Enhance Focus on Lease Administration of City-Owned Properties

This audit highlights the need to focus on effective lease administration and to ensure the City receives all entitled revenue from leasing out City-owned properties. The City needs to effectively review and monitor leases in order to bill and collect the right amount of rents and recoveries. A review of all leases is required to address our audit findings.

What we found

A. Effective Review and Monitoring Needed to Maximize Lease Revenues

- Rents may not be based on market rates – documents to support the basis for negotiated rents were not retained in 11 of 24 commercial leases (46%). We noted better record retention in support of more recent agreements.

- City is not ensuring tenants fulfill their obligations for contracted capital improvements – there was insufficient evidence to support the receipt of $14.1 million in required capital improvements.

- Incremental rent revenues are lost when rent escalations, rent reviews, and lease renewals are not performed – an additional $931,000 could have been generated if expired agreements were promptly renewed with rents annually adjusted in line with inflation (using the Consumer Price Index).

B. Action Needed to Bill and Collect Additional Rents and Recoveries

- In addition to basic rent, commercial leases may require percentage rents, utility costs, property taxes, and/or other eligible operating expenses to be calculated and recovered. In nearly half the leases we reviewed (22 out of 45), the City did not calculate, bill, or collect additional rents and recoveries.

- In our sample, we identified at least $4.5 million that have not been billed for prior periods, of which at least $728,000 relates to 2017. 65% of this amount pertains to below market rent tenants. However, as reflected in the agreements we reviewed, it is expected that these below market tenancies be cost-neutral to the City.

- It is likely that additional concerns exist and amounts have gone unbilled over time in the leases we did not review.

C. New Service Delivery Model Centralizes Lease Administration

This is the opportune time to establish a coordinated strategy to maximize value from City-owned property, develop effective performance measures, standardize City-wide policies and procedures, and ensure appropriate resourcing of the leasing function. A 15% fee applied to operating cost recoveries for commercial agreements could generate over $500,000 annually to help recover the cost of lease administration.

How Recommendations will Benefit the City

The audit makes 19 recommendations to help ensure that the City meets its program and strategic objectives, maximizes rent revenues, and recovers operating costs. Implementing the recommendations will improve how the City manages its leasing agreements going forward as well as how the City collects its rental income.

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