

City of



BUDGET & MANAGEMENT STUDIES – INTERNAL AUDIT

DATE: February 23, 2011

TO: PAUL MELIKIAN, Administrative Manager, PARCS

THROUGH: RENENA SMITH, Budget Director *RS*
Budget and Management Studies

FROM: BOB KOURY, Principal Internal Auditor *Bob Koury*
BILL RICHARDS, Internal Auditor *Bill Richards*
Budget and Management Studies - Internal Audit

SUBJECT: FOLLOW-UP AUDIT REPORT – PARC REVENUE PROPERTY LEASE AUDIT

Attached is the Follow-Up Audit Report with the current implementation status of the seventeen recommendations made in the PARCS Revenue Property Lease Audit report issued on June 8, 2010. (The complete original audit report can be found on the City's Internal Audit web site for reference purposes if necessary.) This follow-up audit was performed in accordance with AO 1-12 and Government Auditing Standards.

Internal Audit has reviewed the Department's provided documentation and concluded:

- 4 - Recommendations Implemented
- 1 - Recommendation Partially Implemented
- 10 - Recommendations In-Progress
- 2 - Recommendations Not Implemented

Thank you for your assistance during the course of this follow-up audit. If you have any questions, please do not hesitate to contact Bob Koury, Principal Internal Auditor at 621-7072 or Bill Richards, Internal Auditor at 621-7063.

Attachments

cc: Ashley Swearengen, Mayor
Council Members
Mark Scott, City Manager
Bruce Rudd, Assistant City Manager
Nicole Zieba, Deputy City Manager
James Sanchez, City Attorney
Joe Gray, Finance Director/City Controller
Jane Sumpter, Principal Budget Analyst, Budget and Management Studies



BUDGET & MANAGEMENT STUDIES – INTERNAL AUDIT

FOLLOW-UP AUDIT REPORT

**PARCS
Revenue Property Lease Audit**

Audit Number 11-0008

**Performed by:
Bill Richards, Internal Auditor
Budget and Management Studies – Internal Audit**

Issued on February 23, 2011

AUDIT RESULTS AND RECOMMENDATIONS

PARCS provided Internal Audit with their Contract List during our Risk Assessment Project. That list contained 26 Revenue Property Leases with an estimated annual lease revenue of \$240,777. Internal Audit selected a sample of thirteen Lease contracts with an estimated annual revenue of \$178,000. The sample consisted of twelve \$1 Year Leases and three other Leases.

I. Contract Administrator

The Contract Administrator position has been vacant for several months. PARCS oversight of contracts is inhibited by the vacant Contract Administrator position and decreases in staffing. Per our review, the contract files are organized and neat with a contract folder for each contract but the vacant position has an adverse impact on the continuous administering, monitoring and enforcing contract compliance (e.g. receipt of timely rent payments, assessment of late payment charges, current Insurance Certificates.)

Audit Recommendation 1

1. PARCS Management should either fill the Contract Administrator vacancy or assign all the Contract Administrator responsibilities to a staff member to ensure the continuous administration, monitoring, and enforcing of revenue property lease compliance and enhanced rental revenue.

Original Management Response to Recommendation 1

PARCS Management agrees with the recommendation of assigning all Contract Administrator responsibilities to staff members to ensure the continuous administration, monitoring, and enforcing of revenue property lease compliance and enhanced rental revenue. Due to the loss of the Management Analyst II position that was previously assigned to this function, the Administrative Manager has taken over oversight of contracts. This is in addition to the elimination of 80% of administrative support positions since January 2010. As a result, only the highest priority tasks will be undertaken. Inevitably, unless additional staff is retained, some lower priority contract management functions will not occur, or at best, at less frequent intervals.

Current Status of Recommendation 1 - Implemented

PARCS Management agrees with this recommendation and has assigned the Executive Assistant, under the supervision of the Administrative Manager, to ensure the continuous administration, monitoring, and enforcing of revenue property lease compliance and enhanced rental revenue.

II. City Owned Property Leased for \$1 Year

Internal Audit reviewed a sample of the \$1 Year Lease Contracts listed on the PARCS Contract List, the respective Contract folders, the PARCS FY08-10 Lease Receivables Listings, and the PARCS FY09-10 Contract Sites Expenses Incurred Lists. Internal Audit noted the following for the sampled contracts:

- Two Lease Contracts are not under PARCS oversight. The Meux Home is under the City Managers Office's oversight and the Fresno Convention and Visitors Bureau Water Tower is under the Department of Public Utilities oversight.

