

**OFFICE OF THE CITY AUDITOR AND CLERK**  
**INTERNAL AUDIT**



**CITY PROPERTY LEASING**

AUDIT #20-06

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# Executive Summary

## Audit #20-06 City Property Leasing

### Audit Purpose, Scope and Time Period

Internal Audit performed an operational/compliance audit of the City of Sarasota's Property Leases.

The purpose of this audit was to provide reasonable assurance that payments received for lease contracts are in agreement with contract terms.

The scope of this audit included a review of property leases held by the City of Sarasota. Our audit assessed the City's monitoring of lessees' compliance with lease terms. Specifically, determining whether the City received timely and accurate lease payments and other lease requirements are being followed. Additionally, we reviewed Purchasing's maintaining lessees' proof of insurance. The audit period was October 1, 2018 to May 31, 2020.

### Audit Objectives

- 1) Determine whether revenue is received according to the lease.
- 2) Determine whether lessees were held accountable for compliance with lease terms.

### Summary Background

The City acts as the lessor or "landlord" to approximately 50 active property leases. Currently, City leases are administered by three different departments. Facilities maintains the master list of contracts and actively works with the Commission on the over all maintenance of these contracts. Purchasing maintains the insurance documentation and policy renewals, while Finance handles invoicing and revenue collection.

### Summary of Conclusions

The audit identified opportunities to strengthen controls over monitoring, reconciling, and documenting the revenue aspect of leases. The results of our audit indicate property lease revenue is not always being consistently received according to the lease. There are controls in place to maintain and track lease renewal dates, certificates of insurance, or other required documentation.

Testing identified the following:

- A need for centralization of lease administration
- Sales tax calculated at incorrect rates
- Additional oversight/monitoring of below market/nominal leases is needed

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This Executive Summary is limited in detail. To obtain the full background on a particular item, please read the Detailed Audit Report or contact Internal Audit prior to drawing conclusions based upon the limited information contained in this summary.

# Detailed Audit Report Audit

## #20-06 City Property Leasing

### Background and Introduction

The City of Sarasota acts as the lessor or “landlord” to lease<sup>2</sup> City-owned properties to third party organizations or “tenants”. These third party organizations are a combination of for-profit entities and non-profit entities. There were approximately 50 active property leases during the scope of this audit. The City classifies the tenants under eight different types of leases with non-profits being the largest category. The leases are administered across three different departments (Facilities, Purchasing and Finance).

Facilities maintains a lease overview spreadsheet to track all of the leases with basic information documented such as name, address, annual renewal dates, etc. Facilities works with the lessees and City management as a liaison to address any changes to leases or updates they may want to do.

Purchasing utilizes contract database software, CADremote3, to track and maintain lessees proof of insurance, original contracts, amendments to contracts and use the software for reports on lease expirations.

The Finance department calculates and invoices tenants based on the terms of their lease agreements.

### Audit Purpose, Scope and Time-period

The purpose of this audit was to provide reasonable assurance that payments made for lease contracts agree with contract terms.

The scope included a review of property leases held by the City of Sarasota. Our audit assessed the City’s monitoring of lessees’ compliance with lease terms. Specifically, determining whether the City received timely and accurate rental payments and other lease requirements. Additionally, we reviewed Purchasing’s maintaining lessees’ proof of insurance.

The audit period was October 1, 2018 to May 31, 2020.

### Audit Objectives

The audit focused on the following objectives:

- 1) Determine whether revenue was received according to the lease.
- 2) Determine whether lessees were held accountable for compliance with lease terms.

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<sup>2</sup> Examples of such agreements include property leases and concession agreements, for this report, we refer to all these agreements as leases.

## Audit Standards

The auditors conducted this audit in conformance 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 that the evidence obtained provides a reasonable basis for findings and conclusions based on the audit objectives.

## Testing Methodology

- Interviewed appropriate personnel from, Purchasing, Facilities and Finance to gain an understanding of the duties of each department;
- Obtained the lease overview spread sheet of property leases from Facilities and reviewed to determine sample size and select sample;
- Leases were reviewed along with any supporting documentation;
- Auditor recalculated rent in accordance with the lease;
- All lease payments from the sample were examined to verify if they were in accordance with the contract and made timely;
- For any leases that had reduced rents, supporting documentation was reviewed, where applicable, and noted why they were given a discount;
- Late payments, if applicable, were verified to see if late fees were added in accordance with the lease;
- Leases that were below market rate were reviewed for supporting documentation to justify the reduced rent and analyzed to see if they were re-evaluated to maintain their status;
- Verified with Finance their calculation of rent, invoicing rent, recording of the rent and deposit of rent as well as how they are aware of any rent adjustments;
- Worked with Purchasing to verify the proof of insurance on file is updated, tracked, and monitored.

To achieve the audit objectives, sampling techniques were utilized to select a random testing sample of the active leases throughout the 20-month testing period.

