

AUDIT TEAM

Jim Williamson, CPA, CIA, City Auditor

Matt Weller, CPA, Assistant City Auditor

Janet McWilliams, CPA, Audit Manager

Tim Alvarez, CICA, Senior Auditor

**ECONOMIC DEVELOPMENT
EXPENDITURES AUDIT**

APRIL 19, 2016

MAYOR AND CITY COUNCIL

<i>Mick Cornett</i>	<i>Audit Committee, Mayor</i>
<i>James Greiner</i>	<i>Ward 1</i>
<i>Ed Shadid</i>	<i>Ward 2</i>
<i>Larry McAtee</i>	<i>Audit Committee, Ward 3</i>
<i>Pete White</i>	<i>Ward 4</i>
<i>David Greenwell</i>	<i>Audit Committee, Ward 5</i>
<i>Margaret S. "Meg" Salyer</i>	<i>Ward 6</i>
<i>John A. Pettis Jr.</i>	<i>Ward 7</i>
<i>Mark K. Stonecipher</i>	<i>Ward 8</i>



April 19, 2016

The Mayor and City Council:

The Office of the City Auditor has completed an audit of economic development program expenditures.

Based on the results of our audit, we believe that, during the 33 months ended March 31, 2015, management controls were adequate and effective to ensure economic development expenditures materially complied with relevant requirements, except for controls ensuring all economic development agreement payment conditions are met prior to the expenditure.

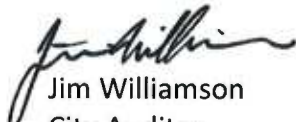
Recommendations for improving administration of economic development expenditures, discussed in more detail in the attached report, are summarized as follows:

- Compliance with agreement payment conditions should be verified or those conditions should be removed from the agreements. See Recommendations 1 and 2.
- Checklists should be developed for use in verifying whether all significant agreement provisions are met. See Recommendations 3 and 15.
- The annual cap for Outlet Mall marketing expense reimbursements should be reasonably estimated using sales tax payments received by the City Treasurer's Office. See Recommendation 4.
- Requiring separate sales tax reporting for stores with more than one Oklahoma City location should be considered for future agreements with incentives or assistance based on sales tax remittances. See Recommendation 5.
- Outlet Mall capital investment requirements contained within the development agreement should be verified with the developer. See Recommendation 7.
- Forfeiture conditions in economic development agreements should be enforced unless the agreements are amended or the Oklahoma City Economic Development Trust (OCEDT) General Manager is authorized to waive those conditions. See Recommendations 8 and 9.
- In-lieu of property tax payments arising from Tax Increment Financing (TIF) redevelopment agreements should be collected when due. See Recommendation 10.

EXECUTIVE SUMMARY: Audit Report 15-03

- Terms in TIF redevelopment agreements and related covenants should be consistent, related subordination agreements should be updated when covenants are amended, and all covenants should be presented to the City Council for acceptance. See Recommendations 11, 12, 13 and 14.
- Agreements directing repayment of GOLT Bond funds used for the KC-46A maintenance facility land purchase as contemplated in the September 9, 2014 Joint Resolution of the City Council and OCEDT should be actively pursued. See Recommendation 16.
- Responsibilities for verifying receipt of contractual benefits and approval of related payments should be segregated. See Recommendation 17.

All comments, recommendations, suggestions and observations arising from our audit have been discussed in detail with appropriate representatives from management. These discussions were held to assure a complete understanding of the content and emphasis of items in this report. Responses to this report from management are attached.


Jim Williamson
City Auditor


Matt Weller
Assistant City Auditor


Janet McWilliams
Audit Manager

ECONOMIC DEVELOPMENT EXPENDITURES AUDIT

AUDIT OBJECTIVE, BACKGROUND, SCOPE AND METHODOLOGY

The objective of this audit was to determine the adequacy and effectiveness of controls ensuring selected economic development expenditures during the 33 months ended March 31, 2015 complied with relevant requirements (i.e., legal, program, agreement).

The Oklahoma City Economic Development Trust (OCEDT) oversees City economic development expenditures stemming from related programs and agreements jointly approved with the City Council. The City Manager serves as the OCEDT General Manager and along with the Economic Development Program Manager (Program Manager) is functionally responsible for administering OCEDT expenditures. The OCEDT's financial structure is comprised of three funds established for distinct purposes as follows:

- An Economic Development Fund using City General Fund appropriations for:
 - Economic development services provided in accordance with management agreements with the Alliance for Economic Development of Oklahoma City and the Oklahoma City Economic Development Foundation¹,
 - Myriad Botanical Gardens development in accordance with a management agreement with the Oklahoma City Myriad Gardens Foundation, and
 - Miscellaneous economic development projects, including but not limited to retail incentives governed by the City's Retail Incentives Policy².

