

FINAL

MANAGEMENT AUDIT REPORT

OF

THE MANAGEMENT OF

THE HISTORIC DISTRICT IMPROVEMENT COMPANY
MASTER DEVELOPMENT AGREEMENT

REPORT NO. 01-106CITY



CITY OF ALBUQUERQUE
OFFICE OF INTERNAL AUDIT



Internal Audit

September 23, 2004

City of Albuquerque
P.O. BOX 1293 ALBUQUERQUE, NEW MEXICO 87103

Internal Audit Committee
City of Albuquerque
Albuquerque, New Mexico

Audit: Management of the Historic District Improvement Company Master Development Agreement
Citywide
01-106CITY

FINAL

INTRODUCTION

The Office of Internal Audit reviewed the City management of, and vendor compliance with, agreements with the Historic District Improvement Company, LLC (HDIC). HDIC has an agreement with the City for the master development of the Alvarado Transportation Center.

This audit and its conclusions are based on information provided through interviews, tests and reviews of current procedures.

AUDIT OBJECTIVES

The objectives of our audit are to determine:

- Is the City managing the agreement with HDIC and ensuring that the objectives of the agreement are met and risks to the City are minimized?
- Is HDIC complying with the terms of the agreement with the City?

SCOPE

Our audit did not include an examination of all the functions, transactions and activities related to the City's agreement with HDIC. Our audit testwork was limited to the documentation and other information that was available related to the City and its relationship with the organization. The audit

covered the period from the inception of the agreements and leases through the most current documents available; in most cases through December 31, 2003.

The audit was conducted in accordance with Government Auditing Standards, except Standard 3.49, which requires an external quality review.

METHODOLOGY

We identified the risks to the City associated with the agreement with HDIC. We examined the controls in place at the City to mitigate risks. This was accomplished through review and analysis of available documents and interviews with key personnel.

We identified the obligations and performance requirements for HDIC as specified in the agreement, Ordinances and approved plans and budgets. We verified compliance through examination and analysis of available documents and interviews with key personnel at the City, and HDIC.

HDIC Background Information

The City and HDIC, LLC (HDIC), entered into the Master Development Agreement for the Alvarado Transportation Center (Master Development Agreement) on November 29, 1999. The purpose of the Master Development Agreement is to:

“ . . . effectuate the Alvarado Metropolitan Transportation Redevelopment Plan (‘Redevelopment Plan’) for the Alvarado Metropolitan Redevelopment Project (‘Project’) by providing for the disposition and redevelopment of certain real properties included in the boundaries of the Alvarado Transportation Metropolitan Redevelopment Area (‘Project Area).”

As part of the project, the City will convey some of the parcels of real property in the Downtown area to HDIC. Parcels are conveyed at “fair value” as provided for by City ordinance. Other parcels are to be purchased by HDIC from the City, for the City’s cost to acquire the same.

The City Council approved the selection of HDIC as the Master Developer for the Project Area. As the Master Developer, HDIC may enter into contracts with third party entities in order to form a “Building Developer” to implement the projects. For example, HDIC Theater Block, LLC (Theater Block) was formed on November 16, 2000, by the HDIC and other parties as a “Building Developer” to purchase, own, develop, operate, lease, sell and otherwise deal with real property related to the Master Development Agreement. HDIC Gold Avenue, LLC (Gold Lofts) was formed to build a high-end residential project. Gold Lofts is owned by HDIC and will be built on property conveyed by the City.

The City does not receive any net operating proceeds in project years one through five other than what the Master Development Agreement refers to as “preferred returns.” This is a 1% preferred return from net operating income derived from the project on a non-cumulative annual basis.

In project years six through 12 the City receives 25% of any profits. In project years 13 through 25 the City receives 50% of any profits. Project years are determined on a parcel-by-parcel basis rather than for the overall redevelopment project. Distributions to the City cease in year 20 or upon repayment of 125% of the City’s Capital Account, whichever occurs first.

In the event HDIC defaults under project loan documents or is otherwise unable to perform under the Master Development Agreement or any Joint Venture Agreement, the City may be substituted for HDIC in the loan documents with a special warranty deed delivered to the City for the applicable real estate parcel.

In April 1999, Enactment No. 47-1999 created an “Alvarado Transportation Center Project Task Force” that was “. . . charged with reviewing all aspects of this project. This Task Force shall consist of one or two City Councillors (sic), the Chief Administrative Officer, the Director of Council Services and the Chair of the Albuquerque Development Commission. This Task Force shall be charged with making recommendations to the City Council on the Alvarado Transportation Center Projects.”

Albuquerque Development Services, a division of the Planning Department, performs some contract administration functions relating to the Master Development Agreement between the City and HDIC.

In July 2002, Albuquerque Development Services was moved from the Department of Family and Community Services to the Planning Department. The previous managers of Albuquerque Development Services, and its subsequent Acting Manager, were involved in the preparation of the Request for Bid that resulted in the Master Development Agreement between the City and HDIC.

For each parcel of real property being redeveloped, if there is a construction cost overrun requiring additional funds, HDIC is exclusively obligated to provide such additional debt or equity capital to complete the construction. The City has relied upon the obligations of HDIC for performance without requiring a surety bond or other similar agreement or arrangement. In connection with this reliance, HDIC agreed that it will not sell or pledge more than 49% ownership of HDIC without City Council approval and that sale or transfers of real estate parcels prior to completion may only occur with approval by the City Council.

The Master Development Agreement also requires that HDIC develop a labor force plan. The plan would outline the total number and types of full time equivalency jobs created throughout the project, together with anticipated wages and personnel hire dates for each employment position. The plan was to be submitted to the City within 90 days of the execution of the agreement.

HDIC is owned in part by the Downtown Action Team, which has a 2.86% ownership in HDIC. In addition to the DAT's ownership interest in HDIC, the other two principals are a charitable foundation (McCune Charitable Foundation – 20% ownership) and a for-profit corporation (Arcadia Land Company – 77.138% ownership). Appendix A shows the various organizations and their ownership.

FINDINGS

The following findings concern areas that we believe could be improved by the implementation of the related recommendations.

1. THE TASK FORCE SHOULD CLARIFY THE RESPONSIBILITY FOR MANAGEMENT AND MONITORING OF THE MASTER DEVELOPMENT AGREEMENT.

The City Council approved Resolution F/S R-190 enactment 47-1999, "Providing a Policy for the Process of Developing the Alvarado Transportation Center Project." The resolution established the Alvarado Transportation Center Project Task Force (Task Force), which was charged with reviewing all aspects of the project and making recommendations to the City Council on the Alvarado Transportation Center Projects.

The Master Development Agreement is between "the City of Albuquerque, a municipal corporation ('City') ...and the Historic District Improvement Company ('HDIC'), a limited liability company...." Section 105 of the Master Development Agreement states that HDIC will provide the City with an annual written report describing the actual progress of the construction of the project. The report is to be delivered to Albuquerque Development Services.

