Hamilton over management differences last year.

"Going wrong." Asset Strategies has made its own complaints about improprieties in the mortgage-sales program. In September 1995, a company attorney, Karen Burstein, wrote to HUD complaining about shoddy work on loan packages and raising concerns about possible "manipulation" of the note-sale program. She warned that "something is, or is going, wrong."

In perhaps her most damaging charge, Burstein asserted that some bidders were working out of Hamilton's offices

Hamilton and BlackRock both deny any inside information ever was passed. Hamilton says BlackRock personnel worked out of its offices as a subcontractor helping structure an \$884 million note sale. During this period, which covered 1995 and part of this year, Hamilton also was structuring other note sales. HUD approved the arrangement.

BlackRock Capital did not bid on the \$884 million deal it helped design. However, one of the winners was an investment fund managed by Goldman, Sachs, which had partnered with BlackRock in successfully bidding on a prior note sale. Both investment firms say they acted properly at all times. Often partnering with others, BlackRock has won about one fourth of the business auctioned thus far, or \$1.6 billion.

HUD officials insist that all bidders have a fair chance at winning. As adviser to HUD on the note-sales program, however, Hamilton Securities was particularly sensitive to the expectations of Wall Street. In a confidential document submitted to HUD three years ago, the company said: "A good financial advisor can take advantage of Wall Street's desire to get a competitive advantage." The document, obtained by *U.S. News*, further explained Hamilton's philosophy: "Wall Street and institutional investors will provide a substantial amount of advice for free" in exchange for increasing "their understanding of a bidding situation." The company added that "their reward is early information and a possible inside track on future transactions. Properly done, there is nothing wrong with this process."

Friends. Fitts's company says it was not suggesting giving an edge to Wall Street firms over other bidders. Hamilton said it provided an equal amount of information to all bidders.

Of particular interest to investigators is Fitts's relationship with Helen Dunlap, the former HUD official. Documents and interviews with senior HUD employees indicate that Dunlap went to bat for Fitts more than once. In one case, the employees say, Dunlap influenced the results of a HUD selection process for recommending outside firms to be the agency's new financial advisers in 1996. According to this account, Hamilton finished out of the "competitive range" in the panel's evaluation. Dunlap intervened, the employees say, urging a new evaluation. The next time around, Hamilton finished first and eventually won a \$20 million contract. HUD officials acknowledge the company may have finished lower in the initial scoring but insist it was still competitive and fully qualified. Since Hamilton was awarded its first HUD contract in 1993, it has won \$47 million in agency-related business.

Fitts says she will ultimately be vindicated. Just a few days after her company got a subpoena from the inspector general last August, Fitts sent an E-mail message to a slew of HUD officials expressing her concern about the "frustration and meanness in the HUD building." She also warned them about the "hippo"—her shorthand for bad news—and urged everyone to stick together. It would be intolerable, she wrote, "if the hippo were to land on our heads this fall—as it surely will—and we were to turn on each other." ■

BY EDWARD T. POUND AND TIMOTHY M. ITO

unds were legal

President Clinton said, "I am absolutely certain that we believed we were acting within the letter of the law," regarding the raising by him and Vice President Al Gore. A12

coming under Justice Department review, the president and vice president have taken another tack publicly.

Both have been at pains to be conducting business as usual. Mr. Clinton addressing the United Nations yesterday and Mr. Gore in Moscow for trade meet-

ings, as the Gore adviser said, "an important audience right now for net Reno."

Justice Department spokesman on Marlin declined comment. He acknowledges that questioning Miss Reno's legal judgment is backfire, forcing her or even putting her into calling for the independent counsels. She is un-

RENO, page A12

Legal doubts raised over HUD contracts

\$20 million deal went to Clinton donor

By George Archibald
THE WASHINGTON TIMES

The Department of Housing and Urban Development wasted hundreds of millions of dollars in questionable contracts awarded since 1993, including one to a major donor to the Clinton re-election campaign, according to a draft report by the agency's inspector general.

The IG report questions the legality of a \$20 million contract given to Big Six accounting firm Ernst & Young LLP. A month before the contract was renewed, the firm gave \$132,000 to President Clinton's 1996 election campaign.

"Departmental managers have for all practical purposes abdicated their procurement- and contract-oversight responsibilities with costly consequences," the re-

port says.

The report questions the legality of a financial-adviser contract awarded to Ernst & Young by HUD's Government National Mortgage Association (GNMA) over the objections of career contracting officers.

Less than a month after Ernst & Young gave the Clinton campaign \$132,000, Deputy HUD Secretary Dwight P. Robinson ordered the firm's contract renewed in October for three years, according to documents turned over to the Senate Governmental Affairs Committee for its probe of campaign fund raising.

The contract was one of 39 targeted for review by the IG. The others include awards to Lockheed

see HUD, page A12

ar, new attitude



by Kevin T. Gilbert/The Washington Times

Principal Gary Washington
day of school in the District.



Facing questions:
Seventh-grader Latisha Jones is ready with an answer yesterday.

and fewer disruptions.

The change in attitude comes after Gen. Becton told 8,000 teachers, principals and other school staffers in August that their jobs are now tied to academic performance.

Among the most drastic changes the retired Army officer will make

Gerber strained by hoax on Internet

Thousands seek \$500 settlement

By Lorraine Woellert
THE WASHINGTON TIMES

Nearly every American mom at some point has navigated a spoonful of Gerber baby food into her child's mouth. It's a good bet few ever thought that mundane act of child rearing could earn them \$500.

Well, it can't.

Gerber Products Co. has joined the annals of urban myth with an official-looking memo that promises parents of young children a \$500 U.S. savings bond as part of a class-action settlement against the baby-food maker. The memo is a hoax, but since January it's been circulated over the Internet, through faxes, and among PTAs and church groups across the country.

It surfaced most recently last week at a meeting of...

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ew principal told seventh-
rs gathered in the Northeast

Washington Times 9/24/97

RENO

From page A1

der intense Republican pressure to seek the appointments.

Most of those who criticized Miss Reno spoke on the condition of anonymity.

But they all echoed an argument first laid out Sunday by former Clinton Deputy Attorney General Philip Heymann, who wrote that "Attorney General Janet Reno has painted herself into a corner."

She did this, Mr. Heymann wrote in the New York Times, by accepting the argument that the funds raised by Mr. Gore were designated for general party-building activities, not to elect specific candidates.

