

# **Audit**

## **Follow-Up**

*As of September 30, 2009*



### **Audit of City Lease Administration**

*(Report #0917, Issued July 22, 2009)*

**Report #1011**

**February 19, 2010**

#### **Summary**

*The Property Management Division and the Electric Utility (as assisted by Utility Business and Customer Services) have completed or resolved nine of the 14 steps (64%) due for completion as of September 30, 2009. Significant actions have been initiated to resolve three of the five remaining steps. Actions to resolve the last two steps were temporarily deferred until a more appropriate time.*

In audit report #0917, issued July 22, 2009, we determined that City leases were generally properly executed, approved, and administered. However, several issues were identified in regard to leases of City property to external entities. Accordingly, recommendations were made to enhance the execution, administration, and management of those leases. Recommendations were also made in regard to billing and collecting lease revenues, maintenance of lease records, and internal operating procedures. Twenty-four action plan steps were developed to address our recommendations, for which 14 were due for completion as of September 30, 2009.

During this follow up engagement, we found nine of those 14 action steps had been completed and significant actions initiated for three of the five remaining steps. Completion of the last two steps, involving application of contract escalation provisions and the billing process for leases of City utility assets, was deferred until the start of the next appropriate billing cycle.

Significant actions completed or initiated included:

- The Property Management Division developed various procedures, forms, and checklists to assist City staff in negotiation, execution, and administration of City leases. Those procedures and forms were adopted and placed into operation. The new procedures and forms were provided to City departments.
- City departments were reminded to notify the Property Management Division of all prospective leases as required by City Real Estate Policy 136.
- Steps were taken to ensure more than one City employee and department is involved in leases initiated, executed, and/or renegotiated.
- The Property Management Division has been appropriately involved in leases executed by other City departments.
- Sales taxes have been properly assessed and collected from lessees that were not always assessed those taxes in the past.
- The Property Management Division developed a spreadsheet system to track City leases. Various data, including lease expiration dates, is tracked on those spreadsheets.
- For one significant lease (General Dynamics) the billing process was revised to provide for collection of the monthly payments (\$33,317) by the due dates established in the lease agreement.

- The Property Management Division established a centralized filing and storage location for the majority of applicable City leases.
- Utility Business and Customer Services (UBCS) staff are monitoring payment activity and working with the one lessee noted in the initial audit as significantly delinquent in payments owed the City.

Actions that were due but remain to be completed included:

- Coordinating with Accounting Services to ensure the billing process for several lessees (other than the General Dynamics lease) is appropriate to provide for timely receipt of the lease payments (Property Management Division).
- Obtaining and storing copies of a few remaining leases in the recently established centralized storage location (Property Management Division).
- Continuing to work with one lessee (noted in the initial audit as significantly delinquent in payments owed the City) to recover amounts owed the City in a reasonable time (Utility Business and Customer Services).

We appreciate the assistance and cooperation of applicable City staff during this follow-up process.

**Scope, Objectives, and Methodology**

The original audit and this subsequent follow-up were conducted in accordance with the International Standards for the Professional Practice of Internal Auditing and Generally Accepted Government Auditing Standards. Those standards require 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 objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

**Report #0917**

The scope of report #0917 included a review of City lease activities during the period January 1, 2006, through April 30, 2008. In some instances, negotiation and execution of leases prior to the above period were reviewed. The audit was conducted to evaluate the process for executing, approving, and administering City leases of real properties. The primary focus was to review the administration of leases of City-owned properties to other entities, including the collection of revenues for those leases. We also reviewed activities relating to the administration of leases of property by the City from external entities

The audit disclosed that, generally, City leases were properly executed, approved, and administered. However, several issues were identified in regard to leases of City property to external entities that, if not corrected, could limit the proper and efficient administration of those leases.

**Report #1011**

The purpose of this audit follow up is to report on the progress and status of efforts to complete action plan steps due for completion as of September 30, 2009. This is our first follow up on action plan steps identified in audit report #0917. To obtain information we conducted interviews with key department staff, made observations, and reviewed relevant documentation.