The Master Development Agreement, Section 201.e. gives the Task Force authority to approve all amendments to the agreement, which may then be executed by the CAO. Only those amendments that require funding appropriations must be approved by the City Council. Throughout the Master Development Agreement, various items are identified that must be provided to the "City" without specifying who or what department or division the required items will be delivered to.

According to Albuquerque Development Services personnel, there was confusion regarding who was responsible for the regular monitoring of the agreement with HDIC. At the inception of the agreement, a Deputy CAO was the primary contact with HDIC. When he retired, his position remained vacant. The responsibility for management and monitoring of the agreement was not specifically delegated to another City employee.

Many of the documents and reports required by the Master Development Agreement were not provided to the City prior to the start of our audit, although they should have been provided earlier at specified dates or intervals. (Documentation was provided after requested by Internal Audit, as discussed in the following findings.) The previous Albuquerque Development Services Division Manager and other Division personnel were involved in the negotiation of the Master Development Agreement and should have been aware of its requirements. However, they indicated that they believed that the Task Force was responsible for the administration of the agreement. As a result, Albuquerque Development Services' involvement in the agreement was limited to the transfer of City-owned land to HDIC. The Task Force members are high-level personnel and may not have the time necessary for the ongoing administration of the agreement.

The Master Development Agreement requires that HDIC provide the City with financial information regarding the projects. However, Albuquerque Development Services does not currently have personnel who are qualified to review and analyze the financial statements of HDIC in order to ensure that the City's interests are protected. The HDIC financial statements relate to real estate development, which is a highly specialized industry. The financing mechanisms used for the Alvarado Transportation Center projects are also unusually complex, and can have a potential impact upon the City's interest.

RECOMMENDATION

The Task Force should ensure that responsibility for administration and monitoring of the Master Development agreement is clarified.

In order to ensure that the City's interests are protected, the Task Force should ensure that the City personnel who review and analyze the HDIC financial information have in-depth knowledge of real estate development financing and accounting.

EXECUTIVE RESPONSE FROM THE TASK FORCE

"The Task Force agrees that the Master Development Agreement requires more monitoring than has been provided in recent years. While it would be preferable, and perhaps more efficient, for Albuquerque Development Services to both administer and monitor the Agreement, that may not be a viable solution based on available staffing. Albuquerque Development Services (ADS) and the Department of Finance and Administration (DFAS) have been working collaboratively for some time now on this matter. In any case, the City will identify a Contract Recorder and charge

the Contract Recorder, ADS, and DFAS with the responsibility for monitoring and administering the Master Development Agreement.

“The Task Force agrees that real estate development is a highly specialized field and that the Master Development Agreement itself, and the projects it contemplates, are complex. It seems unlikely that the City would be able to hire a person with the necessary level of expertise to do nothing but monitor the Agreement. Rather, the Task Force will work with the Administration to identify funding to provide contractual assistance for a Financial Auditor as necessary to support the Internal Audit department in assessing and analyzing HDIC financial information and projects.”

2. THE TASK FORCE SHOULD FORMALIZE THE REQUIREMENTS FOR MAINTAINING THE RECORDS OF THE CITY CAPITAL ACCOUNT.

HDIC is required by the Master Development Agreement to maintain records of the City's Capital Account. The City's Capital Account consists of the fair market value of each City parcel conveyed to HDIC, the amounts of HDIC's tax abatements, the infrastructure costs paid by the City under the agreement, and the amount of any operating deficit for a parking structure incurred as a result of the guarantee of parking spaces. The final cumulative total of the City's Capital account has been estimated at between \$8 and \$12 million when all property has been transferred and other City paid costs are included.

It is important that accurate records be kept of the City's Capital Account, because the amount of money that is repaid to the City from profits of the project is dependent upon the total amount of the City's Capital Account. The maximum distribution to the City will be 125% of the value of the City's Capital Account.

The December 31, 2002 and 2003, financial statements for the Theater Block discuss the City's Capital Account in Note 11. The 2002 financial statements only include the \$1.37 million of land transferred in 2002 as the City's capital account. The 2003 financial statements include the value of land and infrastructure costs, but do not include the operating deficit for the parking structure.

As of February 28, 2002, the City's Capital Implementation program records reflect that the City had \$328,231 of expenditures and an encumbrance for \$103,134; relating to infrastructure costs.

The August 20, 2003, HDIC business plan states, “The actual experience of the first full year of operations by the Transit Department has been approximately \$75,000 loss.” Albuquerque

Development Services personnel did not know which 12-month period this statement referred to or from whom HDIC obtained this information.

In February 2004, because of an audit request, HDIC provided the City with an estimate of the value of the City's capital account as of July 1, 2003. The HDIC letter to the City stated, "Based on HDIC's calculations the City Capital Account value on 7/1/2003 was \$1,765,455." Albuquerque Development Services personnel prepared an estimate of the City's capital account, and sent a March 5, 2004 memorandum to HDIC, which stated, "Accordingly, the value of the City Capital Account as of June 30, 2003 is \$1,820,596."

Although the Master Development Agreement states that HDIC is to maintain the record of the City's Capital Account, the information needed to determine the losses from operation of the parking garage must be obtained from the City. Albuquerque Development Services informed HDIC by a memorandum dated March 5, 2004, that "... in the future the City will provide by December 31 of each year, data for the end of the City's fiscal year, June 30. We will also recommend that the final figures be reviewed and accepted by the Alvarado Task Force within 90 days of each calendar year." However, this arrangement has not yet been formalized by an amendment to the agreement or a Memorandum of understanding between the parties.

The Capital Account is not recorded on the Theater Block financial statements. The notes to the financial statements refer to "the accompanying consolidated financial statements" for HDIC. HDIC did not provide the City with a financial statement for HDIC itself until Internal Audit obtained a Legal Opinion stating that the consolidated statement was necessary to complete an Internal Audit. On June 25, 2004, HDIC provided Internal Audit the consolidated financial statements for HDIC for the years ended December 31, 2000, 2001, 2002 and 2003. Previously, HDIC has only provided the City with financial statements for the Theater Block and the Gold Lofts projects.

According to HDIC officials, HDIC and the City agreed that financial statements for the individual projects were all that would be required. As evidence of the agreement, HDIC provided a letter dated September 2003, from the HDIC Chief Operating Officer to Albuquerque Development Services. The letter states, "As we discussed in our meeting last week with [the Associate Planning Director], HDIC will provide Albuquerque Development Services an annual financial statement on each project within the Alvarado District as they come on line." There is no evidence that the Task Force agreed to modify the reporting requirement. Providing only project financial statements does not appear to comply with the contractual requirement for "Master Developer" annual financial statements.