When she wrote to leaders of both parties in Congress this year to reject seeking an independent counsel, Miss Reno said the law applied only to the latter kind of funds, known as "hard money," not the former, known as "soft money."

It has since come to light that in Mr. Gore's case, and perhaps in the president's, contributions raised by telephone ended up in hard-money accounts used to help elect people.

The revelations mean Miss Reno may be forced to recommend an independent counsel.

"She does not need to be in that box," a frustrated White House aide said. He called the attorney general's focus on hard and soft money "the most significant mistake that she made" in the case.

Republicans and others say she has no choice in the matter now, the Gore adviser said. "But it's ir-

"In the more than 100 years since its enactment... the law appears to have been neither specifically construed by any court nor applied in any prosecution to cover one who solicits a campaign contribution from a federal building by letter or telephone to persons who are not located themselves in a federal building," the nonpartisan Congressional Research Service said in an Aug. 12 report.

Other documents, including the Senate's ethics manual, cite a 1908 Supreme Court opinion that the "solicitation" takes place where a letter — or, in modern days, a phone call — is received.

Mr. Gore has acknowledged making phone calls from his offices; the president has said he may have but cannot recall. Both men have said they are confident they did nothing wrong, a position Mr. Clinton strongly reiterated yesterday.

The attorney general this month initiated a 30-day inquiry into Mr. Gore's activities, the first of several steps that could lead to an independent counsel.

In the vice president's case, it is widely anticipated that when the 30 days end in early October, the attorney general will take the next step: a formal, 90-day review to determine whether she should recommend that a panel of federal judges choose an outside counsel.

"It takes an awful long time to review all of these technicalities, so I wouldn't be surprised to see that," White House counselor Paul Begala said in a weekend television interview.

In a way, White House aides acknowledge, more is at stake for Mr. Gore, to whom ethical trials are

HUD

From page A1

Martin, Price Waterhouse and Chase Manhattan. Those companies, as well as Ernst & Young, contributed to both political parties.

HUD also hindered competition for financial-adviser services and "circumvented proper contracting procedures" to expand the Ernst & Young contract through an inter-agency agreement between the GNMA and the Federal Housing Administration, says the IG report, circulated for comment by HUD managers.

David Egner, a spokesman for HUD Secretary Andrew M. Cuomo, said the department responded to the IG report, but he would not elaborate. "Because the draft audit has not been finalized, it would be inappropriate and premature to release our response at this time," he said.

Housing Affairs Letter, a trade publication, reported Aug. 29 that department officials and lawyers were "combing the draft for mistakes." A HUD source told the newsletter, "They're really scrambling to defuse the allegations."

The IG accuses HUD of wasting millions of dollars by failing to au-

"Some of these contracts awaiting audit have been completed since 1989."

—HUD report

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Mr. Clinton's and Mr. Gore's defenders insist that it makes no difference what kind of money they raised in telephone solicitations.

The 114-year-old law in question, they argue, was enacted to protect federal employees from being pressured by supervisors into contributing to the party in power. And they say it does not apply when the person being solicited is off federal property, as was the case with the businessmen Mr. Gore solicited.

fairly new.

One official, with Mr. Gore's presidential aspirations in mind, recalled how Mr. Clinton faced charges of misconduct during the 1992 New Hampshire primaries, charges that have dogged him ever since.

The question now is: Can Mr. Gore handle adversity? "That's something people are going to look to for Gore," he said.

• Jerry Seper contributed to this report.



Photo by Kenneth Lamber/The Washington Times

encounter Feb. 12 was consensual, arrives for the first day of his trial.

dit company charges on half the 9,600 contracts it has awarded on a "cost-plus basis" since 1992.

"There are currently 129 contracts with costs of over \$900 million that have been completed but audits have not been performed or requested. Some of these contracts awaiting audit have been completed since 1989," the report says.

Susan Gaffney, the IG, recently survived an ouster attempt by Cuomo loyalists, said to be angry over leaks of confidential reports containing criticisms of waste, fraud and abuse at HUD.

The latest IG report, obtained from a source not associated with the IG's office, says HUD is too dependent on a contract with Lockheed Martin to operate the department's computer and data-storage operations.

The department has sought no other avenue, though Lockheed Martin's initial cost of \$525.9 million when the contract was awarded in November 1990 has nearly doubled and "could exceed \$1 billion by the end of the contract life" in six years.

"As of June 1, 1997, there have been 65 modifications to the contract, of which 41 are funding modifications," the report says.

When Mr. Cuomo led HUD's community planning and development division in 1994 and 1995, two consultant contracts worth \$280,029 were improperly awarded to Frank Destefano, a former department employee, auditors said.

Mr. Destefano was retained without competition to analyze legislative proposals affecting HUD and draft legislation for submission to Congress, which the IG called "inherently governmental functions that should not be performed by a contractor."

In its response, the department said that it sought competition for the contracts and that federal guidelines allow the hiring of contractors to help draft government documents.



Outlook

UPDATE



HUD has second thoughts on loan adviser

A year ago, C. Austin Fitts could do no wrong at the Department of Housing and Urban Development. As a contractor to the housing agency, Fitts and her firm, the Hamilton Securities Group, had designed and supervised the running of a complex mortgage-sales program aimed at helping HUD get rid of billions of dollars in bad loans on its books. HUD officials called her a "visionary" and boasted that she had saved taxpayers \$1.3 billion on 15 separate sales.

But last week, the goodwill stopped. Amid a Justice Department criminal investigation into the note sales and other matters, HUD Secretary Andrew Cuomo terminated the firm's \$868,000-a-month contract as a financial adviser. In a two-page letter, HUD demanded that Hamilton pay the agency \$3.9 million. HUD said it discovered the firm had knowingly provided "erroneous instructions" to a computer program that determined the winners in the mortgage sales--a move that lowered the revenues the auctions might otherwise have generated. According to the letter, Hamilton's "erroneous use of the [computer] model resulted in the selection of bidders that were not in accordance" with agreed-upon methods. Hamilton refused to comment on specific charges but said in a statement that it was proud of the loan-sale program's success and that the firm had dramatically reduced HUD's backlog of troubled mortgages. Hamilton also disputed any characterization that its performance had not met the highest professional standards.

