

Highlights

Why We Did This Audit

While conducting work on our December 2020 audit of city buildings and facilities, we noted lease rates may not be increasing according to provisions in the leases. Not increasing rent amounts according to the lease provisions deprives the city of revenue it is entitled to receive.

In April 2015 we recommended and in December 2019 the City Council directed that a policy for leasing city properties at below-market rates be developed. A below-market lease policy would help ensure consistency and transparency when evaluating and considering these types of leases.

Objectives

- Is the city receiving all rent payments due for leased property?
- Does the city have a policy for below-market rate leases?

Background

The General Services Department manages city property leases (except Aviation, Convention and Entertainment Facilities, and Parks and Recreation leases). Uses of city properties leased by third-parties include office and retail spaces, restaurants, farmland, performing arts, and warehouses.

In fiscal year 2020 the city leased about 50 properties and received about \$1 million from leases. General Services also leases some properties to non-profit agencies at below-market rates.

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PERFORMANCE AUDIT

Leases Not Actively Managed, City Owed Money

What We Found

General Services is not actively managing leases. The city is owed nearly \$443,000 in unpaid rent revenue. The department recently started developing a process to collect delinquent rents.

The city also missed out on about \$164,500 in rent revenue because monthly rent rates were not increased as outlined in lease provisions. Additionally, General Services did not renew seven expired leases timely. These properties were occupied for 6 to 56 months without a contract and the holdover provision was not enforced.

General Services does not have documented policies or procedures for managing the city's leases except for City Code Section 3-203 and Administrative Regulation (AR) 3-04 that discuss rent rate increases. The AR is silent on how leases should be managed. Our 2015 audit, [Leasing City-Owned Property](#), recommended General Services develop written procedures that include all aspects of the leasing function, including procedures for collecting lease payments and managing lease renewal. Management reported they are in the process of implementing a recently acquired a property management system which should assist in managing the city's lease properties.

The City Code requires the use of an outdated Consumer Price Index to increase rent rates. This index was discontinued in 2017 and the city needs a current index or other method to increase rent rates on leased city properties.

The city still has not developed a policy to ensure the public benefit of below-market leases. Since 2018 the city entered into two below-market rate leases and waived the rent on another lease. Most of the city's twelve below-market rate leases have a lease rate of \$1.00 per year. Without a below-market lease policy the city may not be consistently evaluating organizations' qualifications and whether they provide enough public benefit to justify the rent subsidy.

Our 2015 audit recommended a formal below-market rate lease policy and process be developed to evaluate subsidy requests, calculate subsidies, and publicly report subsidies to help ensure the city's lease subsidies support city goals. The City Council also passed [Resolution 190858](#) in 2019 directing the city manager to develop a policy for evaluating and reporting on below-market rent leases.

Rent Amounts Owed to the City

Calendar Year	Amount Owed
2016	\$49,133
2017	\$15,674
2018	\$67,498
2019	\$110,267
2020	\$200,194
Total	\$442,766

What We Recommend (full list on back)

We make recommendations to improve the city's lease management program and enhance the transparency and oversight of below-market rate leases.

Management agreed with the recommendations.

Recommendations

1. The director of general services should invoice lessees for unpaid rent amounts and ensure delinquent rent amounts are included on future monthly rent invoices.
2. The director of general services should develop a process to review leases annually and increase rent amounts as outlined in lease documents and update rent invoices to the new amounts.
3. The director of general services should develop a process to systematically identify leases nearing the end of the lease term, begin negotiating lease renewals, preparing to make properties available to potential lessees, or enforcing the holdover provision when applicable.
4. The director of general services should develop documented leasing procedures that addresses issues identified in this audit, other aspects of the leasing function, and use of the new property management system.
5. The city manager should identify an appropriate Consumer Price Index or other method to increase rent rates on leased city properties and prepare for City Council consideration an ordinance to update the City Code with the new index or methodology.
6. The city manager should develop a policy for council consideration for evaluating and reporting on below-market rent leases. At a minimum, the policy should include the following:

Prior to award:

- Determining whether the value of the benefit provided by the requesting organization qualifies it for a subsidy;
- Evaluating financial viability of the organization;
- Calculating the value of the lease subsidy;
- Calculating the capital and general maintenance, and utilities related to the leased properties; and
- Obtaining council authorization for the subsidy.

On a continuing basis:

- Reporting the amount of subsidies to the council annually; and
- Reviewing subsidized organizations periodically to determine whether the organization continues to provide the benefit agreed to at the time of lease approval.