The City and HDIC have both understated the City's Capital Account by more than \$75,000. In December 2001, a construction contractor performed work on the transformer vault on 1st and Gold Street. The two entities using power from the vault are 1) the City of Albuquerque for the parking structure and Alvarado Transportation Center and 2) HDIC for the Theater Block. The utility company estimated that the Theater Block would use 65% the power from the transformer vault.

The CAO sent the Chief Operations Officer of HDIC a letter dated December 31, 2001, stating that the total funds available for infrastructure costs would be reduced by HDIC's prorated share of the costs of the transformer vault, which was \$75,161. The City paid the entire cost directly to the contractor. Although the Capital Improvement Program Application for Payment forms show the decrease in the funds available to HDIC for infrastructure improvements, neither HDIC nor the City included the \$75,161 in the City's Capital Account.

RECOMMENDATION

The Task Force should formalize the requirements for maintaining the records of the City Capital Account. The arrangement should be included in either an amendment to the agreement or a Memorandum of understanding between the parties.

The Task Force should enforce the requirement that financial statements are provided for the Master Developer, not just the individual projects.

The Task Force should inform HDIC and the Department of Finance and Administrative Services that the City's Capital Account has been understated by \$75,161.

EXECUTIVE RESPONSE FROM THE TASK FORCE

"The Task Force believes the City Department of Finance and Administrative Services should be assigned the responsibility of maintaining the records of the City Capital Account. HDIC should continue to maintain a record of the City Capital Account for purposes of its own internal accounting. Any discrepancies between the balances at year end should be reconciled to the satisfaction of the Task Force. Procedures will be put in place by the City to ensure that an annual reconciliation of the City Capital Account is done on a timely basis and submitted to the Task Force.

"With respect to the requirement to provide financial statements, it appears

that as with so many other vague provisions of the Master Development Agreement, HDIC has been successful in securing an interpretation that is favorable to HDIC without necessarily obtaining the understanding or concurrence of the current Task Force. The Task Force will attempt to clarify the provisions of the Master Development Agreement through amendment of the Development Agreement. This amendment is subject to agreement by HDIC.

“The Task Force will request that the Department of Finance and Administrative Services make it a priority to review and determine the correct balance for the City Capital Account. Both the HDIC and the appropriate department(s) of the City will be notified of that determination.”

3. THE TASK FORCE SHOULD ENSURE THAT HDIC COMPLIES WITH THE REPORTING AND DOCUMENTATION REQUIREMENTS OF THE MASTER DEVELOPMENT AGREEMENT.

The Master Development Agreement requires that HDIC deliver various reports and documents to the City throughout the life of the projects. Some documents were provided to the City, but not in a timely manner. Other documents were not provided to the City until they were requested as a part of our audit.

A. Letters of Commitment for Construction Financing

Section 303 of the Master Development Agreement states:

"The Master Developer shall provide the City with a (sic) irrevocable letter of commitment for the construction financing, which shall include a statement of the Lender's requirement for Master Developer's equity capital investment and any other conditions of the commitment, for the improvements to be made to each City parcel . . .

“For each City Parcel being conveyed to the Master Developer, Lender's certification shall be provided to the escrow agent, and to the City, that the Master Developer: (1) has complied with and satisfied all required terms and conditions contained in the irrevocable letter of commitment, including any and all equity capital requirements”

In June 2000, Albuquerque Development Services transferred a piece of property with an appraised value of \$1.37 million to the HDIC for the Theater Block project. According to the Master Development Agreement, a lender's certification should have been provided to the City stating that HDIC had complied with all of the terms and conditions in the associated lender's letter of commitment.

Albuquerque Development Services personnel did not have a copy of the lender's certification. In September 2002 Albuquerque Development Services requested and received a letter from the lender which stated, "In regards to Section 303 (b) of the Development Agreement, please use this letter at (sic) confirmation that HDIC has 'satisfied all required terms and conditions contained in the irrevocable letter of commitment . . .'"

B. Financing Certifications

Section 609 of the Master Development Agreement states:

"Master Developer agrees to pay any Lender providing funding for the Project, or a part thereof, on or before the due date, any amounts required to be paid to Lender and to comply with all terms and conditions of the mortgage or other security instrument delivered to such Lender. Master Developer shall execute and furnish a certificate to the City, one hundred eighty (180) days after execution and delivery of the note evidencing the loan and each succeeding one hundred eighty (180) days thereafter, that the loan is in good standing and that no default exists in any of the terms or provisions thereof."

Albuquerque Development Services personnel were not able to provide the required certificates of HDIC's compliance with loan agreements. In February 2004, at the request of Albuquerque Development Services personnel, HDIC provided the City and Internal Audit with five (5) certificates regarding HDIC's compliance with loan agreements. These 5 certificates that were prepared by the HDIC Chief Financial Officer covered six-month periods beginning in November 2000.

In February 2004, HDIC sent Albuquerque Development Services a letter that stated, "Enclosed you will find the Loan Certification due the City as of November 15, 2003." The Certification required by the Master Development Agreement was three months late. The Certification from HDIC only addresses the status of bank loans. However, the Master Development Agreement requires a certification regarding amounts due to any Lender.

C. Annual Progress Reports

Section 105 of the Master Development Agreement states, "Master Developer shall provide the City with an annual written report describing, in such detail as reasonably required by the City, the actual progress of the construction of the Project. The report shall be delivered to Albuquerque Development Services."

The Annual Progress and Financial Reports for calendar year 2001 were dated April 23, 2002. The Annual Progress Report was prepared on a project-by-project basis for nine projects. The report provided information on progress to date for each project as well as future plans.

As of August 2003, Albuquerque Development Services personnel had not yet received a copy of HDIC's annual report for 2002. Albuquerque Development Services personnel contacted HDIC, and HDIC then provided the City with the "Second Revised Alvarado Transportation Center Project Area Business Plan" (Revised Business Plan) dated August 20, 2003. According to HDIC officials, the Revised Business Plan is the progress report for 2002.

The Revised Business Plan does not provide information about the progress of construction on a project-by-project basis; the report deals primarily with the financing for the projects. Although the Revised Business Plan was delivered seven months after the year end and does not appear to meet the requirement for an annual progress report, Albuquerque Development Services accepted it and did not request additional information.

D. Insurance Requirements

Section 610 of the Master Development Agreement states, "During the construction period and throughout the term of this Agreement, Master Developer, or through its contractors, subcontractors or agents, shall keep the Project insured against loss or damage by maintaining policies of insurance naming the City as a co-insured . . .

Master Developer shall provide evidence to the City of the required insurances before any notice to proceed is given to commence work on the Project." The agreement also states that the "Master Developer shall cause any contractors to maintain performance and payment bonds during construction of the Project in which the City is named as obligee."

HDIC personnel informed us that evidence of the required insurances and payment/performance bonds were not given to the City prior to the start of the Gold

Lofts construction project. They indicated that they did not know if evidence of the required insurances and payment/performance bonds was given to the City prior to the start of the Theater Block construction project. Albuquerque Development Services did not enforce the contractual requirements relating to insurance coverage.