The first public hint of trouble with the program came in a *U.S. News* investigation last fall ("Of Contacts and Confidence," Nov. 11, 1996) that detailed problems with the note-selling process. In particular, the article included allegations of irregular contracting involving Hamilton and aired accusations that Fitts may have illicitly steered some of the lucrative note-sale business to certain favored Wall Street firms like BlackRock Capital Finance and Goldman Sachs. All parties denied any wrongdoing and steadfastly defended their activities.

HUD observers say the agency may have moved against Hamilton to demonstrate it was tackling the problem prior to the completion of the Justice probe, which is expected soon. Part of that inquiry focuses on the involvement of HUD officials in the note sales and their influence on contract awards. The agency is also being sued by another contractor, John Ervin, who says HUD cut off the contracts of his firm in retaliation for his complaints about these issues.--*Timothy M. Ito*

The Washington Times

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HUD Secretary Andrew Cuomo

Cuomo dumps financial adviser

By George Archibald
THE WASHINGTON TIMES

Housing Secretary Andrew M. Cuomo fired his department's chief financial advisory contractor Friday and ordered a fresh top-level review of bid-rigging charges that have tainted multibillion-dollar federal mortgage sales.

The actions sent shock waves through contracting offices at the U.S. Department of Housing and Urban Development, where top officials are at the center of a 17-month corruption probe of possible bid-rigging in HUD note sales organized by Hamilton Securities

Orders probe of bid practices

Group.
In firing Hamilton, HUD accused its chief financial advisory firm — and indirectly HUD officials — of covering up erroneous instructions for a computer model used to determine winners in more than a dozen sales of nearly 100,000 federally backed mortgages worth more than \$8 billion since 1995.

Mr. Cuomo ordered suspension of all work on contracts involving Hamilton until a "fresh review" of

corruption allegations against the firm could be conducted by his General Counsel's Office, HUD sources told The Washington Times yesterday.

The suspension includes contract bids due today for new financial advisory work solicited Oct. 10 on a nationwide rent-reduction project involving federally insured properties, department sources said.

HUD also ordered Hamilton, an investment banking firm, to pay

the government \$3.88 million losses already determined cause of the erroneous computer instructions. The review directed by Mr. Cuomo "could run into millions of dollars of additional claims," a department official said.

HUD's termination letter to Hamilton, obtained by The Times, stated that Nicolas P. Retsis, head of the Federal Housing Administration, and Kathryn R. PHA's comptroller, had known documents detailing the erroneous instructions since last December.

Hamilton nonetheless retains

see CUOMO, page A10

REDSKINS LOSE TOUCH IN MEMPHIS



Traveling Clinton pushes trade bill

Daley optimistic about 'fast track'

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CUOMO

From page A1

its \$20.8 million contract as FHAs
chief financial adviser, renewed in
April 1996, and was currently
overseeing the top-priority HUD
project to force down inflated
apartment rents at federally in-
sured properties. The project was
mandated by Congress.

Mr. Retsinas and Miss Rock de-
clined to respond to inquiries from
The Times. A HUD official, speak-
ing on condition of anonymity, said
Mr. Retsinas "was completely on
board and concurred" with the ac-
tion to terminate Hamilton, a
Washington-based firm.

Carol F. Steinbach, a Hamilton
official, told The Times the firm
would not respond to any inquiries
or make any comment while the
criminal probe was under way.

HUD's actions followed inquiry-
ies by The Times concerning limi-
tation of the Oct. 10 bid solicitation
from FHA on the rent-reduction
project. Bids were sent only to
Hamilton and three other firms
that previously competed success-
fully for financial advisory con-
tracts. Those firms also are in-
volved in the ongoing criminal
probe.

"The ground was moving all
week," said one HUD official about
top-level activity at HUD following
the newspaper's inquiries.
Another official portrayed
FHA's actions on the rent-re-
duction bid solicitation as a "rogue
operation" in defiance of Mr.
Cuomo's orders to clean up con-
tracting abuses possibly including
Hamilton and other firms associ-
ated with sale and restructuring
tens of thousands of troubled HUD
mortgages.

Sources said Howard B. Glaser,
HUD's acting general counsel, dis-
patched officials from his office
late last week to review FHA doc-
uments related to Hamilton's
work.

Two memorandums were dis-
covered that detailed Hamilton's
erroneous instructions to Ham-
Bell Labs, a subcontractor to Ham-
ilton, for an "optimization model" to
analyze note sale bids from Wall
Street firms, the sources said.

Addressing the Mortgage Bankers Association,
Mr. Cuomo noted: "In the past, HUD was almost
a joke. It was inefficient and ineffective. Now we
have a blank slate to reinvent it. There will be
no tolerance for waste, fraud, and abuse."

Mr. Glaser declined to comment
yesterday. But another HUD
source said an angry Mr. Cuomo
gave his general counsel direct in-
structions to "find out what's going
on and whether there's anything to
these allegations that keep appear-
ing."

Another source said the HUD
secretary and his senior advisers
were frustrated by a constant high-
powered damage-control opera-
tion by Hamilton and the contrac-
tor's supporters. C. Austin Fitts,
FHA commissioner under Jack F.
Kemp, HUD secretary during the
Bush administration. Mr. Kemp
forced Miss Fitts to resign for un-
explained reasons, sources said.

Miss Fitts, a former Wall Street
investment banker and director of
Dillon, Read & Co., soon came back
as a top contractor to HUD, where
she has since orchestrated many
multibillion-dollar mortgage and
security sales and restructuring
programs for the department in
the private sector. Hamilton was
being paid \$868,417 per month un-
der its main financial advisory
contract just terminated.

"They always say, 'Where
there's smoke there's fire,' and
there's been a lot of smoke around
the Hamilton situation but nothing
provable," said a HUD source who
asked not to be named.

"We've been looking for the fire.
We think this is the fire."
Mr. Cuomo's actions are said to
be a signal that he wants to strike
a new relationship with HUD's in-
spectors general, Susan Gaffney,
with whom the secretary has had
a strained relationship. Miss Gaff-
ney and the U.S. Attorney's Office
for the District of Columbia are
jointly conducting the probe of
corruption at HUD, which in-

At the request of the U.S. Attor-
ney's Office for the District of Co-
lumbia, much of the legal discov-
ery in the Ervin lawsuit has been
stayed by U.S. District Judge Wil-
liam Bryant because the criminal
probe is tracking the main allega-
tions of the civil lawsuit.