- A General Obligation Limited Tax (GOLT) Bond Fund using proceeds from issuances of the \$75 million GOLT Bond authorization for economic development approved by City voters in 2007. GOLT Bond proceed use is guided by the City's Strategic Investment Program (SIP)³ of which the primary objective is creation of quality jobs meeting the following criteria:
 - New, within Oklahoma City limits, and relating to goods and services sold primarily outside the State of Oklahoma,
 - Qualifying average wage thresholds which are 100% of the Oklahoma City Metropolitan Area Statistical Area average wage,
 - Employee healthcare benefits at least 50% employer paid, and
 - A minimum of 50 full time jobs and annual new payroll equal to or greater than \$1.75 million.

Companies must apply to the Oklahoma City Economic Development Foundation for SIP incentives and be approved by OCEDT. A SIP agreement is then entered with the company

¹ The Oklahoma City Economic Development Foundation is a private nonprofit corporate subdivision of the Greater Oklahoma City Chamber of Commerce.

² The Oklahoma City Retail Incentive Policy was approved by City Council/OCEDT Joint Resolution on October 14, 2008 to set forth guiding principles for the program, including but not limited to defining the types of retailers that may be incentivized and the administrative procedures to be followed in awarding the incentives.

³ The Oklahoma City Strategic Investment Program was approved by City Council/OCEDT Joint Resolution on December 4, 2007 and amended by Joint Resolution on September 11, 2012 to include additional Program activities allowed by amendments to the governing State statute.

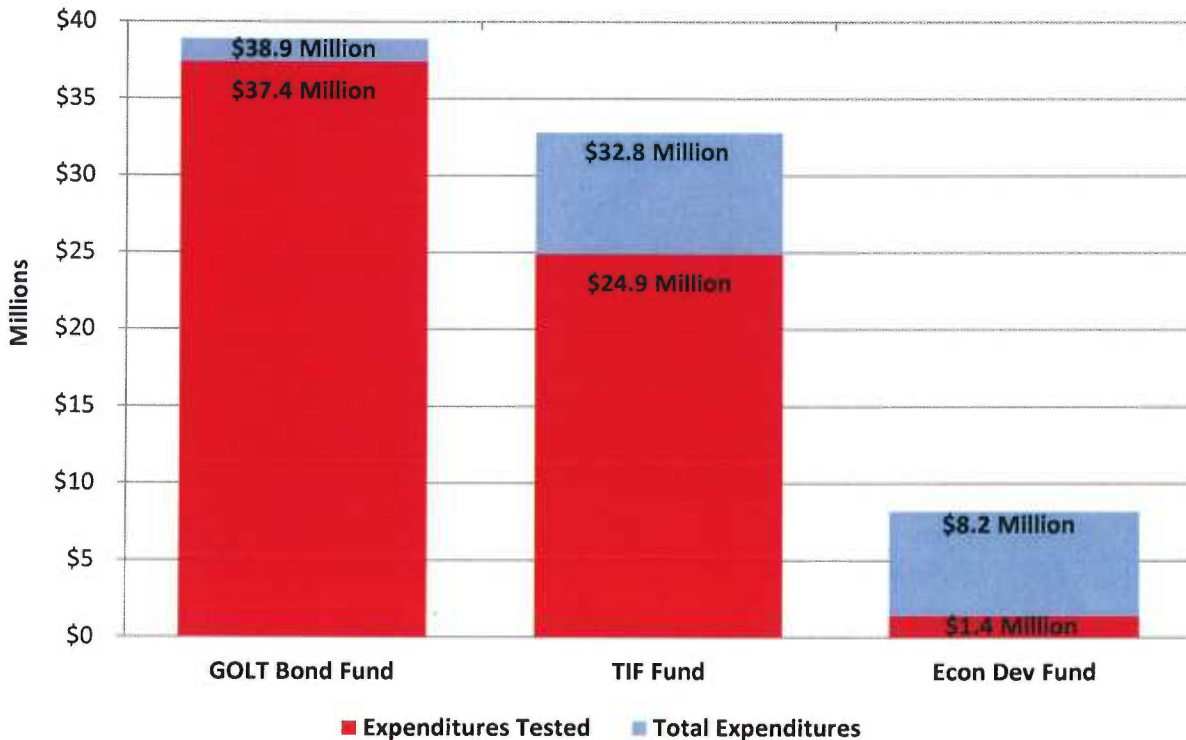
for job creation incentives to be paid based upon documented evidence of performance. The SIP agreements also generally include a minimum capital investment requirement.

- A Tax Increment Financing (TIF) Fund using proceeds from borrowings to:
 - Fund City construction of public improvements on publically owned land or easements,
 - Fund construction of improvements by other public entities (e.g., Oklahoma County, I-89 School District), or
 - Supplement redevelopment financing for improvements by private developers.