The Master Development Agreement requires that the City be named as a co-insured on the insurance policies covering the projects. HDIC provided copies of certificates of insurance relating to the projects. The certificates of insurance for the general liability and property insurance coverage for the Theater Block for the two years from November 2002 through November 2004 did not name the City as co-insured. The certificate of insurance for the property insurance coverage for the Theater Block for the period from November 2001 through November 2002 also did not name the City as co-insured.

HDIC provided us with copies of the payment and performance bonds for the Gold Loft Project and Theater Block Project. The performance and payment bonds do not name the City as an obligee, as required by the Master Development Agreement. Albuquerque Development Services had not enforced these contractual requirements.

E. Labor Force Plan

Section 101.h. of the Master Development Agreement states: "Master Developer agrees to develop a labor force plan, outlining the total number and types of full time equivalency ('FTE') jobs (by occupational title) created throughout this project, together with anticipated wages and personnel hire dates for each employment position, to be submitted to the City within 90 days of the execution of this Agreement." The agreement was executed on November 29, 1999. HDIC did not submit the "labor force plan." Prior to our audit Albuquerque Development Services did not ask HDIC for the required plan.

In June 2000, HDIC requested labor force information from the operator of the new downtown theater. The theater's corporate office provided a schedule with positions and anticipated numbers of employees. The letter accompanying the schedule stated ". . . these figures should be viewed as 'best guess' estimates." In July 2002, the City's Department of Family and Community Services prepared a letter to Albuquerque Development Services with the results from a monitoring visit. The letter informed Albuquerque Development Services "HDIC needs to provide the actual numbers concerning the people hired by Century Theaters." Albuquerque Development Services did not pursue the matter until July 22, 2003, when personnel sent a letter to HDIC asking that the labor force plan be submitted "immediately."

HDIC obtained information from the movie theater in July 2003; however, there are nine lessees in the Theater Block, including four restaurants and several offices. Information from these other businesses should be reported to provide the City complete data on the jobs that resulted from the project. Albuquerque Development Services did not request information for the other lessees.

F. Preferred Return to City

Section 702 of the Master Development Agreement states, "Master Developer shall be entitled to a 4%, and the City to a 1% preferred return from net operating income derived from the Project, on a noncumulative, annual basis. Net Operating Income from the Project shall mean all income produced from the redevelopment and operation by Master Developer or Building Developer of each parcel of Real Property in the Project Area."

The December 31, 2001, financial statement for the HDIC Theater Block LLC indicates that it had a "net operating income" of \$35,237 during calendar year 2001. Therefore, according to the terms of the Master Development Agreement, HDIC should have paid the City 1% of this net operating income. HDIC informed us that they had not made this payment to the City. Although the unpaid amount that was due to the City was nominal, this indicates that the City is not adequately monitoring for compliance with the Master Development Agreement.

G. Lease Agreement between the City and HDIC Theater Block, LLC

There is a "Lease Agreement", dated December 28, 2001, between the City and the Theater Block relating to the \$250,000 Metropolitan Redevelopment Revenue Bond (Series 2001). The lease states in Section 4.20:

Reporting Requirements. The Company will submit to Issuer's Office of Economic Development or such other office of the Issuer as the Issuer may direct, on an annual basis beginning December 28, 2002, a report describing: . . .(ii) any economic benefit(s) arising out of the Project for the benefit of the metropolitan area or its residents, including, but not limited to, number of jobs created and gross payroll; and (iii) any community benefit(s) arising out of the Project, for the benefit of the metropolitan area or its residents."

Neither Albuquerque Development Services nor the City of Albuquerque Office of Economic Development received the required reports in 2002 and 2003.

The requirements for reporting are included in the Master Development Agreement to protect the City's interest in the projects and provide notice of potential problems that may be developing. The City did not follow up with HDIC to ensure that the required documents were prepared and submitted timely, thus exposing the City to increased risk.

RECOMMENDATION

The Task Force should ensure that the City Department or Division that is tasked with administration and monitoring of the Master Development Agreement and lease is cognizant of the requirements for HDIC.

- A system should be established to flag the due dates for the reports that are due at specified time intervals.
- There should be a follow-up process for reports that are not received timely.
- All documents submitted by HDIC should be carefully reviewed for reasonableness and compliance with the Master Development Agreement. Any questionable items should be identified and promptly resolved.
- Non-routine documents should be requested as events occur or as benchmarks are reached.

EXECUTIVE RESPONSE FROM THE TASK FORCE

“The designated Contract Recorder will be tasked with these responsibilities.”

4. THE TASK FORCE SHOULD DETERMINE IF THE METHOD USED BY HDIC TO RECORD THE VALUE OF CONVEYED PROPERTY WAS APPROPRIATE.

The City conveyed ¼ acre of land to HDIC for the Gold Lofts project in August 2003. According to the Settlement Statement, the value of the land was \$175,576. HDIC transferred the land to Gold Lofts prior to December 31, 2003. According to both the Gold Lofts and the HDIC Consolidated Financial Statements for the year ended December 31, 2003, the land was recorded at a value of \$1,100,947. HDIC provided us with an appraisal performed in June 2003, to support the value of the land as recorded on the financial statements.

Statement of Financial Accounting Standards No. 67 states that when allocating capitalized costs to the components of a real estate project, “Land cost and all other common costs (prior to construction) shall be allocated to each land parcel benefited. Allocation shall be based on the relative fair value before construction.” The Statement defines relative fair value before construction as “The fair value of each land parcel in a real estate project in relation to the fair

value of the other parcels in the project, exclusive of any value added by on-site development and construction activities.”

RECOMMENDATION

The Task Force or the City department or division responsible for monitoring and administrating the Master Development Agreement should determine if the method used by HDIC to record the value of the conveyed property was appropriate.

The City should ensure that the City’s capital account reflects the appropriate appraised value of the land.

EXECUTIVE RESPONSE FROM THE TASK FORCE

“There appear to be two provisions for establishing the value of City property transferred to HDIC under the Master Development Agreement. First, particular properties that may be transferred and their values for the purposes of the Capital Account are specified in ‘Exhibit F’ of the Agreement. This is an aspect of public inducements provided by the City to HDIC for the purpose of Downtown redevelopment. Second, the costs of other properties transferred are to be reimbursed by HDIC to the City.

“The Task Force will cause a review to be undertaken to ascertain how the value of the land transferred in August 2003 was determined. In conjunction with Finding 2, a review of the City’s Capital Account will be completed by November 30, 2004 and any necessary adjustments will be made to the City’s Capital Account.”

5. THE TASK FORCE SHOULD ENSURE THAT HDIC PROVIDE THE CITY DOCUMENTATION THAT ANY PREFUNDING REQUIREMENTS ARE MET PRIOR TO TRANSFERRING LAND.