**Background**

The City’s Property Management Division generally coordinates initiation, negotiation, and execution of leases. Administration of executed leases is often the responsibility of affected City departments and offices. Based on information made available to us during the audit, there were approximately 110 leases of City-owned properties. Those 110 leases generated annual revenues that approximate \$6,600,000. Eight City departments and offices, including the Property Management Division, administered those 110 leases. Similarly, information obtained during the

audit showed the City had 17 leases of properties from external entities. Those 17 leases pertain to seven City departments and offices, including the Property Management Division. The annualized value of the lease payments incurred by the City for those 17 leases was \$351,570.

issues. Fourteen of those steps were due for completion as of September 30, 2009. Nine of those 14 (64%) action plan steps were completed. Significant actions were initiated but not completed for three of the remaining steps due for completion. Actions on the last two steps were deferred until a more appropriate time.

***Previous Conditions and Current Status***

In the initial audit report #0917, we identified the need for improvements within four City departments and offices. Twenty-four action plan steps were developed to address the applicable

Table 1 identifies the action plan steps due for completion and describes the current status of those actions.

**Table 1  
Action Plan Steps from Report #0917  
Due as of September 30, 2009, and Current Status**

<b>Action Plan Steps Due as of September 30, 2009</b>	<b>Current Status</b>
<b>Ensure that leases are properly executed and administered</b>	
<i>Property Management Division</i>	
<ul style="list-style-type: none"> <li>Management will emphasize to City departments and offices the requirement (prescribed by Real Estate Policy 136, as revised) for the Property Management Division to be timely notified of prospective leases.</li> </ul>	✓ <u>Addressed and Completed</u> - Property Management Division has called to the attention of City departments and offices the requirement (as prescribed by Real Estate Policy 136) to timely notify the Property Management Division of prospective leases. The requirement was addressed on the newly developed Real Property Lease Procedure provided to City departments and offices through internal office memorandum.
<ul style="list-style-type: none"> <li>The Property Management Division will negotiate, or assist in negotiating, all prospective leases for which it is made aware in accordance with Real Estate Policy 136, as revised.</li> </ul>	✓ <u>Addressed and Completed</u> - City departments and offices were advised to notify the Property Management Division of all prospective leases as provided by Real Estate Policy 136. In accordance with this advisement, the Property Management Division has been notified and/or involved in the execution or renewal of applicable leases since the release of the initial audit report.
<ul style="list-style-type: none"> <li>No leases will be negotiated and executed by any one employee, regardless of circumstances or lease terms and provisions.</li> </ul>	✓ <u>Addressed and Completed</u> - The Property Management Division has not directly initiated or executed any leases since the release of the initial audit report in July 2009. For those leases initiated, executed, and/or renegotiated by other City departments (e.g., Parks, Recreation, and Neighborhood Affairs) since July 2009, more than one City employee and department was involved.

<ul style="list-style-type: none"> <li>• A checklist will be developed and used to assist in the administration of leases. That checklist will address and serve to ensure, at a minimum:             <ul style="list-style-type: none"> <li>- Review and approval by the appropriate authorities as established by Real Estate Policy 136.</li> <li>- Review and approval by the City Attorney’s Office and Risk Management for adequacy of insurance coverage and other provisions needed to protect the City’s exposure to risks.</li> <li>- Updated certifications of insurance coverage are obtained and on file.</li> <li>- Valid exemptions from payment of state sales taxes are obtained and on file for applicable lessees.</li> </ul> </li> </ul>	<p>√ <u>Addressed and Completed</u> - To help administer and track City leases, the Property Management Division developed an appropriate checklist that addresses the noted items, as well as other items. To further facilitate the lease administration process, the Property Management Division also created a worksheet to track City leases and a lease summary form to capture essential elements and characteristics of each lease. Additionally, the Property Management Division created a standard service request form for City departments and offices to complete and submit to the Property Management Division when in need of services relating to leases. Those standard forms, as well as other standard City forms often applicable to City leases have been made available to City departments and offices through the City’s network.</p>
<ul style="list-style-type: none"> <li>• Lease amendments will be timely executed to reflect negotiated revisions, regardless of the related revenue or expenditure amounts involved.</li> </ul>	<p>√ <u>Step Considered Resolved</u> – No leases have been amended since the initial audit. Accordingly, no lease amendments were necessary. In the future, the Property Management Division should ensure appropriate lease amendments are timely executed as needed.</p>
<ul style="list-style-type: none"> <li>• State sales taxes will be assessed and collected from all lessees not exempt from such taxes.</li> </ul>	<p>√ <u>Addressed and Completed</u> - Since the release of the initial audit, state sales taxes have been properly assessed and collected from the two applicable lessees identified in the initial audit.</p>
<ul style="list-style-type: none"> <li>• A system/method will be established to track leases nearing termination and notifying applicable staff of the need to renew or negotiate a new lease, or plan for termination.</li> </ul>	<p>√ <u>Addressed and Completed</u> - The Property Management Division developed a spreadsheet system to track City leases. Various data is tracked, including lease expiration dates. The Property Management Division reviews that information on a monthly basis. Based on those monthly reviews, timely efforts are made to renew existing leases or negotiate new leases before the current leases expire.</p>
<ul style="list-style-type: none"> <li>• The billing process for leases will be revised to provide for receipt of required payments by the due dates established in the controlling lease agreements.</li> </ul>	<p>■ <u>Addressed but Not Completed</u> - For the most significant of the applicable leases, we found that the billing process was appropriately revised to provide for receipt of the required payments by the due dates established in the controlling lease agreement. (Monthly payments for this lessee, General Dynamics, were \$33,317.) However, for the other five applicable leases, City records and discussions with staff show the billing process was not revised to provide for receipt of payments by the required due dates established in the applicable lease agreements. (Monthly payments for those five leases ranged from \$100 to \$3,100.) We recommend the Property Management Division coordinate with Accounting Services staff to ensure the billing process for the five applicable leases is appropriate.</p>