The borrowings are expected to be repaid with increased property and/or sales tax revenues from future expansion of the tax base within a defined district (TIF District) over an established period of time (generally 25 years) as a result of the financed improvements. Financed improvements must comply with parameters established within specific project plans⁴ created to guide the use of specific TIF. The City had established nine TIF Districts as of March 31, 2015.

Economic development expenditures for the 33 months ended March 31, 2015 totaled approximately \$79.8 million and expenditures selected for testing during the audit totaled \$63.7 million across the various economic development activities as illustrated below.

**Economic Development Expenditures
for the 33 Months Ended March 31, 2015**



⁴ TIF Districts and the project plans created to govern the use of TIF are established by City Ordinance. A project plan may include the use of TIF from more than one TIF District.

Procedures performed during our audit included reviews of relevant State statutes, City ordinances, program policy documents, agreements and TIF project plans; interviews with management; observation of on-site reviews of SIP job creation incentive support; analyses of OCEDT expenditures; and reviews of other documentation supporting related payments.

We conducted this audit in accordance with generally accepted government auditing standards. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our audit findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following section of this report includes recommendations intended to provide constructive suggestions for improving the administration of economic development expenditures. Included in the body of this report are management responses to each recommendation. Management responses are attached to this report in their entirety.

RESULTS OF WORK PERFORMED

The results of our audit indicate that controls were adequate and effective to ensure economic development expenditures during the 33 months ended March 31, 2015 materially complied with relevant requirements, except for controls ensuring all economic development agreement payment conditions are met prior to the expenditure.

AGREEMENT PAYMENT CONDITIONS NOT VERIFIED BEFORE EXPENDITURE

Certain economic development expenditures were made without obtaining evidence that all conditions for payment had been met. While evidence that SIP agreement jobs were created and TIF redevelopment agreement projects were completed was obtained before all tested expenditures were made, the following required conditions had not been verified before the expenditures were made.

- Sufficient evidence of minimum capital investments required by two separate SIP agreements was not obtained from The Boeing Company (Boeing). The agreements require documented minimum capital investments of \$5.1 million and \$20 million, respectively. During the audit and after receiving several incentive payments, Boeing reported total capital investments of approximately \$8.4 million and \$15.1 million, respectively, without documented support. Incentive payments were made because the agreed upon jobs were created and only a nominal capital investment is believed to be required by the governing State statute⁵. All SIP objectives may not be achieved if incentive payments are made before evidence supporting required minimum capital investments is obtained.

⁵ Oklahoma Statute §62-802(5)(j) defines qualified economic or community development purpose (for bonds issued for such purpose by municipalities as allowed by §X-35 of the Oklahoma Constitution) as “the acquisition, construction, development, and/or equipping of economic development programs, including but not limited to job creation payments, low interest and/or forgivable loans” [emphasis added].

- Oklahoma County Assessor verification of property minimum taxable market values was not obtained as required by five TIF District 2 redevelopment agreements⁶. The agreements required the developers to prove the developed properties realized, by a specific date, a specified minimum taxable market value verified by the Oklahoma County Assessor. Assistance was paid because the projects were completed and other conditions were met. Further, this condition could not have been reasonably met and was not deemed necessary since the developers agree to minimum annual property tax payments regardless of taxable market value. However, the agreements were not amended to remove this condition. City Council and OCEDT Trustees may not be fully informed of agreement conditions if agreements are not amended for unnecessary payment conditions.
- Evidence of minimum property occupancy was not obtained prior to payment as required by the TIF District 2 redevelopment agreement with City Center Development, LLC. The agreement required the developer to provide evidence of at least 200 residential apartment units covered by one or more Certificates of Occupancy and at least 92 rented and occupied units. Evidence this requirement was met was requested and received 6 months after the assistance payment. All desired development impacts may not be realized if evidence of minimum occupancy requirements is not obtained before assistance payments are made.
- Subordination agreements were not obtained as required by the TIF District 2 redevelopment agreement with 10th & Broadway Parking, LLC. The agreement requires the developer to provide subordination agreements from property lienholders agreeing their liens are secondary to minimum annual property tax payments required by the Deed of Declaration of Covenants (Covenants)⁷. Payment recovery through minimum annual property tax payments may be more difficult if subordination agreements are not obtained before assistance payments are made.
- Evidence of a minimum \$20 million total capital investment was not obtained prior to payment as required by the TIF District 2 redevelopment agreement with OCU Law Building Associates, LLC. The agreement requires the developer to provide documentation showing a minimum investment of \$20 million in the project before receiving the final assistance payment. Evidence this requirement was met was requested and received 4 months after the final assistance payment. All desired development impacts may not be realized if evidence of minimum capital investment requirements is not obtained before assistance payments are made.