A. Gold Lofts Pre-Funding Conditions

The financial institution that is providing construction financing for the Gold Lofts project sent a letter to Gold Lofts on August 22, 2003. The letter states that the financing has been approved subject to several terms. The pre-funding conditions include, “Borrower

shall provide evidence that a minimum of 10 reservation holders (24.4%) have been pre-qualified for financing and have deposited into an escrow account 10% of the purchase price of the units....”

However, it appears that when the City transferred the land for the Gold Lofts project to HDIC (which is currently under construction); HDIC had not met all of the pre-funding conditions of the construction lender.

As of August 2004, HDIC had 14 reservation holders; the lender’s pre-funding requirement that 10 percent of the purchase price of the units be deposited into an escrow account was not complied with. HDIC had 5 purchase agreements and had collected 10% of the purchase price for 4 of the agreements. Consequently, it appears that HDIC would not have been able to make the required certification to the City and to the escrow agent that HDIC “has complied with and satisfied all required terms and conditions contained in the irrevocable letter of commitment”

The success of the Gold Lofts project is dependent upon the actual sale of lofts. According to the Gold Lofts financial statements, Note 7, “HDIC, LLC and HDIC-Theater Block, LLC have guaranteed the construction loans and security agreement with Wells Fargo Bank, New Mexico, N.A.” If the Gold Lofts project is not successful, it could negatively impact other HDIC projects in which the City has an interest. Inflated reports of the number of lofts reserved and/or purchased could result in a misrepresentation to the lenders and investors in the project.

B. Mezzanine Financing

In September 2003, Gold Lofts entered into a promissory note agreement for mezzanine financing of the Gold Lofts project with the New Mexico Urban Initiatives Fund, L.P. A Four Party Agreement was executed between HDIC, Gold Lofts, the City, Wells Fargo Bank and the New Mexico Urban Initiatives Fund, L.P. in October 2003. The agreement specifies each of the parties’ rights related to the project. The promissory note carries an interest rate of 15.5% per annum compounded monthly in arrears. Gold Lofts used the proceeds from the promissory note to meet the equity requirements of the primary lender.

Although the CAO signed the Four Party Agreement, when asked about it at a later date he stated that he was unaware of the terms of the promissory note. It appears that he executed the agreement without full knowledge of the details of the agreement.

RECOMMENDATION

The Task Force should ensure that HDIC provide the City documentation that any prefunding requirements are met prior to transferring land in the future.

The Task Force should ensure that when City executives execute additional agreements with HDIC, full knowledge of the details of the agreement is provided to and understood by the executive prior to the execution of the agreement.

EXECUTIVE RESPONSE FROM THE TASK FORCE

“The Task Force will direct the staff at Albuquerque Development Services to ensure that no land is transferred to HDIC in the future until the City has documentation in hand assuring that any and all prefunding requirements have been met.

“As an oversight body, the Task Force must, of necessity, rely on staff. With the assistance of the Contract Recorder, Financial Auditor, and others, the Task Force will exercise greater diligence in assuring that its members have a clearer understanding of the proposals presented to them under the terms of the Master Development Agreement.”

6. THE CAO SHOULD CONSIDER REQUIRING ALL REAL PROPERTY TRANSACTIONS TO BE PROCESSED BY THE REAL PROPERTY SECTION.

The City has a Real Property Section that typically is responsible for City purchases and sales of land. There are controls in place to ensure that land transactions are recorded on the City's accounting system when the transactions are processed through the Real Property Section. Land transactions related to metropolitan redevelopment funds do not involve the Real Property Section. Albuquerque Development Services is responsible for all aspects of the metropolitan redevelopment funds, including the transfer of land.

In June 2000, Albuquerque Development Services transferred City land to the HDIC. This land was transferred at a value of \$1.37 million. HDIC did not pay the City any cash upon the closing of this transaction. As stated in the Master Development Agreement, the value of the land was to be included as an item in the City's Capital Account.

Albuquerque Development Services personnel did not provide any information to the City's Accounting Division, relating to this land transfer. Consequently, the land transfer was not reflected in the City's financial records and financial statements. In August 2003, another piece of property was transferred from the City to HDIC, with an assessed value of \$175,576.

As of September 2003, the Financial Accounting Manger had not been made aware of this second transfer of land.

The Financial Accounting Manager informed us that the Albuquerque Development Services had not informed the Accounting Division about the City's Capital Account. As a result, the City's Capital Account was not reflected as an asset on the City's financial records and financial statements.

RECOMMENDATION

The CAO should consider requiring all real property transactions to be processed by the Real Property Section regardless of the fund that has control of the property.

EXECUTIVE RESPONSE FROM THE CAO

“Administrative Instruction 5-3 already requires that the Real Property Section be involved in all real property transaction. However, the CAO has drafted an update of the Administrative Instruction and will remind Albuquerque Development Services that all real property transactions must be processed through the Real Property Section.”

7. THE TASK FORCE SHOULD REQUIRE AUDITED FINANCIAL STATEMENTS FROM HDIC.

The Master Development Agreement states, “Master Developer shall provide the City with annual financial statements approved by the Master Developer’s certified public accountant.” The Master Development Agreement did not require that the financial statements that were submitted by HDIC be audited.

HDIC submitted financial statements to the City that were “reviewed” by a certified public accountant. This provides much less assurance to the City, than audited financial statements would provide. A review of financial statements is performed to determine whether the financial statements are plausible in the circumstances. The review process consists of inquiries and discussions with company personnel. Ratios and trends are considered and used to assess the overall plausibility of the financial statements. A review is not a substitute for an audit. An audit requires obtaining an understanding of internal controls and an examination of evidence to support the information supplied to auditors. A true audit function consists of the auditor expressing his opinion as to the fairness in which the financial statements present the financial position and operating results of the organization.

The McCune Foundation (Foundation) required HDIC to hire a CPA firm to conduct an audit of HDIC for the year ended December 31, 2003. HDIC has provided a draft copy to the City.

The City will have more than \$8,000,000 invested in the Alvarado Transportation Center projects. Requiring that HDIC have an annual audit of its financial activities will reduce the risk of loss of the City's investment.

RECOMMENDATION

The Task Force should prepare an amendment to the Master Development Agreement to require annual audited financial statements from HDIC.

EXECUTIVE RESPONSE FROM TASK FORCE

“The Task Force agrees that audited, rather than reviewed, financial statements would have been a more appropriate requirement in the Master Development Agreement. The Task Force does not agree that requiring audited financial statements will necessarily reduce the risk of loss to the City, but they would provide more comprehensive information useful in the monitoring and oversight process. This is an item currently being negotiated for inclusion in the MOU discussed above.”

