State of California
DEPARTMENT OF TRANSPORTATION

Business, Transportation and Housing Agency

Memorandum

Flex your power!
Be energy efficient!

To: TIMOTHY L. CRAGGS
Acting Chief
Division of Right of Way and Land Surveys

ROBERT MACPHERSON
Deputy District Director
District 4
Right of Way

Date: May 11, 2009

File: P4000-373

From: GERALD A. LONG
Deputy Director
Audits and Investigations

Subject: Final Audit Report on Right of Way Property Management, District 4

Attached is Audits and Investigations' final audit report on the Right of Way Property Management audit in District 4. Your response has been included as part of our final report.

Please provide our office with status reports on the implementation of your audit finding dispositions at 60, 180, and 360 days subsequent to the report date. If all findings have not been corrected within 360 days, please continue to provide status reports every 180 days until the audit findings are fully resolved.

We thank you and your staff for their assistance provided during this audit. If you have any questions or need additional information, please call Laurine Bohamera, Chief, Internal Audits, at (916) 323-7107, or me at (916) 323-7122.

Attachment

c: Will Kempton, Director
Randell H. Iwasaki, Chief Deputy Director
Richard D. Land, Chief Engineer
Clark Paulsen, Chief, Division of Accounting
Laurine Bohamera, Chief, Internal Audits, Audits and Investigations
Barry Cowan, Chief, Real Property Services, Division of Right of Way and Land Surveys
Mark Shindler, District Office Chief, District 4

P4000-373
Right of Way Property Management District 4
May 2009

Gerald A. Long
Deputy Director
Audits and Investigations
California Department of Transportation

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ATTACHMENT

Division of Right of Way (R/W) and Land Surveys Management's and District 4 R/W Property Management's Response to the Draft Report

Summary

Audits and Investigations (A&I) has completed the audit of Right of Way (R/W) Property Management in District 4. We performed the audit to determine if adequate internal controls exist over the rental process, payment collection, and inventory. The scope of the audit was limited to R/W Property Management activities in District 4.

Our audit disclosed that the District 4 R/W Office has adequate internal controls over R/W property management except for the issues noted below:

- Management Oversight Needs Improvement
- Deficiencies in Tenancy Approvals and Documentation
- Inappropriate Use of Rental Offsets
- The Data in the Right of Way Property Management (RWPM) System is Not Reliable
- Improvement Needed in the Recording and Processing of Rental Receipts in the RWPM System

Background

The Division of R/W and Land Surveys administers the statewide program for right-of-way acquisition, real property management, surveying, and R/W engineering for the California Department of Transportation (Caltrans). The R/W Property Management office in District 4 is responsible for managing property held for future transportation projects, excess properties, and employee housing in the nine Bay Area counties, which include Alameda, Contra Costa, Sonoma, Marin, San Francisco, San Mateo, Santa Clara, Solano, and Napa. The District 4 Property Management office is also responsible for maintaining an inventory of State-owned properties, which includes inspecting properties for loss prevention, marketing vacant rentable properties, establishing tenancies, arranging property maintenance, and terminating tenancies. The property management budget for the District 4 R/W office in fiscal year 2007-08 was $2.95 million, and for fiscal year 2008-09, it is $3.15 million.

Objectives, Scope, and Methodology

We conducted an audit of the R/W Property Management office in District 4 to determine the adequacy of internal controls over the property management function.

The audit was performed in accordance with the International Standards for the Professional Practice of Internal Auditing. The objectives of the audit were to determine whether:

- The property inventory is current and accurate.
- Only available rentable properties are rented.

Objectives, Scope, and Methodology (Continued)

- A valid rental agreement and all required documents exist and are included in the property rental files.
- Rental payments are collected in accordance with Caltrans' accounting policies.

The audit covered the period January 1, 2007, through May 31, 2008. The audit focused on internal controls and procedural compliance as they related to the R/W Property Management functions. The audit included tests which the auditors determined were necessary to achieve the above audit objectives.