"The criminal investigation is
ongoing and concerns an ex-
tremely complex set of facts,"
wrote J. Ramsey Johnson, princi-
pal assistant U.S. attorney, in his
latest request Oct. 3 for another
60-day stay in the Ervin case.

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ican votes. "Why didn't you tell us you had these concerns before?" an annoyed Mr. Clinton asked, according to congressional and White House accounts. "We worked hard on this; we got more [protections] for fast track than anyone else did before."

Mr. Becerra, who was being pressed by others in the caucus to wring further concessions out of the administration, replied that the legislation was flawed. "I was getting [the administration] to address past transgressions" from Nafta, Mr. Becerra says. He voted against fast track, and his conversation with the president ended with both of them angry. Yesterday, 10 of the lawmakers wrote Mr. Clinton telling him they would oppose fast track.

If Mr. Clinton chalks up another victory, he will have won because he worked doggedly to piece together an oddball, bipartisan coalition. Three weeks ago, as his aides played hearts on an Air Force One flight home from South America, Mr. Clinton was on the plane's phone, twisting arms. He tracked down and lobbied Rep. Chet Edwards, a Texas Democrat, who was at a charity fund-raiser in Waco.

And, as Rep. Tom Allen, a Maine Democrat, watched the final out in a World Series game, he also got a late-night presidential call. He discussed the game with Mr. Clinton, and the president talked about his trip, before making his pitch: "Is there any way I can persuade you to support fast track?" Mr. Allen will vote against fast track, but says: "I sympathize with the president's challenge."

—Kemba Dunham
contributed to this article.

HUD Halts Program To Auction Mortgages As It Seeks Adviser

Dow Jones Newswires

WASHINGTON — The Department of Housing and Urban Development suspended its two-year, multibillion-dollar mortgage auction program until it can select a new financial adviser for the sales.

HUD stopped the program last month when the agency dismissed its adviser, Washington-based Hamilton Securities Inc. It demanded Hamilton return about \$3.9 million following errors in handling bids in two 1996 auctions. Hamilton took with it the technical capacity — including

personnel and access to technology — to conduct the auctions.

Hamilton had described its mistakes in a report to Federal Housing Administration in December 1996, but no action was taken. The official overseeing Hamilton's contract said she wasn't made aware of the errors until 10 months later. Hamilton said it disputes "any characterizations that suggest our performance hasn't been up to the highest standards of professional conduct. We look forward to . . . an amicable resolution of our differences."

HUD is investigating the matter, officials said. The U.S. attorney and HUD's inspector general are also conducting a criminal investigation into circumstances around the sales and other contracting matters.

The auctions have sold off about 80% of \$11 billion or so in defaulted mortgages.

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HUD ignored charges of bid-rigging

By George Archibald
THE WASHINGTON TIMES

Top managers at the U.S. Department of Housing and Urban Development ignored corruption charges for two years against their chief financial advisory contractor.

The contractor, Hamilton Securities Group, a local investment company, was fired Friday by HUD Secretary Andrew M. Cuomo.

Ironically, Mr. Cuomo asked the Federal Housing Administration two years ago to respond to charges that Hamilton illegally gave a Wall Street bidder confidential inside information before HUD sold tens of thousands of troubled mortgages.

FHA ignored the complaint, and Hamilton went on to taint billions of dollars worth of HUD note sales by misusing a computerized process to select winners, according to agency documents.

Mr. Cuomo now is going to move against HUD officials who protected Hamilton and prolonged corruption that has embarrassed him, agency officials told The Washington Times.

He is angry that his own promised program to clean out waste, fraud and abuse at HUD has been clouded by a criminal probe of note-sale corruption that might have been prevented, officials said. The probe is being conducted by the department's inspector general and the Justice Department.

Firing Hamilton sends the message that "we're cracking down outside the agency," an official said, "but we're also sending the message that we're cracking down inside the agency. This is going to shake things up."

Two top officials with immediate worries are Nicolas P. Retsinas, assistant secretary for housing and FHA commissioner, and Kathryn Rock, FHA's comptroller, who ignored complaints against Hamilton sent to them by Mr. Cuomo, documents indicate.

A letter received by Mr. Cuomo in September 1995 charged Hamilton with giving confidential information to a bidding company and professional carelessness before a \$523 million note sale.

"At a meeting at HUD, [Hamilton] discussed the marketing of assets in a portfolio, in front of a representative of a firm which was bidding on that particular portfolio," wrote Manhattan lawyer Karen S. Burstein, a former Democratic candidate for attorney general of New York.

"In the meeting, the prime contractor's officer suddenly spoke, laughing. 'We have to watch what we say; remember there's a bidder in the room,'" she wrote. Miss Burstein was representing a subcontractor to Hamilton that was unhappy with Hamilton's actions.

A meeting participant told The Times that the bidder was BlackRock Financial Capital, a prominent Wall Street firm that ended up winning \$395 million worth of troubled mortgages in HUD's first national sale of defaulted single-family properties in November 1995.

According to HUD sources, BlackRock submitted a "pooled bid" with three partners for 12,981 defaulted mortgages. The bid matched Hamilton's winning sale price for those properties, calculated by a computerized "optimization model" that HUD now says was known by Hamilton to be "erroneous."

Four months later, in March 1996, a partnership of BlackRock and Berkeley Federal Savings Bank, a unit of Ocwen Financial Corp., won all of HUD's defaulted single-family-home loans in the agency's second national sale, buying 16,539 properties for \$633.8 million.

Miss Burstein said Hamilton had "developed a concept called 'teaming partner' which allows it to represent to HUD the availability of (in one case) 20 firms for different projects. Some of these 'teaming partners' are broker/dealers who will bid on portfolios being analyzed by the lead contractor. Such dealers have staff at Hamilton with access to confidential information."

During the period of both single-family sales, BlackRock served as Hamilton's subcontractor in organizing HUD's \$883.6 million "partially assisted" multifamily note sale, which took place in June 1996.

As subcontractor, BlackRock officials were given access to a confidential "servicing tape" containing payment history of all HUD-backed mortgages and other confidential information for borrowers and lenders, sources said. The computer tape was prepared for HUD by Electronic Data Systems.

BlackRock did not respond to inquiries yesterday.

Miss Burstein, who had worked for Mr. Cuomo's father, former Democratic Gov. Mario Cuomo of New York, said in her five-page letter that FHA contracting officials had refused to act on the problems she outlined and the younger Mr. Cuomo "promised that Nic [Retsinas] would see the letter."