## Audit Criteria

- City of Sarasota Administrative Regulations and Municipal Codes
- Government Auditing Standards (GAO) “General Standards for Preparing Accounting Records and Financial Standards”
- Florida Department of Revenue – Sales Tax
- Florida State Statues

## Noteworthy Accomplishments

- Facilities and Purchasing utilize CADremote3 software to help monitor lease expirations, renewals, and proof of insurance to keep up to date documents on file.

## Audit Observations and Testing

For **objective one**, we determined that revenue was not always consistently received according to the lease. The leases are not being effectively monitored to ensure receipt of all deliverables which results from unclear monitoring roles among the involved departments. We identified areas for improvement of managing leases and improving controls over the collection of rental payments.

### Observations and Recommendations – Centralization of Lease Administration and Information

Property leases are administered by three departments, Facilities, Purchasing, and Finance. Each of these departments has a role in administering the lease, however there is no one department that has central oversight and responsibility for the administration of the lease. For example, Facilities handles the legal documentation and is the primary contact with the lessees, Purchasing maintains all the proof of insurance documentation and Finance handles the invoicing and collecting of revenue. Facilities does not consult with Finance on the leases regarding the calculation of the payment of rent resulting in issues when Finance does the calculations for any rent increases. Finance only has one employee (not that employee's only job responsibility) who invoices, records, and collects lease payments. When that one person is not available, or the job position is vacant, lease calculations and invoicing is not being done timely. Currently the software that houses the lease contracts and insurance certificates does not include a place for rental calculations resulting in Facilities and Purchasing not being aware or involved in the annual lease calculations. Below are weaknesses identified in the current design of operations –

- Instances of late payments, unbilled late fees, amounts remitted not in agreement to the lease terms or amounts being posted to the accounting system with no supporting documentation for what it is or how it was invoiced.
- One lease included in the sample was calculated and invoiced by Parks and Recreation, with no involvement in the calculation from Finance.
- One lease stipulated \$600 monthly flat fee for utilities in addition to monthly rent. The amount was being paid by the lessee; however, the amount was not being invoiced by Finance nor was Finance making sure the payment was collected.
- There are no reconciliations of rents received to expected rents being performed, contributing to incorrect and delayed lease payments.
- There are no written policies and procedures for administration of property leases.
- The current process Finance uses for invoicing leases is contributing to the above issues. The process involves manually tracking leases on a spreadsheet and then calculating annual adjustments, if applicable. These calculations are not being maintained in a centralized database or a shared drive which complicates other employees picking up a lease and invoicing accordingly, creating a very time-consuming process.

**Internal Audit recommends** that one department take ownership for the overall process of administering leases. Create a shared drive or location to store lease calculations and maintain invoices that is accessible to all three departments. The CADremote3 database appears to be the optimal location as it already houses all lease contracts, insurance forms and lease amendments. Written policies and procedures should be designed to contribute to the proper oversight of lease provisions, including updating the CADremote3 database with terms and rent for each lease contract. The written policy should also establish a reconciliation process to be performed quarterly or bi-annually to determine rents remitted are in agreement with expected amounts.

## Management Response

### **1.1. We recommend that one department take ownership for the overall process of administering leases.**

Leases are primarily managed by Facilities and invoiced/collected by Finance. As a result of this audit, we understand that better coordination is necessary. With the implementation of updating the CADremote3 database, and creating procedures, the coordination effort will be greatly improved. In addition, with the implementation of a new ERP system, a true accounts receivable module will be established.

### **1.2. Create a shared drive or location to store lease calculations and maintain invoices that is accessible to all three departments. The CADremote3 database appears to be the optimal location as it already houses all lease contracts, insurance forms and lease amendments. The current rent information and changes including the calculation method should be stored in the common Database.**

Finance will continue to utilize FMS and Excel for invoicing. When the new ERP system is implemented, this information will be converted to an accounts receivable module. However, the current rent information and changes including the calculation method is stored in the common Database (CAD) by Facilities, with access for Finance Staff.

### **1.3. Written policies and procedures should be designed to contribute to the proper oversight of lease provisions, including updating the CADremote3 database with terms and rent for each lease contract.**

Currently, each lease agreement is unique. To the extent possible, new lease agreements will be standardized to facilitate monitoring and compliance. Finance agrees that there should be written procedures for monitoring and invoicing leases. Both Finance staff and Facilities staff will work on creating procedures in this new fiscal year.

### **1.4. The written policy should also establish a reconciliation process to be performed quarterly or bi-annually to determine rents remitted are in agreement with expected amounts.**

Procedures will be developed for reconciliations of leases that are being invoiced/collected monthly/quarterly/annually.