Conclusion

The audit disclosed that internal controls over District 4 R/W Property Management are generally adequate, except for the issues noted below:

- Management Oversight Needs Improvement
- Deficiencies in Tenancy Approvals and Documentation
- Inappropriate Use of Rental Offsets
- The Data in the RWPM System is Not Reliable
- Improvement Needed in the Recording and Processing of Rental Receipts in the RWPM System

Views of Responsible Officials

We requested and received a response to our findings from the Acting Chief, Division of R/W and Land Surveys, and the Deputy District Director, R/W Property Management in District 4. These officials have, in general, acknowledged the findings and recommendations. Please see the Attachment for a complete response.

GERALD A. LONG
Deputy Director
Audits and Investigations

June 17, 2008
(Last Day of Audit Field Work)

FINDINGS AND RECOMMENDATIONS

Finding 1 – Management Oversight Needs Improvement

Our review found that the overall administration and management of the District 4 Right of Way (R/W) Property Management function needs improvement in enforcing the provisions contained in the Right of Way Property Management (RWPM) Manual. Specifically, our review found the following:

- Several property files were missing evidence of the property manager's or designee's review or were missing required documentation altogether.
- Numerous files were missing proof that properties had been inspected by a property manager or designee, when appropriate.
- Inappropriate use of rental offsets was allowed to continue with management knowledge and consent.
- Some key R/W agent functions were not adequately separated to protect State assets. For example, R/W agents set up the tenancy account in the RWPM system and were allowed to collect the security deposit and the first month's rent.
- The confirming process to verify tenant occupancy dates, rental rates, and deposits is not being completed.

The RWPM Manual has comprehensive policies and procedures related to all facets of R/W. Chapter 11 of the RWPM Manual addresses property management requirements.

Staff's compliance with policies and procedures is key to achieving proper protection of the State and its assets. Lack of adherence to these policies and procedures puts Caltrans and the State at risk for loss of revenues and assets. In addition, lack of adherence to policies and procedures could result in inappropriate activities by State personnel or its vendors.

Senior R/W agents are expected to assign, supervise, review, and approve the work of the R/W agents. During the course of our audit, we found that this unit has had turnover and, as a result, had vacancies at this level, which may be a contributing factor to the existing condition.

The specific findings and recommendations are presented in Findings 2-4 below.

Recommendation

We recommend that District 4 R/W Property Management improve overall administration and management of the property management

Recommendation (Continued)

function by enforcing the policies and procedures described in the RWPM Manual.

District 4 R/W Property Management Response

District 4 R/W Property Management acknowledges the finding and recommendation and will enforce the policies and procedures as described in the R/W Manual.

Finding 2 – Deficiencies in Tenancy Approvals and Documentation

Forty rental files consisting of thirty-three occupied rentable properties and seven vacant rentable properties were reviewed. We observed that the files did not always have the appropriate approvals, and had incomplete or missing documentation.

Specifically, we found the following:

- Twenty-four percent (8 of 33) of occupied rentable properties were missing the property manager's or authorized person's review and approval on maintenance requests. In addition, thirty-three percent (11 of 33) of occupied rentable properties had maintenance requests/invoices with no evidence of contract manager review. The RWPM Manual Chapter 11, section 11.10.11.02, states, if maintenance work is required, the agent shall enter a full description of the job, including a cost estimate, on the RWPM Maintenance Screen and submit it to the property manager or authorized person for approval. Upon approval of the request, the agent shall file a hard copy of the Maintenance Request Screen in the rental folder.

- Twenty-seven percent (9 of 33) of occupied rentable properties had no fair market rent determination documentation included in the file. The RWPM Manual Chapter 11, sections 11.05.01.00 and 11.06.02.00 explain that for nonresidential rentals . . . and residential rentals, the property manager shall annually review the rental rate and maintain an up-to-date sampling of fair market rental rates for similar properties in the vicinity of the State-owned properties.