Jon J. Cowan, HUD's chief of staff, said Mr. Cuomo received Miss Burstein's letter when he was assistant

secretary for community planning and development. Mr. Cuomo remembers immediately referring the letter for action to Mr. Retsinas, the assistant secretary for housing, who said he asked Miss Rock to look into the matter, Mr. Cowan said.

HUD has not responded to a request by The Times, under the Freedom of Information Act, for records of HUD's actions or response to Miss Burstein's charges. Mr. Retsinas and Miss Rock did not respond to inquiries.

The inspector general's office denied The Times' request. "The records we located that are responsive to your request are part of an ongoing law enforcement investigation and cannot be released at this time," wrote Darlene D. Hall of the HUD IG's staff.

A Hamilton official told The Times the firm would not respond to inquiries because of the criminal probe. However, in a statement yesterday to the Associated Press, the firm said it was "extremely proud of its work" for HUD and hoped to reach an amicable resolution.

The firm said it has given taxpayers an "extraordinary return" of billions of dollars through its work in the note-sale program. HUD has demanded immediate payment of \$3.9 million for losses caused by Hamilton and said the government may seek "additional millions of dollars" in further claims.

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In a release issued Monday, Hamilton defended its work for HUD, arguing that it has given taxpayers an "extraordinary return" of billions of dollars through its work in the auction program.

HUD said it is reviewing all work performed by Hamilton and may make additional claims.

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HUD told last year of rigged loan sales

By George Archibald
THE WASHINGTON TIMES

Top officials at the Department of Housing and Urban Development knew a year ago that its chief financial advisory contractor altered bids, changing the winners and losers in multibillion-dollar sales of troubled mortgages.

HUD has just fired Hamilton Securities Group, a local investment firm used to carry out the agency's national sales of defaulted housing properties.

But HUD's top officials at the Federal Housing Administration knew last October that the contractor secretly changed bid numbers because of a serious flaw in a computer program used to decide winners and losers in the auctions, according to sources involved.

Other contractors working with Hamilton discovered a discrepancy in two 1995 and 1996 sales of more than 300 defaulted apartment properties worth \$1.5 billion, the sources said.

The discovery occurred Oct. 24, 1996, at a planning meeting for the sale of an additional 107 troubled apartment complexes worth \$873 million, said a former Hamilton employee who asked not to be named.

"Over the next several days, it became apparent that there was a problem," the employee said. "It was not until Dec. 5 that the problem was brought to the attention of HUD. Hamilton sat on this for six weeks."

The news was delivered to FHA Comptroller Kathryn M. Rock as Hamilton was putting finishing touches on HUD's \$873 million Multifamily Nonperforming Midwest Mortgage Sale. Miss Rock previously worked for GE Capital, the investment firm that was a principal winner in that sale.

Miss Rock and Nicolas P. Retsinas, HUD's assistant secretary for housing and FHA commissioner, had the power to end Hamilton's \$20 million contract when they were informed of the problems in December 1996, department sources said.

Both officials declined to respond to inquiries yesterday. The department issued a brief statement in Mr.

Retsinas' name saying Hamilton was fired because "at this time it was appropriate to recommend termination of the contract." HUD cited "past performance errors by Hamilton," among other things.

Charges of bid-rigging in HUD's 19 sales of \$11 billion worth of defaulted mortgages, started in 1994, are part of an ongoing criminal investigation by HUD's inspector general and the U.S. Attorney's Office in the District of Columbia.

Hamilton has been at the center of the probe but continued receiving \$868,417 monthly contract payments until The Washington Times raised questions this month about the arrangement.

Miss Rock and Mr. Retsinas received a detailed report Dec. 20 on Hamilton's errors in the bidding process and the firm's actions to alter bid numbers in deciding the sales' winners and losers.

The report was cited last week in Hamilton's termination letter from Annette Hancock, a HUD contracting official, who wrote she "was apprised for the first time" of the document Oct. 14.

The report is Hamilton's explanation of a computer error in its analysis of bids from Wall Street firms and other potential buyers of defaulted HUD properties. Hamilton's analysis, done by Lucent/ Bell Labs, decided the winning bids.

After HUD's March 1995 Southeast sale, in which 177 apartment complexes worth \$907 million were awarded to Allied Capital, GE Capital and 10 other bidders, "Hamilton recommended and HUD approved that bidders would have the option to set a floor in future multifamily sales," the report stated.

By doing this, agency officials hoped a company would bid more for a series of assets if it was guaranteed that any winning bid would be worth at least the floor amount, or no properties would be awarded. Therefore, bidders would not be forced to take fewer assets than they wanted.

Bid packages sent out for HUD's \$622.3 million "west-of-the-Mississippi" sale of 152 apartment properties in September 1995 made "clear that the floor is to be expressed in terms of unpaid principal balance (UPB)," the report noted in explaining Hamilton's computer error.

However, Hamilton officials told their computer technicians at Lucent/Bell Labs that the floor should be expressed "in terms of minimum revenue, that is the price the bidder is offering to pay."

To compensate for the error, the report says an unnamed Hamilton official came up with a mathematical formula to change the bid numbers before the computer picked the winners and losers.

"They summed the UPB on all assets for which a floor bidder offered to purchase," the Hamilton employee said. "Then second, they summed the revenue on all assets for which a floor bidder offered to purchase. Then they divided the total revenue by the total UPB, arriving at an average percentage offered. Then they finally multiplied

the bidder's floor by the average percentage offer, arriving at the prorated revenue floor."

The altered bid numbers changed the winners and losers in HUD's \$622 million "West-of-Mississippi" sale, for which bids were submitted Sept. 18 and 19, 1995, and \$847 million "North-Central" sale on Aug. 5 and 6, 1996, the Hamilton employee said.

Bidders did not know their numbers were changed, said Wes Edens, manager of BlackRock Capital Financial, a winner of tens of thousands of defaulted properties auctioned in the HUD sales.

"We submitted bids on a clean disk; they could only be changed electronically," Mr. Edens said.

But the Hamilton employee said bidders also submitted their bid amounts on cards. The cards were used to change the bid numbers before they were fed into Hamilton's Lucent/Bell computer, he said.