In part, likely because of the preceding issues, completion certificates indicating satisfaction of all agreement conditions were not promptly issued as required by 3 of the TIF 2 redevelopment

⁶ TIF District 2 redevelopment agreements with 4th Street Properties, LLC, Carnegie Centre TIF, Inc., 10th & Broadway Parking, LLC, and two separate agreements with Midtown HC, LLC, included this requirement. A redevelopment agreement with City Center Development, LLC, required obtaining verification by the Oklahoma County Treasurer of property tax payments for the tax year following expected completion equating to a specified minimum taxable market value multiplied by the applicable millage rate which was also not obtained.

⁷ The Covenants attach minimum annual property tax payment requirements to the properties until the specified total amount of the assistance payment plus interest is recovered or the TIF District expires or is terminated. Covenants for these properties were accepted jointly by the City Council and OCEDT on March 31, 2015 and were subsequently filed with the Oklahoma County Assessor.

agreements discussed above. One completion certificate was issued more than 2 years after completion while the other two were issued 2 to 4 months after completion.

RECOMMENDATION (1)

The required documentation should be obtained to evidence compliance with agreement payment conditions discussed above. Alternatively, if the discussed payment conditions are deemed unnecessary, the agreements should be amended to remove those conditions and be presented to the City Council and OCEDT for approval.

MANAGEMENT RESPONSE (1)

Management agrees. Staff has implemented processes that include checklists to ensure all requirements are met prior to payment. In addition, staff has received documentation supporting an investment in excess of \$38 million in investment for the Boeing project that required a minimum investment of \$20 million and \$5.2 million in investment for the Boeing project that required a minimum investment of \$5.1 million. The subordination agreement for the 10th & Broadway Parking, LLC has also been received. Staff has also initiated contract amendments for contracts that have unnecessary requirements for OCEDT and City Council approval.

RECOMMENDATION (2)

All future agreement payment conditions should be verified before expenditures are made. Future agreements containing payment conditions deemed unnecessary should be amended and presented to the OCEDT and City Council for approval.

MANAGEMENT RESPONSE (2)

Management agrees. Staff has implemented processes that include checklists to ensure all requirements are met prior to payment.

RECOMMENDATION (3)

A checklist should be developed to document if and how all payment conditions were met, culminating with timely issuance of completion certificates for future development agreements when required.

MANAGEMENT RESPONSE (3)

Management agrees. Staff has implemented processes that include checklists to ensure all contract requirements, including the issuance of the certificate of completion are met prior to payment.

OTHER AGREEMENT CONDITIONS NOT VERIFIED

Certain other non-payment related economic development agreement conditions were not verified. While of lesser importance than the payment conditions, these other unverified conditions could impact expected City benefits from these agreements.

Outlet Mall Agreement

The OCEDT and City entered a retail incentive agreement with Horizon Group, LP (Horizon) to develop The Outlet Shoppes at Oklahoma City (Outlet Mall) on May 6, 2008. While the Outlet Mall has expanded the City's retail base as intended by the agreement since opening in August 2011, the following conditions in the agreement were not verified.

- OCEDT regional marketing expense reimbursements were not capped annually based upon verified sales tax remitted to the Oklahoma Tax Commission (OTC) by Outlet Mall tenants. The agreement requires annual⁸ reimbursements to be capped at 12.5% of sales tax remitted to the City by the OTC for Outlet Mall tenants or \$550,000, whichever is less. Reimbursements have been capped annually based upon the lesser of sales tax estimated using Horizon reported gross tenant sales or \$550,000. Annual reimbursements totaled the \$550,000 maximum for each fiscal period except 2013⁹. The accuracy of sales tax estimates used to determine the cap could not be verified using OTC data¹⁰ supporting sales tax payments received by the City Treasurer's Office. Reimbursement overpayments could occur if annual reimbursements are not capped based upon verifiable data.
- The annual regional marketing expense reimbursement cap was not calculated using prior fiscal period sales activity as required by the agreement. The reimbursement cap used was established based upon sales tax estimated using Horizon reported gross tenant sales for the current fiscal period. The amounts reimbursed would not have been affected by using Horizon reported sales for the prior fiscal period since the reported sales for each fiscal period exceeded the threshold required to receive the maximum reimbursement. The Program Manager believes it was intended for the cap to be based upon sales tax remittances by tenants during the current fiscal period. The agreement may not achieve the desired results if the agreement terms are not carried out or the actual intent is not expressed.
- Documentation of expenditures on construction and development of the Outlet Mall has not been obtained from Horizon. The agreement required Horizon to provide documentation supporting the investment of at least \$50 million in Phase 1 completed in

⁸ The agreement provides that the aggregate amount of annual reimbursements will not exceed \$5.5 million over 10 years. However, the agreement does not require aggregate annual reimbursements of \$5.5 million over 10 years.

⁹ After certain regional marketing expenses submitted for reimbursement were disallowed by the Program Manager, reimbursements totaled approximately \$470,000 for the 2013 fiscal period.