- Twenty-four percent (8 of 33) of occupied rentable properties had no documentation of a property occupancy inspection (move-in inspection), subsequent annual property maintenance inspection, or were missing the date and signature of the agent and tenant. Chapter 11 in the RWPM Manual describes the requirements for property inspections. Specifically, section 11.07.17.00 states, "When a tenant moves into or out of a residential property . . . Residential Property Occupancy and Vacancy Inspections shall be completed and signed by the agent." In addition,

Finding 2 – (Continued)

section 11.10.06.00 provides that all property management agents shall be responsible for periodically inspecting and documenting every rental account under their control.

- Twelve percent (4 of 33) of occupied rentable properties had missing or expired tenant documentation, such as insurance policies, rental applications, and rental agreements. The RWPM Manual Chapter 11, sections 11.11.01.00 and 11.11.04.00 require a liability insurance policy for leases or rental agreements where extraordinary liability features are present. The Certificate of Insurance form from the tenant's or lessee's insurance carrier is kept in the rental file with the rental agreement or lease.

- Fifty-seven percent (4 of 7) of vacant rentable properties had no documentation of a property manager's or designee's property move-out inspection or documentation of any required subsequent inspections. Section 11.09.03.01 of the RWPM Manual states, "When a tenant vacates, the agent shall thoroughly inspect and secure the property as soon thereafter as possible . . . , and prepare the necessary accounting documents to close the tenant's file." Additionally, section 11.09.04.00 states, "Field inspections of occupied property shall be made at least annually."

- Seventy-one percent (5 of 7) of vacant rentable properties were not advertised on the current monthly vacancy listing. The RWPM Manual Chapter 11, section 11.07.04.00, states that the agent should use newspaper advertisements for residences . . . to attract tenants. Posting of improved properties with advertising signs may be desirable in some cases and is at the district's discretion.

Caltrans is at risk for loss of State revenues when unauthorized property maintenance is allowed, idle properties exist, and tenant qualifications for rentals are not fully met. In addition, lack of inspection documentation could result in inappropriate rental activities. For example, A&I found in a separate review that a R/W agent rented a property for several months without having an approved rental agreement in file.

According to R/W District 4 management, this unit has had high turnover which has contributed to these conditions. In addition, the lack of formal desk procedures makes it difficult for R/W agents to manage tenant files consistently.

Recommendation

We recommend that District 4 R/W Property Management:

1. Ensure that R/W agents follow the requirements identified in the RWPM Manual when managing their assigned rental properties.

2. Ensure the property manager or designee inspect State-owned properties as required to ensure the assets of the State are safeguarded against loss.

District 4 R/W Property Management Response

District 4 R/W Property Management stated that since March 7, 2008, all maintenance requests are submitted to the Senior or Supervising R/W Agent and include an estimated cost of work to be performed. In addition, vacant properties are inspected by the Senior or Supervising R/W Agent at least once a month to ensure that all properties occupied have rental accounts. For a complete response, please see the Attachment.

Finding 3 – Inappropriate Use of Rental Offsets

The RWPM Manual allows rental offsets for minor repairs, maintenance, or emergency repairs for health and safety reasons, which are performed at the renter's expense. However, we found two rental files in which District 4 R/W Property Management staff allowed the use of rental offsets regularly for major repairs and non-emergency maintenance. In addition, the rental files did not contain any documentation to support the need for using rental offsets.

Specifically, we found:

- Over the period of 16 months, one of the tenancy files had rental offsets totaling $78,204. This included a rental offset of $13,400 for the tenant to install a sewer system that would connect to the city's main line. The total also included a $15,686 offset to have the tenant install a water main, electrical lines, and sewer lines on the property. In this last offset, there appear to be duplicate invoices submitted by the tenant for reimbursement.