<ul style="list-style-type: none"> <li>• A standard and centralized system for retention of applicable leases records and documents will be established.</li> </ul>	<ul style="list-style-type: none"> <li>■ <u>Addressed but Not Completed</u> - For those leases managed by the Property Management Division (PMD), we found PMD staff has established a centralized filing and storage location in the PMD office (i.e., a cabinet in a cubicle within the PMD office). Leases were filed alphabetically. As also noted above, the PMD prepared, distributed, and placed into operation “Real Property Procedures” that provide, among other things, for all leases of real property entered into by the City of Tallahassee to be kept on file in the PMD, and for the PMD to administer all leases of real property unless otherwise directed by the City Manager or the City Commission. Those procedures also provide that once a lease has been approved and executed, the PMD shall (1) record the original lease and related documentation with the Treasurer-Clerk’s Office, to be recorded in EDMS, (2) provide a copy to the requesting department, and (3) retain a copy in the PMD files. While most applicable leases appear to be stored in the centralized PMD files, management acknowledged that records for a few of the leases (e.g., some of the leases of space at the City’s community centers) are not yet on file in the PMD. Management indicated that the copies of those few remaining leases would be obtained and filed in the PMD. We recommend that action be completed.</li> </ul> <p>(NOTE: We also found that copies of leases of space on City utility assets {pole and tower attachments and cable fibers}, as well as airport terminal space, were not maintained in PMD files. However, as noted in the initial audit, City management may revise the current City Real Estate Policy 136 to exclude those leases from the provisions of that policy. Under those circumstances, the PMD will not be responsible for tracking or administering those leases.)</p>
<ul style="list-style-type: none"> <li>• Written internal procedures and guidelines will be developed to assist Property Management staff in negotiation, execution, and administration of City leases.</li> </ul>	<ul style="list-style-type: none"> <li>√ <u>Addressed and Completed</u> - The Property Management Division developed various procedures and forms to assist staff in negotiation, execution, and administration of City leases. Those procedures (i.e., the “Real Property Lease Procedures”) and forms (e.g., lease summary form and service request form) have been adopted and placed into operation.</li> </ul>
<p><b><i>Electric Utility (As assisted by Utility Business and Customer Services)</i></b></p>	
<ul style="list-style-type: none"> <li>• Staff will closely monitor the lessee that has been significantly delinquent in payment of amounts due for use of City–owned fiber optic cables.</li> </ul>	<ul style="list-style-type: none"> <li>√ <u>Addressed and Completed</u> – Staff continues to closely monitor activity to ensure payment for lease of City fiber optic cables. In regard to the lessee, noted in the initial audit report as approximately \$100,000 delinquent in amounts owed the City for lease of a City fiber optic cable, we found the lessee continued to struggle making its monthly payments. As</li> </ul>