¹⁰ Data submitted by the OTC to the City Treasurer's Office supporting sales tax payments does not separately identify sales tax remittances for each store location when payments are made for multiple store locations. Nearly half of the Outlet Mall tenants have more than one store location in Oklahoma City. Given this condition, determining sales tax remittances directly relating to Outlet Mall tenants requires reasonable allocation between the store locations.

2011 and at least \$65 million through Phase 3 completed in 2014. Amounts expended to date were to be reported upon the completion of each phase. The Oklahoma County Assessor's taxable market value for the Outlet Mall was approximately \$72.9 million for the 2015 tax year. The agreement may not achieve the desired development impact if the total required investment is not verified.

RECOMMENDATION (4)

OTC sales tax remittance data supporting sales tax payments received by the City Treasurer's Office for Outlet Mall tenants should be used to reasonably determine the annual regional marketing expense reimbursement cap. Further, a current listing of all Outlet Mall tenant store locations in Oklahoma City should be developed and maintained such that sales tax remittances for all store locations can be estimated and used when tenant store sales tax remittances are not individually reported by the OTC.

MANAGEMENT RESPONSE (4)

Management agrees. Staff is working with the City Treasurer's Office to reasonably determine the outlet mall remittance data. In addition, staff has initiated discussion with OTC to determine if obtaining site specific remittance data is feasible.

RECOMMENDATION (5)

Requiring separate OTC reporting for stores with more than one location in Oklahoma City should be considered for future agreements where sales tax remittances are used to determine the amount of incentives or assistance to be paid.

MANAGEMENT RESPONSE (5)

Management agrees. Staff from the Economic Development Program and the City Treasurer's Office are working with OTC to determine if such detail could be provided under routine remittances for future projects.

RECOMMENDATION (6)

Sales tax remittances by Outlet Mall tenants during the prior fiscal period should be used to calculate the regional marketing expense cap as stated in the Horizon agreement or the agreement should be amended to specify current fiscal period sales tax remittances be used.

MANAGEMENT RESPONSE (6)

Management agrees. Beginning with the contract fiscal year beginning August 2015, staff will utilize the prior year sales tax amounts to calculate the marketing reimbursement cap.

RECOMMENDATION (7)

Documentation of expenditures on construction and development of the Outlet Mall supporting a total investment of at least \$65 million should be obtained from Horizon.

MANAGEMENT RESPONSE (7)

Management agrees. Staff has obtained the investment information for the initial capital outlay along with Phase 2 and 3 expansions.

Boeing SIP Agreements

Both tested Boeing SIP agreements stated Boeing would, beginning in the second fiscal year of the agreements, submit incentive payment applications within 120 days of the fiscal year end or forfeit half of the incentive payments for that fiscal year. Boeing submitted incentive payment applications for \$333,000 and \$664,800 less than a month late and six months late, respectively, for the two agreements. The forfeiture condition within the agreements was not enforced for either payment. The Program Manager included this condition to encourage timely submission for cash outflow forecasting purposes. The agreement may not achieve the desired results if the actual intent is not expressed in the agreement terms.

RECOMMENDATION (8)

The Boeing SIP agreements should be amended to remove the condition requiring forfeiture of incentive payments for untimely submission of payment applications if the condition will not be enforced.

MANAGEMENT RESPONSE (8)

Management agrees. The Boeing #1 and #2 agreements were amended by the Oklahoma City Economic Development Trust on March 22, 2016 to allow the General Manager discretion regarding certain conditions and existing contracts will be amended as needed.

RECOMMENDATION (9)

All agreement conditions should be enforced and the merit of expected benefits should be fully weighed against the potential impact of forfeiture conditions. If the merit of the expected benefits given the potential impacts is unclear, making forfeiture enforcement an option at the option of the OCEDT General Manager rather than a requirement within the agreement should be considered.

MANAGEMENT RESPONSE (9)

Management agrees. All future agreements will include language providing the General Manager discretion regarding certain conditions and existing contracts will be amended as needed.

TIF District 2 Agreement In Lieu of Property Tax Payments

In lieu of property tax payments totaling \$154,863¹¹ due in 2014 for properties included in the first Midtown HC, LLC, TIF District 2 redevelopment agreements were not collected until 2015. The original Deeds of Declaration of Covenants (Covenants) relating to the agreement required payment of minimum annual property taxes by the property owner to the Oklahoma County Treasurer. The Program Manager became aware in early 2015 that the Oklahoma County Treasurer would return any minimum annual property tax payment amounts exceeding property tax assessments (the in lieu of tax portion) to the property owner. Opportunities for reinvestment of TIF funds or earned interest could be lost if in lieu of property tax payments are not collected when due.

All redevelopment agreements and covenants with such a requirement are being amended to require payment of in lieu of property taxes directly to the OCEDT according to the Program Manager¹².