- The other rental file had four rental offsets over seven months totaling $93,041. One of the offsets totaled $38,189 and was used for the repair and remodel of a warehouse and office building; and to install plumbing and sewer lines on the property.

- Due to the nature in which tenants submitted invoices, it was difficult to determine whether these invoices were legitimate expenses. For example, one invoice submission consisted of a Home Depot credit billing statement, with no detailed supporting documentation for the amounts on the statement. Upon further

Finding 3 – (Continued)

review, we determined that the entire balance on the Home Depot credit billing statement was paid as part of a $12,773 rental offset. In addition, there were other invoices submitted for costs that did not appear to be maintenance related, including gasoline and tires.

- The rental offset agreements were generally dated the same day the tenant was required to have the work completed and furnish the paid bills to Caltrans. As a result, we could not conclude that the rental offsets were pre-approved.

The RWPM Manual Chapter 11, section 11.10.15, states:

- Occasionally, rental offsets may be appropriate for certain repairs or maintenance. However, such offsets should only be used as an exception and not routinely. There are other alternatives to using rental offsets that are discussed in detail in Chapter 11 including, service contracts, CAL-Card, and non-credit card processes.
- Rental offsets should be limited to minor repairs and maintenance, or emergency repairs for health and safety reasons.
- Generally, a tenant cannot hire a contractor to do the work and receive an offset. This violates Caltrans contracting policy.
- Before any work commences, the property manager or supervising R/W agent shall approve the amount of the allowance.
- The reason for using a rental offset must be documented in the rental file.

District 4 R/W Property Management did not comply with the above-referenced requirements contained in the RWPM Manual. As a result, the district may have paid for duplicate invoices and unallowable costs, and may have violated Caltrans contracting policies.

According to District 4 R/W Property Management, it was faster to use rental offsets for maintenance and repairs than to use the contracting process. In addition, the management in District 4 R/W Property Management felt that there was a cost benefit to the State by using rental offsets instead of other methods to rehabilitate the properties.

Recommendation

We recommend that the management and staff in District 4 R/W Property Management adhere to the policies and procedures in the RWPM Manual and Caltrans' contracting policies.

District 4 R/W Property Management Response

District 4 R/W Property Management feels that the situation described in the finding is an isolated instance. The District will adhere to the policies and procedures as described in the RWPM Manual in the future.

Finding 4 – The Data in the Right of Way Property Management (RWPM) System is Not Reliable

The RWPM system does not contain current and accurate information, thus making the data in the system unreliable. For example, we selected a property file for review and found the most current rental agreement had the monthly rent as $7,000. However, in the RWPM system, the monthly rental rate was $10,000. Furthermore, the property file contained a lease that renewed on August 1, 2006; however, the RWPM system still showed the lease start date of January 1, 1994. In another example, a tenant lease agreement and the RWPM system identified that a $2,500 security deposit was collected while the accounting records showed no evidence of receipt and deposit.

During our efforts to define the universe of parcels and/or properties that District 4 R/W manages, we concluded that due to inconsistencies of the data in the RWPM system, the universe was not attainable. As a result, we could not be certain that we selected our samples from all eligible parcels and/or properties. In addition, the inconsistencies result in inefficiencies in the property management system, causing additional State resources to be used to accomplish the property management goal.

According to the General Accounting Office (GAO)-03-273G section 2, data are reliable when they are (1) complete (they contain all of the data elements and records needed for the engagement) and (2) accurate (they reflect the data entered at the source or, if available, in the source documents). A subcategory of accuracy is consistency. Consistency refers to the need to obtain and use data that are clear and well-defined enough to yield similar results in similar analyses.

The data in the RWPM system is not reliable due to the following:

- Since the implementation of the RWPM system in the 1980's, R/W agents have not consistently input property attributes into the system.
- There are no controls in place to ensure that the RWPM system is current and accurate.