**1.0 Action Item Owner** – Financial Administration (A/R) and Facilities  
**Committed Resolution Date** – March 31, 2021

## Observations and Recommendations – Sales Tax

Sales tax was deducted from the rent, of a nonprofit, by the Finance department and then paid to the Florida Department of Revenue (FDOR) at a rate of 7%. Three expectations with this: 1) Sales tax was not paid to the City by the lessee and the City should not have calculated sales tax on nonprofit rent per F.S. 212.08 7(p). 2) Sales tax was not deducted on a regular basis, some months it was deducted, other months it was not. 3) In the event sales tax should have been paid, it should not be paid at 7%, instead it should be paid at the sales tax rate for rent of real property which was 6.7% in 2019 and 6.5% in 2020. Testing identified for profit organizations with 6.7% or 7% sales tax calculated on 2020 invoices, sales tax should have been calculated at 6.5%.



**Internal Audit recommends** the City review leases with nonprofit organizations and determine if sales tax should be collected and paid to the FDOR in accordance with F.S. 212.08. If it is determined that no sales tax should be collected or paid then the City should retain a copy of the nonprofits tax exempt certification in the event the City is asked for support for the exemption of tax.

Additionally, tax rates per FDOR should be updated annually and reflected on invoices or payments on leases so that the City does not invoice, collect and pay the incorrect amount of sales tax.

## **Management Response**

**2.1. We recommend the City review leases with nonprofit organizations and determine if sales tax should be collected and paid to the FDOR in accordance with F.S. 212.08. If it is determined that no sales tax should be collected or paid then the City should retain a copy of the nonprofits tax exempt certification in the event the City is asked for support for the exemption of tax.**

Facilities will obtain the Sales Tax Exemption Certificate at the time of signing the lease agreement and for future lease contracts, a clause will be added to the agreement requiring the lessee send an updated copy of the certificate upon renewal. Facilities will monitor this through the CAD system.

**2.2 Additionally, tax rates per FDOR should be updated annually and reflected on invoices or payments on leases so that the City does not invoice, collect and pay the incorrect amount of sales tax.**

Finance is responsible for monitoring any changes in tax rates and will send communication to tenants as well and reflect the new tax rate on the invoices.

**2.0 Action Item Owner** – Financial Administration (A/R) and Facilities

**Committed Resolution Date** – March 31, 2021

For **objective two**, we determined that controls are in place utilizing CADremote3 software to maintain and track all lease renewal dates, certificates of insurance, or other required documentation. Monthly reports are generated with any upcoming expirations and updated accordingly. All leases and required documents (certificates of insurance) were up to date and easily accessed during the audit using the CADremote3 software. We did identify opportunities to improve monitoring of lessees reporting of results, if applicable.

## **Observations and Recommendations – Administration of Below-Market/Nominal Leases**

The City has more than 20 leases considered below-market rate, \$1-\$10 annually. As a condition of below-market or nominal rates some of those leases stipulate that the lessee will provide services to a certain demographic of the population and provide some kind of “performance reports” to the City. For example, one lease includes services to be provided to a certain percentage of clients that have low or moderate incomes. As part of the lease agreement the lessee agreed to perform record keeping functions for income verification purposes to certify that the required percentage of all people receiving services are of low to moderate income. There was no supporting documentation provided during the audit that the City is receiving or verifying that the tenant met the performance expectations included in the lease. This results in the uncertainty about whether the tenants are delivering expected services to

the public. This could lead to the City providing reduced rent to an organization that might not be operating in a manner originally determined for the below-market rent. Additionally, annual leases for \$1 are not being invoiced or collected due to the costs to invoice being greater than the revenue received.

There are other leases that are not at market rate but instead based on memberships and require that non-city residents pay a premium for joining the organization and using the property. The audit sample selected two of these organizations (Sarasota Outboard Club and Sarasota Sailing Squadron) and it does appear these two organizations are providing the City detailed reports identifying membership by city and non-city residents thus allowing Finance to determine that amounts received for rent are in accordance with lease agreements.

**Internal Audit recommends** the City develop procedures to track and ensure that all reporting requirements stated in the leases are met and provided for proper lease oversight. Reports verifying that the tenant is maintaining its status of providing, in this example, services to the people with low to moderate income to support its current reduced rent should be received and reviewed. Additionally, rents included in leases should be invoiced and collected according to the lease document.

### **Management Response**

**3.1 Internal Audit recommends the City develop procedures to track and ensure that all reporting requirements stated in the leases are met and provided for proper lease oversight. Reports verifying that the tenant is maintaining its status of providing, in this example, services to the people with low to moderate income to support its current reduced rent should be received and reviewed.**

Facilities has agreed to monitor reporting requirements and maintain this information in CAD.

**3.2 Additionally, rents included in leases should be invoiced and collected according to the lease document.**

Finance currently invoices all leases as applicable (Note: Some are for \$1 or \$10. This amount is for consideration only. The cost to invoice and collect exceeds the value). Some rents are based on the revenue earned by the tenant. Finance is responsible for obtaining revenue information (tax returns, etc.) to invoice the correct amount. Finance will monitor payments and assess late payments as applicable.

**3.0 Action Item Owner** – Financial Administration (A/R) and Facilities  
**Committed Resolution Date** – March 31, 2021

### **Final Comments**

We would like to thank Facilities, Purchasing and Finance personnel for providing their time and assistance during this audit.