HUD also auctioned 158 apartment complexes worth \$884 million in a "partially assisted" sale in June 1996 and another 107 properties worth \$873 million in the Midwest sale last December, after the inconsistency between Hamilton's bid instruction and computer program were discovered. GE Capital was a major buyer in both sales.

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HUD orders fired firm to surrender documents

Hamilton may resist because of bid-rig probes

By George Archibald
THE WASHINGTON TIMES

The Department of Housing and Urban Development has ordered a fired financial advisory firm to turn over bids and sale records for multibillion-dollar mortgage auctions being probed for bid-rigging.

Hamilton Securities Group may resist turning over the records because of legal complications in a criminal probe and the firm's defense in a civil lawsuit charging corruption, said a Hamilton employee terminated this week with about a third of the HUD contractor's 35-member workforce.

Seven more employees are expected to be laid off by next week, the employee said, as Hamilton struggles to survive after losing its \$868,417 monthly contract with HUD.

Leslie H. Lepow of Jenner & Block, Hamilton's lawyer, did not respond to inquiries about HUD's demand that the firm immediately turn over all submitted bids and other records of winners and losers in more than 19 HUD mortgage sales brought into question by the bid-rigging charges.

Hamilton was fired last Friday for "errors" in government auctions of more than \$9 billion worth of federally insured loans on 100,000 houses and apartment complexes nationwide. Hamilton organized and conducted the auctions as a HUD contractor.

HUD's inspector general and the U.S. attorney in the District of Columbia are conducting a criminal probe of charges that the auctions were rigged to benefit a few Wall Street firms.

In a report last December to Nicolas P. Retsinas, head of the Federal Housing Administration, Hamilton acknowledged altering bids and changing winners in several multibillion-dollar sales because of errors in the firm's computer analysis of bid sub-

missions.

Mr. Retsinas did not act on the report until its discovery last week by other top HUD officials, leading to Hamilton's firing. Mr. Retsinas has refused to be interviewed.

Carol F. Steinbach, a Hamilton official, also refused comment yesterday.

Jenner & Block's representation of Hamilton has complicated President Clinton's nomination of Gail Laster as HUD's general counsel, according to Senate sources, because Mrs. Laster is married to the firm's managing partner, Donald B. Verrilli Jr.

As HUD's chief lawyer, Mrs. Laster would be barred from participating in legal issues involving HUD and Hamilton as long as her husband's firm represents Hamilton, administration sources said yesterday.

Corruption charges swirling around HUD and Hamilton are the department's most pressing legal matters.

Howard B. Glaser, HUD's acting general counsel, has been heading the department's legal work on the disputed loan sales while Mrs. Laster awaits Senate confirmation. Mr. Glaser would continue that work as Mrs. Laster's deputy general counsel, shielding her and the department from any conflict of interest, the official said.

Chester Kamin, chief lawyer for Jenner & Block's litigation unit, said yesterday the firm will "vigorously represent" Hamilton and recuse or screen Mr. Vermilli from any actions "adverse to the spouse's . . . institution." He said Mrs. Laster's husband has done no work for Hamilton and "will not be involved in any way."

Robert Pincus, president of Franklin National Bank, Hamilton's banker, yesterday denied reports by laid-off employees that Hamilton was closing.

"They have other work and are looking for other sources of revenue," the bank president said after a meeting yesterday with Hamilton's directors.



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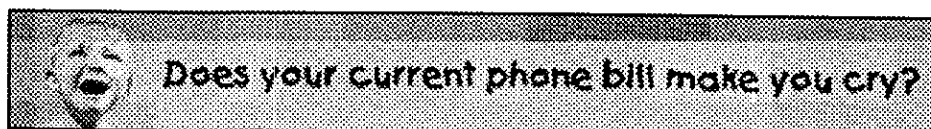
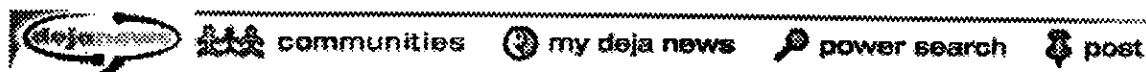
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The Washington Times

November 10, 1997

Official at HUD removed records

By George Archibald

A key official at the U.S. Department of Housing and Urban Development was caught improperly removing records involved in a criminal probe of possible bid-rigging in multibillion-dollar mortgage auctions, the department has confirmed.

Audrey Hinton, a HUD contracting officer with close ties to a fired financial advisory firm at the center of the corruption probe, was seen removing boxes of records from her office Oct. 21 -- the day The Washington Times disclosed that HUD had fired Hamilton Securities Advisory Services.

The firm was fired for computer errors that led to bid altering, which changed winners and losers in tainted note sales totaling \$9 billion since 1994.

According to court documents, a HUD employee anonymously reported the document removal, as it was under way, to Bethesda-based Ervin & Associates, a former HUD contractor who has sued the department for corruption.

John J. Ervin, the firm's owner, passed on the whistleblower's tip to HUD Inspector General Susan Gaffney and Howard B. Glaser, the department's acting general counsel, who swung into action to prevent further document dumping, officials said.

"All of our anonymous sources [in the department] have been extremely accurate," Mr. Ervin said yesterday.

Miss Hinton admitted to investigators that she removed documents but minimized their importance, said a HUD source close to the probe. "She said, 'Oh yes, I was just cleaning out my old files; all the documents were 20 years old. They had nothing to do with the note sales.'"

But in a subsequent interview, the source said, Miss Hinton acknowledged she threw out things "associated with the note sales but

she did it according to procedures. She said the note sales are over, so why keep the files?"

In a telephone interview Friday, Miss Hinton told The Times: "That's not true. That is not a fact."

Asked to give her version, Miss Hinton said, "I choose not to speak with you about this," and hung up the phone.

Albert B. Sullivan, Miss Hinton's supervisor at the Federal Housing Administration's asset disposition management office, also refused to comment.

Officials said Miss Hinton had been away from the department for six months. In May, HUD detailed her to the Enterprise Foundation of Columbia, Md., a nonprofit neighborhood housing group that receives HUD grants. She was seen carting boxes of documents out of her office during her first day back at the department, the officials said.

"It happened the day the [Times] story came out about Hamilton and the bid-rigging. Who did she talk to?" asked a source close to the investigation. "It doesn't hold water to say, 'I was cleaning out my desk.'"