- The Fresno County EOC Head-Start Program Lease of space at the Mosqueda Center expired on December 31, 2007.
- Ten annual rent payments of \$1 each were not received and two Lease entities were not listed on the Lease Receivables List.
- Two Lessees did not pay the utilities expenses as required by the Lease. PARCS paid \$7,133 in FY-09 for the Boys & Girls Club, East; and paid \$2,658 in FY-09 and \$2,429 in FY-10 for the Discovery Center, for a total of \$12,220 paid by PARCS instead of by the Lessees.
- Four Insurance Certificates have expired and two contract folders did not contain an Insurance Certificate. In addition, one current Certificate does not list the City as Certificate Holder and Additional Insured and one current Certificate does not list Workers Compensation coverage.
- Twelve City owned properties are being leased to outside entities with no rent being assessed and collected (Exhibit A). If the City (PARCS) were to assess and collect even a reasonable rent amount of \$250 per month from each of the twelve entities, this would equate to approximately \$36,000 in additional rental revenue for the City (PARCS). This additional rental revenue could also help defray some of the maintenance and repair expenses for these City owned properties.

Audit Recommendation 2

2. PARCS Management should update their Contract List and Lease Receivables List to ensure the Lists contain the Lease Contracts for which PARCS has oversight responsibility.

Original Management Response to Recommendation 2

The Meux Home Museum lease is in the middle of the renewal process and will be taken to Council for approval in the next 60 days. The new lease will specify that PARCS is the contract administrator. Staff will investigate IA's finding that the Water Tower should be under DPU's oversight. PARCS is currently working with the CVB to transfer Water Tower utility accounts to the City as they are vacating the premises mid-June.

Current Status Response to Recommendation 2 - In-Progress

PARCS Management agrees with this recommendation and assigned the Executive Assistant to update the Contract List and the Senior Account Clerk to keep current the Lease Receivables List.

Audit Recommendation 3

3. PARCS Management should determine if the expired Fresno County EOC Head-Start Program Lease is to be extended or the property leased to another non-profit organization.

Original Management Response to Recommendation 3

PARCS has met with representatives from Fresno County EOC Head-Start Program to discuss their building and land leases at five locations within the park system. (All five leases are currently expired.) The five sites have been renegotiated to both parties satisfaction and will be taken before Council in the next 60 days.

Current Status Response to Recommendation 3 – In Progress

PARCS Management agrees with this recommendation. On January 20, 2011 Administrative Manager met with Fresno County EOC representative to discuss renegotiating the lease to include rent for the five Head Start sites. A consolidated Master Lease for the five locations will be brought forward to Council in the next 60 days.

Audit Recommendation 4

4. PARCS Management should pursue the collection of all unpaid annual rents and increase their monitoring efforts in the future to ensure the receipt of all revenue in a timely manner.

Original Management Response to Recommendation 4

Staff will address the non-payment of the \$1.00/year leases as time permits, however recognizing the challenges described in response #1; this has been deemed a lower priority activity. The lease receivables list has been updated to include all lease entities.

Current Status Response to Recommendation 4 - In Progress

Staff is pursuing the collection of all unpaid annual rents and increase monitoring efforts to ensure the receipt of all revenue in a timely manner. A monthly lease/rent log is maintained and reviewed regularly.

Audit Recommendation 5

5. PARCS Management should pursue the collection of the Lessees' utility expenses for FY09-10 to ensure cost recovery and increase their monitoring efforts in the future.

Original Management Response to Recommendation 5

The Department no longer pays the utilities for Boys & Girls Club, East. The Discovery Center lease is being revised and updated, which will clear up the utility issue there.

Current Status Response to Recommendation 5- Not Implemented

PARCS Department will not be pursuing collection of utility payments as recommended/called out in the lease. The \$7,133 is likely related to the changeover in responsibility of utilities from the City to Boys & Girls Club. The \$2,658 of utilities paid on behalf of the Discovery Center has been factored into the new negotiated lease with this entity. The Department does not anticipate any future issues in this area.