RECOMMENDATION (10)

In-lieu of property tax payments should be collected when due to ensure those funds are available for reinvestment and/or interest earnings. Amendments to redevelopment agreements and related Covenants to require in lieu of property tax payments directly to the OCEDT should continue.

MANAGEMENT RESPONSE (10)

Management agrees. Staff has developed standardized processes to timely monitor the in lieu of property tax payments.

TIF DISTRICT 2 COVENANT AND SUBORDINATION AGREEMENTS

Covenants and subordination agreements relating to certain TIF District 2 redevelopment agreements included conflicting terms, need to be amended or updated, or were not handled consistently. While not affecting project completion, these issues could limit City Council and OCEDT oversight or affect the availability of TIF fund repayments for reinvestment or interest earnings.

¹¹ In lieu of property tax payments are calculated as the difference between minimum required annual tax payments in the Covenant for each property and the actual 2013 property tax payments for each property from the Oklahoma County Assessor's website.

¹² As of the end of audit fieldwork, all tested redevelopment agreements and related Covenants had been amended to appropriately reflect this requirement except for the 4th Street Properties, LLC, redevelopment agreement.

Conflicting Tax Roll Dates Included in Original Filed Covenants

The redevelopment agreements include a covenants section specifying what will be included in separate Covenant agreements for each redeveloped property including the date when the properties are expected to be added to the property tax roll (tax roll date). The Covenant for each property specifies the amount of minimum annual property tax payments due for the first eligible tax year after the tax roll date, is signed by the property owner, accepted by the City Council and OCEDT, and filed with the Oklahoma County Assessor. The tax roll dates included in certain original Covenants accepted and filed were different than the tax roll dates that had been included in the original agreements as shown below.

Development Agreement	Original Agreement Tax Roll Date	Accepted Covenants Tax Roll Date
Midtown HC, LLC, – 1 st Agreement	01/01/2011	01/01/2013
City Center Development, LLC	01/01/2013	12/31/2013
Midtown HC, LLC, - 2 nd Agreement	01/01/2014	12/31/2014

The tax roll dates in the covenant sections of the original agreements were eventually amended to match those in the original Covenants previously accepted and filed. However, the amendments¹³ were not clearly identified and were not made until months, or in the case of the first Midtown HC, LLC, years after the Covenants were in place. The tax roll date represents a significant agreement term, determining when minimum annual property tax payments should be expected to begin. City Council and OCEDT Trustees may not be fully informed of agreement conditions if tax roll date changes are not clearly identified when made.

RECOMMENDATION (11)

Redevelopment agreements with amended tax roll dates clearly identified should be presented to the City Council and OCEDT for approval at the same time related Covenants with tax roll dates differing from the original agreement are presented for acceptance.

MANAGEMENT RESPONSE (11)

Management agrees. All agreements identified have been amended and any agreements with discrepancies will be amended accordingly. In addition, staff is revising new documents to reduce redundancy between the agreement, related covenants and subordination agreements.

Tax Roll Dates in Agreement and Filed Covenants Amended to Conflicting Dates

The tax roll date in the second agreement with Midtown HC, LLC, was amended to December 31, 2014 while the tax roll date in the related Covenants was amended to December 31, 2013. Given the conflicting dates, it is unclear when minimum annual property tax payments relating

¹³ The purpose of these amendments was to specify in lieu of tax payments would be paid directly to the OCEDT as previously discussed.

to these properties should be expected to begin. In lieu of property tax payments¹⁴ totaling \$119,194 would have been due in 2015 if the 2013 date is correct or \$59,891 would be due in 2016 if the 2014 date is correct. Conflicting agreement terms could result in not receiving minimum annual property tax payments when due and those payments being unavailable for reinvestment or interest earnings.

RECOMMENDATION (12)

The correct tax roll date for the properties should be determined, the tax roll dates in the redevelopment agreement and related Covenants should be amended accordingly, and uncollected in lieu of property tax payments due, if any, should be collected.

MANAGEMENT RESPONSE (12)

Management agrees. On January 26, 2016 the Oklahoma City Economic Development Trust approved revised Covenants that were in agreement with the Economic Development Agreement.

Subordination Agreements Not Updated

Updated subordination agreements referring to the liens imposed within the amended Covenants for the second agreement with Midtown HC, LLC, accepted on March 31, 2015, have not been obtained from property lienholders. The subordination agreements on file refer to the liens in the superseded Covenants accepted on July 1, 2014. TIF fund recovery through minimum annual property tax payments may be more difficult if amended subordination agreements referring to the amended Covenants are not obtained.

RECOMMENDATION (13)

Amended subordination agreements referring to the liens in the amended Covenants for the second agreement with Midtown HC, LLC, accepted on March 31, 2015, should be obtained from the property lienholders.