8. THE TASK FORCE SHOULD CLARIFY THE MASTER DEVELOPMENT AGREEMENT LANGUAGE RELATED TO CERTIFICATES OF COMPLETION.

The Master Development Agreement states in Section 702, "Each parcel of Real Property shall be assigned a Year 1 commencement date, which shall be the date that the City issues a Section 611 certificate of completion for each such parcel." The establishment of this date is necessary because the City starts to receive monies from the master developer in the sixth year after this date.

Section 611 of the agreement states:

"Promptly after completion of the improvements to each parcel of Real Property in accordance with the provisions of this Agreement, the City will furnish the Master Developer with an instrument certifying completion of same ('Certificate of Completion'). The certification of the City shall be a conclusive acknowledgement by the City of satisfaction by the Master Developer of its obligations under this Agreement, as to the applicable parcel of Real Property."

Albuquerque Development Services considers the Certificate of Occupancy that was issued by the Building Safety Division of the Planning Department to be the "Certificate of Completion." However, the Building Safety Division may not have knowledge regarding whether HDIC has satisfied all of its obligations under the Master Development Agreement. This could increase the City's exposure to risk.

RECOMMENDATION

The Task Force should review the language in Section 611 of the Master Development Agreement and determine if the Certificate of Occupancy meets the intent of the requirement for a Certificate of Completion.

EXECUTIVE RESPONSE FROM THE TASK FORCE

“The Task Force will review the language in Section 611. It is possible that the Certificate of Occupancy imposes a higher standard and implies a different intent than the required Certificate of Completion, which starts the clock for the City to be entitled to receive compensation under the terms of the Master Development Agreement.”

9. THE TASK FORCE SHOULD AMMEND THE MASTER DEVELOPMENT AGREEMENT TO REQUIRE TASK FORCE APPROVAL IN ADVANCE OF RELATED PARTY TRANSACTIONS.

The December 31, 2003, draft consolidated financial statements for HDIC, Theater Block and Gold Lofts include notes to the financial statements, which disclose related party transactions. A related party transaction is a business deal in which an entity makes a payment to a different business entity; and there are individual(s) who are officers and/or directors in both business entities. These types of transactions are disclosed in financial statements because they are generally considered to lack the “arms-length” or un-biased characteristic, which is normal in typical business transactions.

Note 8 to the **HDIC Consolidated** Financial Statements disclosed that:

“HDIC - Theater Block, LLC paid a leasing commission of \$88,768 to HDIC Asset Management in 2003 in connection with the Chamber of Commerce lease. The commission was calculated based on 6% of gross potential rent for the first 5 years, 4% of gross potential rent for the second 5 years, and 0% of gross potential rent for the final 5 years of the Chamber of Commerce's 15 year lease with HDIC – Theater Block, LLC. The percentages used for the calculation of the commission are at or below comparable

percentages used to calculate commissions to outside brokers that were paid on other retail and office spaces within the Theater Block project.

“HDIC, Theater Block, LLC has entered into an operating lease with the firm of Bryan & Flynn O’Brien for the lease of the office space. Bryan & Flynn O’Brien is a law firm whose principals are members of Arcadia at Albuquerque, L.P. The lease is on terms that are comparable with other similar space rented to unrelated third parties. HDIC has entered into an agreement with the law firm of Bryan, Flynn O’Brien. The company pays a legal retainer of \$6,000 per month to cover the law firm's overhead costs that have been allocated to HDIC by the law firm based on the work performed for HDIC. This includes covering the cost of support staff necessary to conduct HDIC business. In addition to the legal retainer, HDIC is paying the rent (\$4,434 per month) for the Bryan, Flynn O’Brien office space in the Theater Block project, since three of four members of the firm work primarily on HDIC business.

“In 2002, HDIC Theater Block, LLC entered into an agreement to pay service fees to HDIC Asset Management, LLC. The aggregate amount of service fees to be paid is capped at \$420,000 based on the appraised value of the Theater Block property. The services provided by HDIC Asset Management, LLC relate to the initial development of the property and its ongoing successful operation. The full value of the capped service fee was capitalized as part of the Theater Block building in 2002. Payments of the service fees have junior priority to the NOI fees, City distributions, preferred returns to LLC members, and cash flow splits to members other than HDIC. As a result, payment of service fees has no financial impact on City distributions and returns to non-HDIC Theater Block, LLC members which are based on Theater Block Cash Flow. HDIC Asset Management, LLC has a related agreement with the McCune Foundation that stipulates that no service fee payments will be made unless cash flow distributions from Theater Block, that flow through HDIC to the McCune Foundation, are made. The service fee payments are restricted to be part of the split of HDIC distributable cash flow made to HDIC members: Arcadia at Albuquerque and The McCune Foundation. No service fee payments were made in 2003. HDIC Asset Management, LLC is owned by Christopher B. Leinberger and George R. Bryan who are the President and Chief Operating Officer, respectively, of HDIC.

“During 2003, HDIC Theater Block, LLC advanced monies to HDIC. The advances are treated as a loan, bearing interest at 5% per year, compounded Monthly. All advances were made using idle funds that HDIC Theater Block, LLC would otherwise have placed in bank interest bearing accounts yielding less than 2% per year. These advances had no impact on HDIC Theater Block, LLC’s ability to make timely distributions to any LLC members or the City of Albuquerque. HDIC will repay the advances as distributions are

made available by HDIC Theater Block, LLC. Management believes that in 2004, cash distributions based on 2003 operations, will allow HDIC to repay at least \$220,000 of these advances and accrued interest. It is anticipated that the balance of these advances plus interest will be paid in 2005 based on 2004 operations.”

“The HDIC - Gold Avenue, LLC Agreement requires that a construction management fee be paid to HDIC - Asset Management, LLC. The construction management fees were payable commencing in October of 2003. Management fees paid to date under this agreement total approximately \$190,000. In addition, there is a total due of \$17,500, as of December 31, 2003.

There is currently no provision in the Master Development Agreement that requires that the Master Developer disclose related party transactions, prior to entering in these business arrangements. Further, it appears that the Task Force may not be aware of the number of related party transactions related to HDIC and its principals.

RECOMMENDATION

The Task Force should amend the Master Development Agreement to require Task Force review and approval in advance of HDIC, Theater Block, Gold Lofts or subsequent projects entering into related party transactions.

EXECUTIVE RESPONSE FROM THE TASK FORCE

“The creation and use of related entities is a common occurrence in complex, sophisticated real estate development projects. This finding is still another example of the short-comings in the Master Development Agreement to allow the City to obtain all the necessary information for informed decision making with respect to the venture. To an extent, the Master Development Agreement calls for disclosure of financial development-related information relative to HDIC properties. The Task Force will require the submittal of this information as a condition of project approval.

”The Task Force is uncertain if an amendment to the Master Development Agreement will, in and of itself, be able to achieve full and complete disclosure of related party transactions. The Task Force has been negotiating with HDIC for inclusion of a related party disclosure requirement in the MOU discussed above. However, it is uncertain whether HDIC will agree to this amendment.”