Audit Recommendation 6

6. PARCS Management should immediately obtain from all applicable Lessees a current Certificate of Insurance with applicable endorsements evidencing renewal of all required insurance and monitor insurance coverage in the future to ensure coverage exists.

Original Management Response to Recommendation 6

Staff will make every effort to obtain from all applicable Lessees' a current Certificate of Insurance with applicable endorsements.

Current Status Response to Recommendation 6 – In Progress

The Contract Administrator position has been vacant since late 2009. The Executive Assistant is reviewing contract files and sending notices to Lessees requesting current Certificate of Insurance with applicable endorsements. Risk Management reviews document and date stamps approval.

Audit Recommendation 7

7. PARCS Management should immediately pursue and implement a reasonable and fair amount of rent for all City owned properties currently being leased to outside entities at "no rent", e.g. at \$250 per month for the twelve lessees would generate \$36,000 per year in additional rental revenue.

Original Management Response to Recommendation 7

The Department has committed to renegotiate 'no rent' leases as they come up for renewal (or as an opportunity arises) to, at minimum, recoup some or all of the City cost associated with maintaining/providing the facility or space to the lessee. However, some leases simply do not support the collection of any rent because of the value of services provided to the general public, i.e. Meux Home Museum, etc.

Current Status of Recommendation 7 – In Progress

The Department has provided the City Manager's Office with the list of \$1.00/year and no-rent leases to be used for a Council workshop to discuss future City policy in this area. Where possible, the Department is meeting with Lessees to discuss implementing a reasonable and fair amount of rent. As an example of implementing this goal, PARCS Management met with the Fresno County Library representative who stated that the Library's current budget situation does not allow the ability to pay any rent at this time.

III. Valley Arts and Science Academy

The Valley Arts and Science Academy lease is for vacant property adjacent to the Ted C. Wills Community Center to establish a charter school. The Lease period is March 2007 through February 2012. The rent is \$2,000 per month with an annual rent increase in the second through the fifth year. The rent is due on the first of each month and subject to a late charge of 7% for payments received after the fifth day of the month. Internal Audit reviewed the Lease Contract, the Contract folder, the FY08-10 Lease Receivables Lists and noted the following:

- The base rent was not adjusted yearly. The FY08-10 Lease Receivables Lists shows the rent received as \$2,000 a month. The monthly rent was not increased on September 2008 and September 2009 resulting in an estimated \$1,309 in lost rent revenue. The Lease Contract Section 1.7.4 states, "The Base Rent for the second, third, fourth and fifth calendar years of the Term shall be adjusted yearly on the anniversary of the Commencement Date and shall be the greater of (i) the product of the Base Rent for the immediately preceding calendar year multiplied by 1.025 or (ii) the product of the Base Rent for the immediately preceding calendar year multiplied by

COLA, as in effect on the first business day of the each respective calendar year of the Term.” Internal Audit informed PARCS Management and a meeting was immediately scheduled with the Lessee.

- Late payment charges were not assessed. The PARCS Lease Receivables Lists for FY08-10 shows the monthly rent payment amount and date. Internal Audit estimated late payment charges were not assessed on 30 late payments totaling \$4,246. However, based on a discussion with PARCS staff, the payment date recorded on the Lease Receivables List may not be the actual payment received date as payments received are not date stamped. The Lease Contract Section 5.1 states, “Base Rent shall be payable to Landlord in advance on the first business day of each calendar month.” Contract Section 5 states, “Tenant shall be entitled to a five (5) day grace period to pay rent.” Section 5.6 states, “... if any installment of rent or other sum due from Tenant shall not be received in full by Landlord or Landlord’s designee on the date said payment is due, than Tenant shall pay to Landlord a late charge equal to interest accrued on such payment at the rate of seven (7%) percent per annum, based upon the full amount of said payment, any partial payment notwithstanding.”
- The Lessee did not pay their share of utility expenses. PARCS paid the Ted C. Wills Community Center utility expenses of \$94,181 in FY-09 and \$72,204 in FY-10 to date. Internal Audit was unable to estimate the Lessee’s share of utility expenses. The Lease Contract Section 12.1 states, “Tenant shall pay Tenant’s Share of Expenses of all water, gas, heat, light, power, sewer, electricity, and telephone or other service metered, chargeable or provided to the Property and Project.”
- The Certificate of Insurance in the contract folder expired in November 2009. All required insurance coverage may not be in full force and effect. The Lease Contract Section 15.1 states, “In the event any policies are due to expire during the term of this Lease, Tenant shall provide a new certificate evidencing renewal of such policy not less than 15 calendar days prior to the expiration date of the expiring policy(ies).”
- The Lessee did not submit annual Financial Statements. The Lease Contract Section 19.1 states, “Tenant shall furnish the following to the Landlord on or before June 30 of each year, a copy of ...consolidated financial statements audited...or reviewed by a ... recognized firm of certified public accountants.”