	<p>described in the initial audit report, the City negotiated a monthly payment of \$5,046 for 48 months, with \$2,240 to represent payment for past due amounts and \$2,806 representing payment for the current month. Since the release of the initial audit report in July 2009, the lessee indicated that it was experiencing inadequate cash flows due to economic hardship. Accordingly, Utility Business and Customer Services (UBCS) renegotiated the monthly payment from \$5,046 to \$3,000. To date, the lessee has made the required payments (renegotiated amounts).</p>
<ul style="list-style-type: none"> <li>• Timely efforts will be made to obtain amounts due from lessees that are significantly delinquent in payments of amounts due. Lessees with continued delinquencies beyond a reasonable time will not be allowed to continue use of City property.</li> </ul>	<ul style="list-style-type: none"> <li>■ <u>Addressed but Not Completed</u> – As noted above in the described status for the preceding action plan step, staff continues to make efforts to collect both past due and current amounts due from the lessee that was significantly delinquent in amounts owed the City. As described, due to financial difficulties experienced by the lessee, the monthly lease payment was renegotiated since the release of the initial audit. That renegotiated amount of \$3,000 includes \$194 as payment for past due amounts and \$2,806 as payment for the current month. Based on the renegotiated payment amount, it will take the City approximately 40 years to recover all delinquent amounts. UBCS staff indicated that the renegotiated payment amount is “temporary.” We recommend UBCS continue to monitor the financial circumstances of the lessee and, when circumstances are appropriate, revert monthly billing amounts to the initial negotiated amount of \$5,046.</li> </ul>
<ul style="list-style-type: none"> <li>• Escalation provisions will be exercised and applied. In the event such provisions are not exercised/applied, justification and explanation will be documented.</li> </ul>	<ul style="list-style-type: none"> <li>▶ <u>Deferred</u> - Management amended the due date of the action plan step from 6/29/09 to 1/31/10. According to staff, the new billing period starts in January 2010. Accordingly, any applicable escalation will be applied in the 2010 billing cycle.</li> </ul>
<ul style="list-style-type: none"> <li>• The billing process for leases will be revised to provide for receipt of required payments by the due dates established in the controlling lease agreements.</li> </ul>	<ul style="list-style-type: none"> <li>▶ <u>Deferred</u> - Management amended the due date of the action plan step from 6/29/09 to 1/31/10. According to staff, the new billing period starts in January 2010. Accordingly, any applicable changes to the billing process will be applied during the 2010 billing cycle.</li> </ul>

**Table Legend:**

- Issue to be addressed from the original audit

- √ Issue addressed and completed or resolved
- Issue addressed but not completed or resolved
- ▶ Action on issue temporarily deferred

***Conclusion***

As noted above, nine of the 14 action plan steps due for completion as of September 30, 2009, were addressed and resolved. As also described, significant actions were initiated for three of the five other steps, while the actions for the last two steps were deferred until a more appropriate time. We commend staff for being responsive and thorough in their follow up actions.

In addition to the 14 steps addressed above, there are 10 more action plan steps due for completion subsequent to September 30, 2009. The more significant actions to be completed pursuant to those 10 action plan steps include:

- Revising the City Real Estate Policy 136 to identify lease types covered by that policy and to provide delegation of approval authorities under specified circumstances.
- Using recently developed checklists to ensure the proper execution and administration of new or renegotiated City leases.
- Maintaining a complete and centralized inventory of all City leases within the Property Management Division.
- Providing training to applicable City staff on policies, procedures, and processes developed or revised as a result of audit report #0917.
- Notification to the Property Management Division of prospective leases by applicable departments pursuant to Real Estate Policy 136, as revised; and obtaining assistance from the Property Management Division in the negotiation and execution of leases as prescribed by the revised policy.

We appreciate the cooperation and assistance the applicable City departments and offices provided in this audit follow-up.

***Appointed Official's Response***

**City Manager:**

The City Auditor's assistance in reviewing City lease administration has been very beneficial. The audit suggested numerous steps to improve lease administration, most of which were implemented during the audit process. The remaining items in the action plan will be completed in the next 90 days. We appreciate this effort to review our processes and improve accountability. The City Auditor's staff was professional, cooperative and made some excellent suggestions.

Copies of this Audit Follow-Up or audit report #1011 may be obtained from the City Auditor's web site (<http://talgov.com/auditing/index.cfm>), via request by telephone (850 / 891-8397), by FAX (850 / 891-0912), by mail or in person (City Auditor, 300 S. Adams Street, Mail Box A-22, Tallahassee, FL 32301-1731), or by e-mail ([auditors@talgov.com](mailto:auditors@talgov.com)).

Audit Follow-Up conducted by:  
Reuben C. Iyamu, Senior Auditor  
T. Bert Fletcher, CPA, Sr. Audit Manager  
Sam M. McCall, Ph.D., CPA, CGFM, CIA, CGAP, City Auditor