Recommendation

We recommend that the Division of R/W and Land Surveys management:

1. Provide training and communicate with the districts the importance of accuracy and consistency in recording property inventory data into the RWPM system to ensure consistency.

2. Develop and implement procedures and controls to ensure that data in the RWPM system is current and accurate.

Division of R/W and Land Surveys Management Response

The Division of R/W and Land Surveys Management stated that data integrity is a high priority and is continually emphasized to the Districts. It currently requires that District Directors and R/W Managers certify the integrity of their data and it is one of the review criteria of the Quality Enhancement Joint Reviews.

Finding 5 – Improvement Needed in the Recording and Processing of Rental Receipts in the RWPM System

Currently, the RWPM system is designed to automatically generate a late fee when the monthly rental receipt is not posted to the system by the 10th of each month, even though the rent has been received timely. The system is also designed to automatically allocate collections which may include the guarantee deposit, utilities, damages, rent, etc. . . . in a pre-determined hierarchy when the R/W agent has not specified how the collection is to be applied by the 20th of each month. This results in inaccurate tenant account information and requires an adjustment form to be prepared and approved by property management staff and then processed by the Division of Accounting (DofA) to either reverse the late fee or properly apply the rental collection.

Of the 16 new tenant rental files reviewed in the RWPM system, we noted that five files (31 percent) have several reversing or correcting entries as follows:

- Thirteen percent (2 of 16) of the rental files had reversed late fee entries because the RWPM system automatically generated late fees when the rent collections did not post by the 10th of the month.

- Nineteen percent (3 of 16) of the rental files had correcting entries because the RWPM system incorrectly allocated the collections.

District 4 property management staff indicated that this has been a long-standing condition and that as much as 10 to 15 percent of staff time is spent initiating and approving such entries, which is not an effective use of staff time.

Recommendation

We recommend that the Division of R/W and Land Surveys work with DofA to review existing processes and explore the possibility of modifying the RWPM system to minimize the need for adjusting entries and improve operational efficiency.

Division of R/W and Land Surveys Response

The Division of R/W and Land Surveys Management agrees that the recording and processing of rental receipts is an ongoing concern. It will put together a multifunctional team from the Division of R/W and Land Surveys, the Division of Accounting, and representatives from Districts 4 and 7 to resolve this issue.

Audit Team

Laurine Bohamera, Chief, Internal Audits
Juanita Baier, Audit Supervisor
Michelle Mai, Auditor
Kathy Brooks, Auditor
Dawn Beyer, Auditor

ATTACHMENT

Division of Right of Way (R/W) and Land Surveys Management's and District 4 R/W Property Management's Response to the Draft Report

Memorandum

Flex your power!
Be energy efficient!

To: GERALD A. LONG
Deputy Director
Audits and Investigations

Date: May 1, 2009

File: P4000-373

From: TIMOTHY L. CRAGGS
Acting Chief
Division of Right of Way and Land Surveys

Subject: Response to Draft Audit Report on Right of Way Property Management District 4

The following is provided in response to the Draft Audit Report on Right of Way Property Management (RWPM) District 4 (District) dated February 10, 2009.

Finding 1

Recommendation: We recommend that District 4 RWPM improve overall administration and management of the property management function by enforcing the policies and procedures described in the RWPM Manual.

Response: The finding of the audit is noted and the District Management is enforcing the policies and procedures described in the Right of Way (R/W) Manual.

Finding 2

Recommendation: We recommend that District 4 R/W management:

1) Ensure that R/W agents follow the requirements identified in the RWPM Manual when managing their assigned rental properties.

Response: The District is doing the following to be in compliance with policy and consistent with the recommendation:

- Since March 7, 2008, all maintenance requests submitted to the Senior or Supervising R/W Agent include an estimated cost of work to be performed.
  - If the request is approved the contractor is then instructed to proceed.
  - The agents and sometimes the senior inspect the work.
  - If satisfactory the invoice is attached to a new copy of the maintenance request and is submitted to the senior with the rental file and diary for approval.
  - The senior then approves the electronic copy of the request for payment and initials the hard copy.