10. THE TASK FORCE SHOULD APPROVE METHOD OF SETTLEMENT OF CLAIMS MADE BY DEVELOPERS.

In June 2000, the City transferred a piece of property with an appraised value of \$1.37 million to the HDIC. After the transfer, it was determined that the land had a very large amount of construction debris throughout the site, at depths of six to eight feet. The site could not be considered “a clean buildable site” as assumed in the appraisal.

This issue went to arbitration to determine a resolution. The arbitrator awarded a judgment of \$262,340 to HDIC. The arbitration agreement stated, “The City shall pay this sum to the Developer by check delivered not later than October 27, 2000. Alternatively, at the City’s option, the City may take a reduction of \$262,340 in the amount of its capital account maintained under the Development Agreement.”

The City paid \$262,340 to HDIC from the Risk Management fund, instead of taking a reduction in the City’s Capital Account. It appears that Albuquerque Development Services personnel made the decision to pay HDIC. Albuquerque Development Services personnel do not have an explanation or documentation as to why the City made this payment instead of taking a reduction in the City’s Capital Account. There is no indication that the Task Force was consulted regarding the method of payment. The payment of \$262,340 was made to HDIC at a time when the Risk Management fund was facing a serious deficit. The City will be transferring other properties to the HDIC in the future, which could result in a similar situation.

RECOMMENDATION

The Task Force should approve any settlements of additional claims related to the Master Development Agreement.

The Task Force should instruct the department or division that is assigned the responsibility for administering the Master Development Agreement that the Task Force must approve the settlement of claims related to the agreement.

EXECUTIVE RESPONSE FROM THE TASK FORCE

“The Task Force agrees that any claim related to the Master Development Agreement should be brought to its attention for review and approval. The Contract Recorder and Albuquerque Development Services will be directed to do so.”

11. THE TASK FORCE SHOULD AMEND THE MASTER DEVELOPMENT AGREEMENT TO REQUIRE DOCUMENTATION FOR REIMBURSEMENT TO HDIC FOR INFRASTRUCTURE COSTS.

The Master Development Agreement with HDIC states, “The City shall provide infrastructure costs for the Project, as described in the Master Plan, up to an amount of \$500,000.” HDIC directly contracted with several vendors to provide infrastructure improvements for the project, although the Master Development Agreement did not specifically provide for this action. HDIC then billed the City for these infrastructure costs. The Capital Improvements Program Division (CIP) reimbursed HDIC for these infrastructure improvement costs.

The agreement between the HDIC and the City does not specify whether any documentation is required from HDIC, prior to the City’s reimbursement of the infrastructure costs that HDIC incurs. There was a notation in the CIP Division’s files that the CIP Official had indicated that “backup” is not required for the payments being made by the City to HDIC.

The CIP Division did obtain some documentation prior to reimbursing HDIC. However, the documentation that the CIP Division obtained was not the same as the documentation required when the City makes payments directly to the infrastructure improvement contractors.

The Master Development Agreement did not support the CIP Division in its efforts to obtain documentation from HDIC. In February 2002, HDIC sent the CIP Division a memorandum regarding the payment by the City of infrastructure costs. This memorandum stated, “. . . HDIC was not supposed to have to provide back up to the invoices”

The contractors who are making the infrastructure improvements may also be working on buildings and tenant improvements for HDIC during the same period. Without the supporting documentation, the City cannot be sure that it is only paying for the infrastructure improvements.

RECOMMENDATION

The Task Force should amend the Master Development Agreement to require documentation for reimbursement to HDIC for infrastructure costs.

EXECUTIVE RESPONSE FROM THE TASK FORCE

“The Task Force agrees that the expenditure of City funds should always be fully and completely documented. The Task Force will either direct City agencies to obtain such documentation or attempt to amend the Master Development Agreement to ensure that reimbursed infrastructure costs are adequately documented.”

12. THE ADMINISTRATION SHOULD ENSURE THAT THE CITY COMPLIES WITH THE STATE STATUTE ON METROPOLITAN REDEVELOPMENT.

Section 3-60A-12.A of the state statute on Metropolitan Redevelopment states, "A municipality may sell, lease or otherwise transfer real property or any interest therein acquired by it in a metropolitan redevelopment area . . . The purchasers or lessees and their successors and assigns shall be obligated to devote the real property only to the uses specified in the metropolitan redevelopment plan for a period of years as set out in the sale or lease agreement"

Section 3-60A-9 D. states, "A metropolitan redevelopment plan may be modified at any time. . . . Any proposed modification which will substantially change the plan as previously approved by the local governing body shall be subject to the requirements of this section, including the requirement of a public hearing before it may be approved."

Section 101.f. of the Master Development Agreement states, "Compliance with Metropolitan Redevelopment Plan requirements. The Master Developer agrees for itself, and its successors and assigns, and every successor in interest to the Project or any part thereof, that the Master Developer and such successors and assigns shall devote the Real Property conveyed to it and the Project to the applicable uses and restrictions specified in the Metropolitan Redevelopment Plan as it exists on the date of submission by the Master Developer of an application for a building permit for the Project, or part thereof."

Section II.B.8 of the "Alvarado Transportation Center Metropolitan Redevelopment Plan", which is an attachment to the Master Development Agreement, states, "Housing development in the Plan will include a minimum of 20% of the dwelling units affordable to households less than 80% of median income."

HDIC informed the auditors that 10% of the housing units in the Silver Court Apartment project would be low income housing. An August 25, 2003, letter from the CAO to HDIC stated:

“Section 408 of the Alvarado Master Development Agreement between the City of Albuquerque and the Historic Development Improvement Corporation (HDIC)

designated that Phase I of the master plan include a 'low income housing' component. We have all agreed that that component would be built into the Silver Court Apartment project. Over the past several months' considerable discussion has occurred around the low income housing issue. It is time to bring closure to this issue.

"Following is a concise recap of the outstanding items and final resolutions:

"1. Number of Low Income Units --- 17 of the apartment units will meet the 10% low income housing set aside."

The HDIC Chief Operating Officer stated that the Gold Lofts project was not subject to the low-income housing component. He justified the departure from the plan for the Silver Court Apartments project (the next project to be developed under the Master Development Agreement) in a letter to an Assistant City Attorney dated December 12, 2002. The letter states in part:

"The Redevelopment staff believes that the low income housing component should be 20% of the units because that was their desire when they put out the original RFP. That condition was not included in the Master Development Agreement. The reality is that the only promise made by HDIC in the Master Development Agreement was to provide a low income housing component.

"To cut to the chase, however, we are proposing to set aside 10% of the approximately 174 units (17 units) as the component of low income housing for the project. Had we set even 20% of the original 60 townhouses, that would have been 12 units. The reality is that we are providing nearly 50% more affordable units than was originally envisioned (by Redevelopment Staff)."