MANAGEMENT RESPONSE (13)

Management agrees. The revised subordination agreements have been received.

Original Covenants Not Presented for Acceptance

The original Covenants relating to the first agreement with Midtown HC, LLC, were signed by the property owner on April 15, 2013 but a Joint Resolution to accept the Covenants was never presented to the City Council or OCEDT. Amended Covenants were jointly accepted by the City

¹⁴ The in lieu of property tax payments due were calculated as the difference between minimum annual tax payments in the Covenant for each property and 2014 and 2015 property taxes, respectively, for each property from the Oklahoma County Assessor's website.

Council and OCEDT on March 31, 2015 and March 24, 2015, respectively. City Council and OCEDT Trustees may not be fully informed of when minimum annual property tax payments are expected to begin if Covenants are not consistently presented for acceptance.

RECOMMENDATION (14)

Covenants to make minimum annual property tax payments signed by the property owners should be consistently presented to the City Council and OCEDT for acceptance.

MANAGEMENT RESPONSE (14)

Management agrees. Staff has implemented a process that includes checklists that ensures all covenants going forward will be accepted by the Oklahoma City Economic Development Trust and the City Council prior to payment.

REVIEW OF SIP ANNUAL JOB CREATION INCENTIVE SUPPORT

Review of documentation supporting annual job creation incentive payment requests could be more consistent, complete and clearly documented. Review procedures had been applied to documentation supporting all tested job creation incentive payments. However, the following weaknesses were identified in those procedures.

- The accuracy and completeness of Oklahoma Quality Jobs (OQJ) reports submitted by the California State Automobile Association to support incentive payment requests was not verified. Information on other incentive payment requests was selected for verification to actual payroll data. Incorrect OQJ reports could be submitted as support without detection if not verified to actual payroll data.
- Employer paid health insurance benefits offered to the newly created job positions were not confirmed. SIP agreements require added jobs to be eligible for health benefits substantially paid¹⁵ by the employer in addition to meeting average annual salary requirements. Health benefits offered to new full time employees were confirmed by the Program Manager during the audit for all tested SIP agreements. Incentive payments for created jobs of lower than expected quality could occur if offered health benefits are not confirmed.
- Review procedures applied and supporting documentation reviewed, including the source, was not completely and clearly documented.

¹⁵ The Continental Resources SIP agreement was the only tested SIP agreement in which the minimum expectation for health benefits was explicitly defined as an employer contribution of at least 50% towards the cost of health insurance or benefits offered to the new employees.

RECOMMENDATION (15)

A standard checklist should be developed and used to conduct and document reviews of annual job creation incentive payment request support. The checklist should minimally ensure:

- Job creation incentive payment requests are mathematically correct, the baseline number of jobs used to calculate the number of added jobs is accurate and added job average salaries and hours worked included are supported by company payroll data.
- Employer paid health insurance benefits have been offered to the created positions for which job incentive payments are being requested.
- Clear documentation of procedures applied and supporting documentation reviewed, including the source.

MANAGEMENT RESPONSE (15)

Management agrees. Staff has developed a standardized checklist that includes a worksheet to ensure each applicant will provide more consistent payroll information along with annual health insurance benefits.

TINKER AIR FORCE BASE (TAFB) PROJECT SIP AGREEMENT

Agreements directing repayments of GOLT Bond funds used for the KC-46A maintenance facility land purchase on behalf of TAFB are not in place. The City Council approved a Joint Resolution with the OCEDT on September 9, 2014 authorizing a \$23.5 million payment for the land purchase. The Joint Resolution contemplated repayments totaling approximately \$21.1 million to the City through Oklahoma Quality Jobs (OQJ) incentives applied for and collected by the Oklahoma Industries Authority¹⁶ (OIA) on behalf of TAFB. To this end, the Joint Resolution further included an expectation of negotiation by OIA with the U.S. Department of the Air Force and TAFB of agreements providing for:

- OIA receipt of necessary information from TAFB to apply for OQJ incentives for created maintenance facility jobs.
- OIA receipt of OQJ incentives on behalf of TAFB.
- OIA payment of received OQJ incentives to the City and Oklahoma County proportionally based upon respective funding from each for the land purchase with the City receiving the first \$5 million.

Maintenance facility operations allowing for OQJ incentive applications are not expected to begin until 2018. The ability to recover a significant amount of funds is at risk while these agreements are not in place.

¹⁶ The Oklahoma Industries Authority, an Oklahoma County beneficiary trust, acted as the fiscal agent for Oklahoma County, the City, and OCEDT in the \$44 million land purchase transaction. In addition to the \$23.5 million paid by the City, Oklahoma County was to contribute \$12.5 million and the U.S. Department of the Air Force and TAFB were to contribute \$8 million towards the purchase.