Audit Recommendation 8

8. PARCS Management should immediately pursue the assessment and collection of the current and prior years rent adjustments and increase their monitoring efforts in the future to ensure the timely receipt of all appropriate lease revenue.

Original Management Response to Recommendation 8

VASA’s rent will be adjusted July 2010 to bring them current to the annual adjustments built into their lease. The Department will add annual rent adjustment reminders to its lease tracking spreadsheet so that lease payments will be adjusted as required.

Current Status Response to Recommendation 8 – Not Implemented

The Department will not be pursuing collections of prior years rent adjustments; however, future contractual rent adjustments will be flagged so that they are not missed going forward. All lease payments are tracked on a monthly log so that delinquencies are dealt with in a timely manner.

Audit Recommendation 9

9. PARCS Management should implement a procedure to date stamp all rent payments received from Lessees to properly document actual receipt dates of rent payments. In addition, PARCS Management should pursue the feasibility of determining the actual received date of the rent payments from the Lessee and assessing late payment charges accordingly.

Original Management Response to Recommendation 9

Staff will investigate internal procedure and feasibility of date stamping payments received from Lessees' to properly document actual receipt dates of rent payments. As time/schedules permit, Staff will assess late payment charges accordingly.

Current Status Response to Recommendation 9 - Implemented

All payments will be date stamped the day they are received and compared to the contractual due date to determine if a late fee is applicable.

Audit Recommendation 10

10. PARCS Management should calculate and pursue collection of Lessee's share of the utility expenses for FY09-10, as appropriate, and ensure the Lessee pays their share in the future as required by the Lease.

Original Management Response to Recommendation 10

Using IA's findings as the catalyst, Staff met with the VASA Board May 2010 and negotiated a utility reimbursement formula that will be put in place July 2010.

Current Status Response to Recommendation 10 – Partially Implemented

This has been completed. Department staff met with the VASA Board last summer and worked out a procedure to begin billing for proportionate share of utilities. VASA is current in their share of the utility expenses.

Audit Recommendation 11

11. PARCS Management should immediately obtain from the Lessee a current Certificate of Insurance with applicable endorsements evidencing renewal of all required insurance and monitor insurance coverage in the future to ensure coverage exists.

Original Management Response to Recommendation 11

Done.

Current Status Response to Recommendation 11 – In Progress

A letter requesting this information has already been sent to the lessee.

Audit Recommendation 12

12. PARCS Management should obtain from the Lessee a current copy of the required Lessees' Financial Statements and ensure a copy is received annually in the future per the lease.

Original Management Response to Recommendation 12

Done.

Current Status Response to Recommendation 12 – In Progress

A letter requesting this information has already been sent to the lessee.

IV. Central California Events, Inc.

Central California Events leases a building with paved parking for the purpose of entertainment and recreational uses. The Lease commenced in January 2009 and is month-to-month and shall automatically renew until terminated. The monthly rent is \$1,000 January through July and the month of December, and \$4,000 per month August through November. The rent is due on the first of each month and subject to a late charge of 10% for payments received after the seventh day of the month. Internal Audit reviewed the Lease Contract, the Contract folder, the FY08-10 Lease Receivables Lists and noted the following:

- The Lessee was not on the FY-09 Lease Receivables List and the FY-10 List did not show the receipt of the March 2010 rent payment. Internal Audit informed PARCS Management and immediately received updated Lease Receivables Listings and determined that rent payments were timely received.
- The Certificate of Insurance in the contract folder expired in November 2009. All required insurance coverage may not be in full force and effect. The Lease Contract Section 11 states, "In the event any policies are due to expire during the term of this Lease, Lessee shall provide a new certificate evidencing renewal of such policy not less than 15 calendar days prior to the expiration date of the expiring policy(ies)."