Mr. Ervin's lawsuit accuses Hamilton of conspiring with Miss Hinton's former boss, Helen Dunlap, to rig the selection of contractors that organized HUD's multibillion-dollar sales of defaulted housing mortgages.

The criminal probe is tracking Mr. Ervin's charges.

Miss Dunlap, HUD's former deputy assistant secretary for multifamily housing, promoted Hamilton's selection to organize 19 separate auctions to sell more than 100,000 troubled HUD-insured mortgages to private investment firms at sharply discounted prices.

Mr. Ervin charged that HUD and Hamilton gave inside information to at least one repeat winner in the sales and rigged bidding to favor a select group of repeat winners in the auctions.

Miss Hinton, as HUD's "government technical representative" on Hamilton's \$20 million contract, was chief liaison to the firm and coordinated daily activities between Hamilton, other contractors and potential bidders in organizing the sales.

Her files contain meeting notes, reports of Hamilton's contacts with bidders, Hamilton's handling of bids, and records detailing final selection of note sale winners, officials said.

HUD fired Hamilton Oct. 20, citing a Dec. 20 report from the firm that said Hamilton altered bid numbers and changed winners and losers in several big sales because of "errors" in a computer program to select winners. Miss Hinton and Federal Housing Administration Comptroller Kathryn Rock knew of the report but took no action, officials said.

Nicolas P. Retsinas, FHA commissioner, also was sent the report.

HUD officials said Miss Hinton and other department employees were ordered nine months ago, when corruption charges were first lodged, "not to dispose of any records relevant to the Ervin litigation" and not to dump any records regarding the disputed note sales.

Officials said Mr. Retsinas sent out periodic reminders and recently dispatched another order to preserve all records after the general counsel's office told him of reports that Miss Hinton improperly removed records.

"When I became aware of the allegation involving the destruction of documents ... I asked the office of general counsel to independently review and investigate the allegation," Mr. Retsinas said in an interview.

"In consultation with the office of general counsel, I issued an additional memorandum reminding all housing headquarters employees about the importance of retaining all relevant documents," he said.

Officials said Mr. Glaser ordered a probe into the whistleblower's allegations immediately after a call from Mr. Ervin Oct. 21.

"The department has taken and will continue to take all appropriate action to ensure that all documents relevant to the civil litigation are preserved," the acting general counsel told The Times in an interview.

He declined to disclose findings so far about removal or destruction of documents, saying the probe "concerned matters in litigation."

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February 28, 2000

Justice unable to find bids worth \$5.2 billion

By George Archibald
THE WASHINGTON TIMES

The Justice Department, defending housing Secretary Andrew M. Cuomo against efforts to force his testimony in a bid-rigging case, told a federal judge that bids are missing for government housing auctions worth \$5.2 billion.

The claim in court affidavits 10 days ago is now disputed by Mr. Cuomo's spokesman at the Department of Housing and Urban Development. He said disputed bids were seized more than two years ago by investigators for Susan M. Gaffney, the agency's inspector general, as part of an ongoing criminal probe of multibillion-dollar contract fraud and bid-rigging in HUD's auctions of defaulted federally subsidized housing properties.

The criminal investigation has not resulted in any prosecutions to date. The IG has declined to comment, saying the probe is still under way.

But left in the middle of administration finger pointing is a frustrated and angry HUD contractor, Bethesda, Md.-based Ervin & Associates, which has sued HUD for multibillion-dollar fraud in defaulted housing sales.

It has asked District of Columbia Judge Emmet G. Sullivan to sort out whether a cover-up is under way — now assisted by criminal investigators appointed by President Clinton.

"Susan Gaffney is asleep at the switch or they're being told to kill this thing," said HUD contractor whistleblower John Ervin, who has used a four-year federal lawsuit and the Freedom of Information Act to extract evidence of HUD mismanagement and wrongdoing.

"They aren't stupid. There's a cover-up going on."

The tug-of-war over bid records involves Mr. Ervin's claim that Hamilton Securities Group, HUD's fired contractor for six housing mortgage auctions valued at \$5.2 billion, improperly awarded most of the properties to Wall Street

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investment firm Goldman Sachs & Co. and its partners, among the biggest contributors in the current and past presidential campaigns.

Ten days ago, Mr. Ervin asked Judge Sullivan to compel Mr. Cuomo's testimony to explain the whereabouts of bids HUD officials had claimed were missing — and why HUD turned over erased bid diskettes under court order for several sales tainted by Hamilton's actions to change bids and auction winners in several HUD property sales.

Justice responded that Mr. Cuomo's testimony was unwarranted because HUD never retrieved tainted bids from Hamilton after the firm was fired 28 months ago. Court records show that the firing occurred only after Miss Gaffney's investigators discovered HUD's knowledge of bid alterations and the agency's prior failure to protect the integrity of its sales.

"To the best of my knowledge, HUD did not receive the bids, original or copies, from Hamilton Securities at any time," said Gerald Salzman, then-supervisory financial adviser to FHA's comptroller, in an affidavit filed Feb. 18.

Joseph McCloskey, director of HUD's asset management division at the time of the auctions, said in a separate affidavit that HUD retrieved no bids for two auctions of 29,177 properties valued at \$1.3 billion. "HUD received copies of most of the bid diskettes" for three other sales of properties valued at \$3 billion, he said. Those were sales for which Mr. Ervin was provided some blank bid diskettes, court filings show.

Mr. McCloskey was silent about bids for 158 defaulted apartment complexes valued at \$884.5 million, which HUD sold at auction in June 1996. HUD has produced no bid records for that sale.

Mr. Ervin called HUD's position untenable for an agency on the General Accounting Office's "high risk" list for waste, fraud, and abuse.

"Even accepting this reputation, it is difficult to believe that HUD would not take control of the bids even after it learned that its multi-billion-dollar note sales auctions might have been rigged," he said.

"The only rational explanation for such obvious malfeasance is that a high-level cover-up of the problems with these note sales is in place, which includes concealing the bids that might expose blatant favoritism."

David Egner, a HUD spokesman, told The Washington Times on Friday that the IG's criminal investigators moved in 28 months ago and sequestered the auction documents provided by Hamilton, which is why HUD never received them. According to court filings, no such explanation was offered by the Justice

Department or HUD in its litigation with Mr. Ervin.