RECOMMENDATION (16)

Agreements directing the repayment of GOLT Bond funds used for the KC-46A maintenance facility land purchase from OOJ incentives applied for and received by OIA on behalf of TAFB as contemplated in the September 9, 2014 Joint Resolution should be actively pursued.

MANAGEMENT RESPONSE (16)

Management agrees. Staff has drafted an agreement for Oklahoma Industries Authority and the Oklahoma City Economic Development Trust regarding the repayment of GOLT bond funds used for the KC-46A maintenance facility land purchase. The agreement will be in place by June 30, 2016.

SEGREGATION OF RECEIPT VERIFICATION AND PAYMENT APPROVAL DUTIES

A single employee¹⁷ both verified the receipt of contractual benefits and approved the related payments. While no such payments were identified, payments without receipt of the contractual benefit could occur without detection when a single knowledgeable employee is solely responsible for both benefit receipt verification and related payment approval.

RECOMMENDATION (17)

Responsibilities for verifying receipt of contractual benefits and approval of related payments should be segregated.

MANAGEMENT RESPONSE (17)

Management agrees. The Administrative Specialist verifies whether contractual requirements are satisfied and the Economic Development Program Manager approves payment. Per the updated professional services policy, two signatures are applied to all economic development related payments.

¹⁷ While the Program Manager performed these duties for most of the audit period, these duties were assumed by a full-time Administrative Specialist hired in September 2014.



MEMORANDUM

The City of OKLAHOMA CITY



TO: Jim Williamson
City Auditor

THROUGH: James D. Couch
City Manager

FROM: Brent Bryant
Economic Development Program Manager

DATE: April 5, 2016

SUBJECT: Audit # 15-03 Economic Development Expenditure Audit

The following are Management's responses to the recommendations outlined in the recent Economic Development Expenditure Audit.

1. Management agrees. Staff has implemented processes that include checklists to ensure all requirements are met prior to payment. In addition, staff has received documentation supporting an investment in excess of \$38 million in investment for the Boeing Project that required a minimum investment of \$20 million and \$5.2 million in investment for the Boeing Project that required a minimum investment of \$5.1 million. The subordination agreement for the 10th & Broadway Parking, LLC has also been received. Staff has also initiated contract amendments for contracts that have unnecessary requirements for OCEDT and City Council approval.
2. Management agrees. Staff has implemented processes that include checklists to ensure all requirements are met prior to payment.
3. Management agrees. Staff has implemented processes that include checklists to ensure all contract requirements, including the issuance of the certificate of completion are met prior to payment.
4. Management agrees. Staff is working with the City Treasurer's Office to reasonably determine the outlet mall remittance data. In addition, staff has initiated discussion with OTC to determine if obtaining site specific remittance data is feasible.

5. Management agrees. Staff from the Economic Development Program and the City Treasurer's Office are working with OTC to determine if such detail could be provided under routine remittances for future projects.
6. Management agrees. Beginning with the contract fiscal year beginning August 2015, staff will utilize the prior year sales tax amounts to calculate the marketing reimbursement cap.
7. Management agrees. Staff has obtained the investment information for the initial capital outlay along with the Phase 2 and 3 expansions.
8. Management agrees. The Boeing #1 and # 2 agreements were amended by the Oklahoma City Economic Development Trust on March 22, 2016 to allow the General Manager discretion regarding the forfeiture of earned incentives.
9. Management agrees. All future agreements will include language providing the General Manager discretion regarding certain conditions and existing contracts will be amended as needed.
10. Management agrees. Staff has developed standardized processes to timely monitor the in lieu of property tax payments.
11. Management agrees. All agreements identified have been amended and any agreements with discrepancies will be amended accordingly. In addition, staff is revising new documents to reduce redundancy between the agreement, related covenants and subordination agreements.
12. Management agrees. On January 26, 2016 the Oklahoma City Economic Development Trust approved revised Covenants that were in agreement with the Economic Development Agreement.
13. Management agrees. The revised subordination agreements have been received.
14. Management agrees. Staff has implemented a process that includes checklists that ensures all covenants going forward will be accepted by the Oklahoma City Economic Development Trust and the City Council prior to payment.

Mr. Jim Williamson

Page 3

April 5, 2016

15. Management agrees. Staff has developed a standardized checklist that includes a worksheet to ensure each applicant will provide more consistent payroll information along with annual health insurance benefits.
16. Management agrees. Staff has drafted an agreement for Oklahoma Industries Authority and the Oklahoma City Economic Development Trust regarding the repayment of GOLT bond funds used for the KC-46A maintenance facility land purchase. The agreement will be in place by June 30, 2016.
17. Management agrees. The Administrative Specialist verifies whether contractual requirements are satisfied and the Economic Development Program Manager approves payment. Per the updated professional services policy, two signatures are applied to all economic development related payments.

We appreciate your professional review of the economic development program and the constructive recommendations.