- With regard to rental surveys, agents currently review rates using Craig's Lists, and other published data to determine a market rate.
  - A master file of current rents is kept on file for future reference.
  - Supporting rental rates are documented in the file as a part of the yearly inspection.

- Move-in inspections are performed and submitted with each new rental file along with the signed lease and deposit/rent check to the senior.
  - Move out inspections are submitted along with the file to the senior at the time of vacancy.
  - The senior closes out the account in RWPM. Only the Seniors approval activates or de-activates a tenancy. The senior periodically checks the agent's account for inspection dates.

- Leases become month-to-month rental agreements after the expiration of the original lease term, therefore they technically do not expire.
  - New agreements now state month to month as the term and don't require an expiration date.
  - Evidence of insurance polices continue to be a problem. Tenants' insurance companies sometimes neglect to send documentation of coverage to the Department. Follow-up requests for evidence of insurance are documented in the file.

- Craig's List is used for vacant Property Listings.

Recommendation: We recommend that District 4 R/W management:

2) Ensure that property manager or designee inspects State-owned properties as required to ensure the assets of the State are safeguarded against loss.

Response: The Senior or Supervising R/W Agent inspects vacant properties at least once a month to ensure that all properties occupied have rental accounts.

Finding 3

Recommendation: We recommend that the management and staff in District 4 RWPM adhere to the policies and procedures in the RWPM Manual and Caltrans' contracting policies.

Response: The situation identified in the audit was an isolated instance and the District will adhere to the policies and procedures in the future.

Finding 4

Recommendation: We recommend that the Division of R/W and Land Surveys Management:

1) Provide training and communicate with the districts the importance of accuracy and consistency in recording property inventory data into the RWPM system to ensure consistency.

Response: The Department recognizes that the integrity of the data in not only this system but all Right of Way systems is critical to the Department's credibility. The Division of Right of Way and Land Surveys embarked on a program to ensure data integrity by requiring District Directors and Right of Way Managers to certify the integrity of their data. Data integrity is a review criteria for each Quality Enhancement Joint Review (QEJR) performed. It continues to be a high priority and is continually emphasized.

The RWPM system is a fairly intuitive system. Manuals and guide books are available to assist the user in its use. The Division of Right of Way and Land Surveys (R/W&LS) provide training on the use of the Oracle Discoverer also, which is the best tool we have available to identify incorrect or anomalous data.

2) Develop and implement procedures and controls to ensure that data in the RWPM system is current and accurate.

Response: The RWPM is an old legacy mainframe system developed in the late 1980's. It has very limited checks built into it to prevent erroneous data from being entered. The ability to make substantive changes to the RWPM is extremely limited. Recently the Department initiated the use of Oracle Discoverer as a tool to help manage the program, and assist the Senior in identifying incorrect data and other anomalies. Ultimately it is the responsibility of the District to ensure their data is current and accurate. The Division of R/W&LS provides tools, continues to stress the importance of current and accurate data, reviews data on a regular basis for accuracy, and reviews data integrity through its QEJR process. There are 890 data elements in the RWPM. When multiplied by the number of parcels in the system, the amount of data is significant. One hundred percent accuracy is not achievable.

Finding 5

Recommendation: We recommend that the Division of R/W&LS work with Division of Accounting to review existing processes and explore the possibility of modifying the RWPM system to minimize the need for adjusting entries and improve operational efficiency.

Response: The concerns expressed in the audit regarding recording and processing of rental receipts is an ongoing concern. The Division of R/W&LS will put together a multifunctional team from the Division of R/W&LS, the Division of Accounting, and representatives from both District 4 and District 7 R/W to try to resolve this issue.

c. BCowan
LBohamera
JBaier