Audit Recommendation 13

13. PARCS Management should ensure the Lease Receivables Listings are timely updated to ensure accurate and timely recording of lease revenue and for future reference or audit purposes.

Original Management Response to Recommendation 13

PARCS Management has taken the necessary steps to ensure that all Lease Receivables Listings are timely updated to ensure accurate and timely recording of lease revenue and for future reference or audit purposes. This list will be reviewed by the Administrative Manager on a monthly basis.

Current Status Response to Recommendation 13 – In Progress

CCE is current with their monthly lease payments.

Audit Recommendation 14

14. PARCS Management should immediately obtain from the Lessee a current Certificate of Insurance with applicable endorsements evidencing renewal of all required insurance and monitor insurance coverage in the future to ensure coverage exists.

Original Management Response to Recommendation 14

Done.

Current Status Response to Recommendation 14 – In Progress

PARCS has requested CCE to provide a current Certificate of Insurance. A follow-up request will be sent this week with a deadline to respond.

V. EBIT Golf, Inc.

The EBIT Golf contract is a Lease and management agreement to operate the Riverside Municipal Golf Course. The extended Lease period is September 2009 through August 2019. The rent is 14% of gross golf revenue, 3% of gross merchandise revenue, and 3% of gross food and beverage revenue. The rent is due in arrears on the twentieth day of each month and subject to a late charge of 2% for payments received after the last day of the month. Internal Audit reviewed the Lease Contract, the Contract folder, the Lease Receivables Lists, the Lessee's Sales Detail Reports, and reconciled a sample rent payments to the Lessees' support documentation. Internal Audit noted the following:

- The Lease Receivables Lists did not list the rent payments for FY-08 and February 2010. Internal Audit informed PARCS Management and staff and immediately received updated Lease Receivables Listings.
- Late payment charges were not assessed. The PARCS Lease Receivables Lists for FY08-10 shows the monthly rent payment amount and date. Internal Audit estimated late payment charges were not assessed on four late payments totaling \$1,521. However, based on our discussion with PARCS staff, the payment date recorded on the Lease Receivables List may not be the actual payment received date. Payments received are not date stamped. The Lease Contract Section 4.02 states, "Rent shall be paid in arrears in the following manner: On the twentieth (20th) calendar day of each month." The Contract Section 4.04 states, "A late payment charge of two percent (2%) per month shall be added to any late payment that is received after the last day of the calendar month in which payment is due."
- The Certificate of Insurance in the contract folder expired on June 30, 2009. All required insurance coverage may not be in full force and effect. The Lease Contract Section 13.1 states, "In the event any policy is due to expire during the work to be performed by City, Lessee shall provide a new certificate, and applicable endorsements, evidencing renewal of such policy not less than 15 calendar days prior to the expiration date of the expiring policy."

Audit Recommendation 15

15. PARCS Management should ensure the Lease Receivables Listings are timely updated to ensure accurate and timely recording of lease revenue and for future reference or audit purposes.

Original Management Response to Recommendation 15

Same answer as #13.

Current Status Response to Recommendation 15 – In Progress

See below.

Audit Recommendation 16

16. PARCS Management should implement a procedure to date stamp all rent payments received from Lessees to properly document the actual received date of rent payments. In addition, PARCS Management should pursue the feasibility of determining the actual received date of the rent payments from the Lessee and assessing late payment charges accordingly.

Original Management Response to Recommendation 16

Same answer as #9.

Current Status Response to Recommendation 16 - Implemented

PARCS has implemented a procedure to date stamp all rent payments received from Lessees to properly document the actual received date of rent payments and assessing late payment charges accordingly. When cash payments are received, a receipt is computer-generated.

Audit Recommendation 17

17. PARCS Management should immediately obtain from the Lessee a current Certificate of Insurance with applicable endorsements evidencing renewal of all required insurance and monitor insurance coverage in the future to ensure coverage exists.

Original Management Response to Recommendation 17

Done.

Current Status Response to Recommendation 17 - Implemented

This has been completed.

The Contract Administrator position has been vacant since late 2009. The Executive Assistant is reviewing contract files, sending notices to Lessees requesting current Certificate of Insurance with applicable endorsements, and coordinating with Risk Management for review and approval. Risk returns document with approval date stamp.