"Our understanding is that the inspector general or special master is in possession of the documents requested by Mr. Ervin," Mr. Egner said. "The inspector general's office has advised Mr. Ervin that it will not release the documents to him. If HUD had possession of the documents, the department would turn them over to Mr. Ervin, just as we have done with the other 12,000 pages of documents Mr. Ervin previously requested."

A senior HUD official told The Times that HUD received the bid documents from Hamilton, but they were promptly taken by IG investigator's on the eighth floor of HUD headquarters.

"It is my understanding that they took exclusive possession of these documents when they arrived in the department," the official said on the condition he not be named.

Mr. Ervin said the department's position proved concealment. "HUD always had access to the bids from their contractors and they could have gotten copies from the IG at any time. They have chosen not to," he said. "HUD was responsible for the note sales, not the IG."

HUD officials familiar with the criminal probe said IG investigators and the Justice Department have limited their probe to just two auctions involving Hamilton's admitted bid tampering and change of winners. By narrowing the scope, investigators excluded sales involving bids sought by the Ervin lawsuit that HUD officials said were missing, they said.

A criminal probe of possible bid-rigging in the HUD auctions commenced in October 1996, a year before Hamilton was fired. No officials have explained why the probe has taken more than three years to complete.

The disputed bids involve five auctions from 1995 to 1997 in which HUD sold 83,002 defaulted apartment complexes and single-family homes to developers and investment firms. Goldman Sachs and its partners won 68 percent of the properties valued at \$3.6 billion.

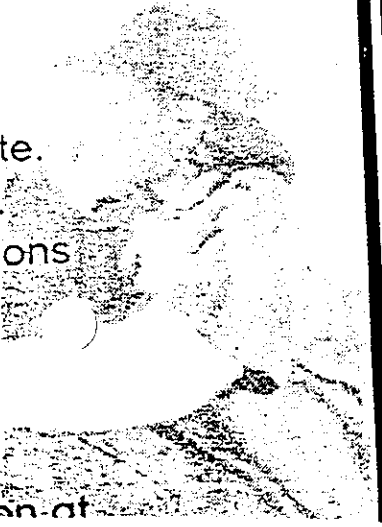
Justice attorneys representing HUD told Judge Sullivan in their filings that the department never saw the auction bids but entrusted Hamilton, the fired contractor, to maintain and certify them before awarding defaulted properties to successful bidders at a discounted price.

"That's extraordinary," said Wayne G. Travell, Mr. Ervin's attorney, "because what it means is the government conducted \$8.9 billion worth of auctions of government notes and never did even the most cursory review of how their contractor conducted those sales."

Wall St. Journal
10/21/97

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HUD Fires Contractor After Finding Errors Tied to Program on Mortgages

By CARL JOHNSTON
And ANITA SHARPE

Staff Reporters of THE WALL STREET JOURNAL
WASHINGTON — Housing Secretary Andrew Cuomo fired his chief financial advisory contractor after discovering that the company had developed "erroneous instructions" for a computer program that determined winners in mortgage auctions totaling about \$9 billion over the past two years.

Hamilton Securities Group Inc., run by former Federal Housing Administration commissioner C. Austin Fitts, immediately stopped receiving \$868,000-a-month payments on its \$20 million housing contract after it was fired last Friday. It also was ordered to repay the Department of Housing and Urban Development \$3.9 million lost due to the errors. A HUD official said some of the wrong bidders were selected because of a flaw in the model.

Hamilton, which notified HUD last year about the mistake, disputed "any characterizations that suggest our performance hasn't been up to the highest standards of professional conduct. We look forward to discussing these contentions with HUD and coming to an amicable resolution of our differences." The company said HUD was withholding \$1.6 million in fees for successfully completed work.

Mr. Cuomo also ordered a probe of all contracts involving Hamilton Securities, which has been a subject of a 17-month

investigation into systematic fixing of contracts awarded to firms handling mortgage auctions. Mr. Cuomo had been alerted about mortgage auction irregularities in 1995, while an assistant HUD secretary. He passed the allegations on to Nicolas Retsinas, the current FHA commissioner.

The department, meanwhile, said in court papers filed in federal district court in Washington, D.C., last week that it wanted to explore settling a \$40 million civil lawsuit filed by contractor John Ervin, who claims the agency cut off his contracts in retaliation for his criticism of it. That lawsuit, which HUD initially dismissed as "baseless," alleges that HUD officials illegally directed "enormously valuable contracts" to favored contractors.

Mr. Ervin's lawsuit says that Ms. Fitts, head of Hamilton Securities, is a close friend of Helen Dunlap, a former assistant HUD secretary who controlled the mortgage auctions until 1995, when she was transferred. Hamilton's initial maximum contract award was \$5 million over five years, the lawsuit says, but that ballooned to \$18 million over two years after Ms. Dunlap authorized a series of noncompetitive change orders and contract modifications.

Terrence O'Donnell, Ms. Dunlap's attorney, couldn't be reached for comment.

this," said Frank Clemente, Public Citizen's Congress Watch, "the best way to ensure they don't woodshed in the future is to have someone who is doing the spanking," Mr. said.

Mr. Schultz said the job-swaps reflect any cozy relationship between company and regulators. "It's a stern report," he said.

The report followed a series of accidents on CSX tracks, including an Amtrak derailment that injured last week in Georgia; a 34-car hazardous-materials train near Marianna, Fla., that derailed between two freight trains near W.Va., that killed one person and injured another.

The railway company was facing numerous safety problems, including working employees, track defects and a management that doesn't prioritize safety over profits. CSX has paid about \$7 million for violations uncovered in a recent FRA official.

Lawrence Mann, a Washington rail-safety attorney for railroads including the United Transp. at CSX, said Mr. Schultz's report "raises the question of what other problems have been in the report." The report was reported by The Washington Post.

CSX's Mr. Carpenter said that Mr. Schultz "has built a reputation as a zealot for employee safety" and will make a team the best in the industry. He described Mr. Schultz as "safety ombudsman" and top management.

After leaving the Air Force, he joined the private sector as an engineering manager at Proctor & Kierulff and joined the Chicago & North Western in 1980 and qualified engineer. He was a trainee and rules compliance officer at that railroad's executive office.

He started at the FRA as an officer in the Los Angeles office, rising through the ranks to being named associate safety director this past June.

Carl Cochran, legislative director for the United Transportation Union, who has worked with Schultz in the past, said he understands the problems that afflict the railroad. "Anything will be done," he said.

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