The CAO agreed to the changes without modifying the Metropolitan Redevelopment Plan. State statute 3-60A-9 D. requires specific hearings and approvals for any proposed modification, which substantially changes the approved plan. If the change in the percentage of low-income housing units from 20% to 10% is considered a substantial change, the modification should be the subject of public hearings and approved by the City Council.

RECOMMENDATION

The Task Force should request an opinion from the City Legal Department regarding whether or not the change in the percentage of low-income housing units is a substantial change to the Metropolitan Redevelopment Plan as defined by State Statute.

EXECUTIVE RESPONSE FROM THE TASK FORCE

“The Legal Department has issued an opinion that, with respect to the Silver Court project, the 10% set-aside for low income housing was a negotiated concession on the part of the Task Force, reflecting, in part, the nature of the proposed Silver Court project. Furthermore, the Alvarado Transportation Center Metropolitan Redevelopment Area Plan states: ‘Housing development in the Plan will include a minimum of 20% of the dwelling units affordable to households less than 80% of median income.’

“The Legal Department has further opined that the 10% set-aside for the Silver Court project was unique to the proposal from Phoenix Properties. That proposal has now been withdrawn by HDIC and any deviation from a 20% set-aside would again become a matter of negotiation.”

13. THE TASK FORCE SHOULD REQUEST CITY COUNCIL APPROVAL FOR THE 2004 “PODIUM PARKING” AGREEMENT, AS REQUIRED BY THE MASTER DEVELOPMENT AGREEMENT.

Section 606.d, Podium Parking/Phase II Residential, of the Master Development Agreement (dated November 29, 1999) states:

"The City shall pay the cost to construct podium parking spaces, described in the Master Plan/Phase II Residential, **upon City Council approval of a subsequent agreement** [emphasis added], negotiated by the Task force and Master Developer, as to the cost and the number of parking spaces to be constructed and paid for by the City."

In February 2004, the City and the Master Developer executed the “Third Amendment To Master Development Agreement for the Alvarado Transportation Center.” The portion of the amendment that relates to the “Podium parking” states:

“THEREFORE, the parties agree that the Development Agreement is hereby amended as follows: . . .

6. The cost of parking in the amount of one million nine hundred thousand dollars (\$1,900,000), authorized by the approval of the City Council, will be applied to the Silver Court redevelopment . . .”

The 1999 Master Development Agreement requires that this subsequent 2004 agreement, which establishes the cost of the parking, be approved by City Council. There has apparently been no City Council approval of this subsequent agreement, as was required by the Master Development Agreement. The City Attorney confirmed that City Council approval is still needed before the City can make payments for the Podium Parking.

The same contractor(s) may build the "Podium Parking" at the same time as the Silver Court project. To avoid improper payments, it is important that the City ensure that there are adequate project management controls in effect to ensure that costs are properly allocated between the Podium Parking and the Silver Court project (See Finding No. 9 for additional information and recommendation).

RECOMMENDATION

The Task Force should ensure that City Council approval is obtained prior to approving the plans for the Podium Parking.

EXECUTIVE RESPONSE FROM THE TASK FORCE

"Bill No. R-01-365 (Enactment No. 175-2001) appears to approve applying the requirement that the City pay the cost to construct podium parking spaces to the high density residential project. The high density residential project is subject to all the provisions of the Master Development Agreement and shall require review and approval of the Task Force, including, but not limited to, plans regarding the cost and number of parking spaces. The Task Force will again review Bill No. R-01-365 and other relevant documents and if additional approval from the City Council is determined to be necessary will obtain such approval."

CONCLUSION

The City should improve its administration and monitoring of the agreements and contracts with HDIC. Required reports and other documents have not all be submitted to the City when required. The Task Force should clarify the language in the Master Development Agreement to ensure that the City's interest in the various projects is better protected.

We appreciate the assistance and cooperation of the City personnel during the audit.

GENERAL COMMENT FROM THE TASK FORCE

“The Task Force has demonstrated its willingness to successfully redevelop Albuquerque’s Downtown by cooperating in a variety of projects. At the same time, the Task Force believes it is apparent that the Master Development Agreement entered into between the City and HDIC, LLC in November, 1999 failed to adequately address several issues. The majority of the individuals involved in the process of creating and entering into that Agreement are no longer available to provide background information about the rationale for many of the provisions, or the lack of provisions that now seem to be prudent. Therefore, the Task Force now finds itself in the position of attempting to rectify situations that may not be readily susceptible to modification or correction at this time. The Task Force has made diligent efforts to address the concerns identified in this audit, and all others that may come to its attention.”

“The Task Force, including the CAO, acknowledges the challenges encountered by the Internal Audit staff. The “lessons learned” will be incorporated by the Task Force into changes adopted with regard to City staffing assignments and practices and have been incorporated into a draft Memorandum of Understanding (MOU) amending the Development Agreement as the City continues to take a proactive role in the redevelopment of Albuquerque. The draft MOU is subject to HDIC’s approval. In general, the Task Force intends to scrutinize all future decisions in terms of their conformance to the Master Development Agreement.”

“Additionally, the Task Force recognizes that there are a number of findings included in the Audit Report which are critical of Albuquerque Development Services (ADS) and the degree to which, in the judgment of Internal Audit staff, they carried out certain responsibilities. It appears that, as with other functions required by the Master Development Agreement, there was a lack of clarity in delineation of responsibilities. It is also the opinion of the Task Force that the staff of ADS was often “out of the loop” during the previous Administration and that decisions regarding HDIC may have been made at a higher level within the previous City Administration.”

“For a time period, it appeared that the only role of ADS in relation to the Task Force was to set up and attend Task Force meetings. The Task Force believes that the role of ADS in relation to HDIC should be reexamined and the Task Force should clearly delineate what is expected. It is also”

noted that while the staff of ADS has expertise and experience in redevelopment, contract monitoring is a different function. There also appears to have been little emphasis placed on the monitoring function, such as regarding the City Capital Account, and a lack of clarity about who was responsible for it within the City structure. Accordingly, as noted elsewhere in the Task Force's response, a new structure is proposed which will emphasize acquiring real estate development and financial expertise, clear responsibility assigned to an individual position for receiving and distributing documents required by the Agreement, and ensuring that documents are in accordance with Agreement requirements and received according to schedule.

“At the direction of the Task Force, and in response to the findings in this report, staff has been actively involved in attempting to negotiate with HDIC a Memorandum of Understanding to clarify certain provisions of the Master Development Agreement. As of the date of this response, those negotiations are on-going. In addition, the Task Force intends to take action on a number of findings as indicated in the responses within the purview of its authority.”

Principal Auditor

REVIEWED AND APPROVED:

APPROVED FOR PUBLICATION:

Carmen L. Kavelman, CPA, CISA, CGAP
Acting Internal Audit Officer

Chairman, Audit Committee