



Internal Audit Report: Contract Managed Buildings Audit

Item 3D

October 19, 2016

Building Investment, Finance and Audit Committee

Report:	BIFAC:2016-137
To:	Building Investment, Finance and Audit Committee (BIFAC)
From:	Chief Internal Auditor
Date:	October 11, 2016
Strategic Plan Priority:	<p>Quality Homes:</p> <ul style="list-style-type: none"> • Improve Building Conditions • Maintain the Condition and Quality of New and Repaired Buildings <p>Service Excellence:</p> <ul style="list-style-type: none"> • Provide Excellent Customer Service • Demonstrate Value for Money and Public Accountability

PURPOSE:

To provide the Building Investment, Finance and Audit Committee (the Committee) with the Internal Audit report *Contract Managed Buildings Audit*.

RECOMMENDATIONS:

That the Committee receive the Internal Audit report *Contract Managed Buildings Audit*.

REASONS FOR RECOMMENDATIONS:

Background

Subsequent to a public Request for Proposal (RFP) process, in 2012 TCHC entered into contracts with third party property managers to subcontract property management of 12,017 units in 58 communities, including 2 seniors' buildings¹. This was the continuation of a property management subcontract program from prior years. These

¹ In 2012, via a RFP, 427 additional units were added to the CM building portfolio to bring the number of units in the CM building portfolio to 12,444.

buildings are known throughout TCHC as the 'contract managed buildings' (CM buildings).

Prior to TCHC issuing the next RFP for contract managed buildings, management asked Internal Audit to do a review of the contract managed buildings.

The signed contract (CM contract) for each of the four vendors (the CM vendors) selected includes a right-of-audit as well as full access to the premises. This is the first time TCHC exercised the right-of-audit.

Findings

Vendor Performance

We found that the CM vendors:

- Were not in compliance with the Key Performance Indicators (KPIs) that we reviewed; and
- Consistently exceeded annual operating budgets.

Key Performance Indicators

With respect to the KPIs we reviewed we found that:

- Some of the KPI targets for the CM vendors were unrealistic and generally unachievable;
- We also found that some KPI targets for direct managed buildings were not met by TCHC;
- There were KPIs not included in the CM contract that should possibly be included in the next RFP process for CM buildings; and
- The KPIs set out for the CM buildings were not necessarily in alignment with the KPIs used for direct managed buildings.

Some of these observations are in alignment with the findings contained in the final report from the Mayor's Task Force on Toronto Community Housing², in particular Recommendation 26:

That (TCHC) review current private sector management contracts adopting clear performance standards to ensure equity in tenant services, adequate small capital repairs and fair wages for staff...

Vendor Operating Budgets

CM vendor budgets did not include a budget for capital expenditures as TCHC is responsible for capital expenditures.

More importantly, there was no clear direction from TCHC to the CM vendors on the delineation between operating expenses and capital expenses. As such, there is an

² *Transformative Change for TCHC, A Report From the Mayor's Task Force on Toronto Community Housing* January 26, 2016

incentive for CM vendors to delay making operating repairs so that operating repairs turn into a capital expenditure.

TCHC Administration, Monitoring, and Performance Assessment of the CM Contracts

We found that there was insufficient monitoring and review by TCHC over the course of the CM contracts of:

- CM vendors not achieving KPI targets; and
- CM vendor budget over spending.

In addition, to our knowledge, over the course of the CM contracts there has been no effective reporting about the savings that have been achieved by using CM vendors.

There is a cost in staff resources to effectively administer, monitor, and assess the performance of the CM vendors. We are not convinced that this function has been adequately resourced.

The Value Proposition in Having Contract Managed Buildings

The value proposition with respect to having CM buildings must take into consideration not only the financial aspects of the contracts (including the cost of administering the contracts), but also other things such as the quality of customer service provided, and the level of customer satisfaction upon receiving those services.

We have recommended that a thorough review of the 'CM building value proposition' be made prior to issuing the next RFP for CM buildings.

Recommendations

We have made six Recommendations in this report to address the matters noted above.

More importantly, the Recommendations in this report address issues relating to

- (i) The development, structure and oversight of the current CM contract for the purpose of strengthening the accountability of a future contract, as well as
- (ii) Addressing the value for money and strategic implications of the CM building initiative.

Management's Action Plan with respect to our Recommendations is attached to this report as Appendix A.

IMPLICATIONS AND RISKS:

In the contract managed buildings program there is a risk that public funds are not being used economically or effectively, resulting in a negative impact on the public's perception of the contract vendors, TCHC, and their reputations.

SIGNATURE:

“Michael Vear”

Michael Vear, CPA, CA, CPA (Illinois)
Chief Internal Auditor

ATTACHMENT:

1. Internal Audit Report: *Contract Managed Buildings Audit*

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Contract Managed Buildings Audit

REPORT

October 6, 2016

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EXECUTIVE SUMMARY

Background

Subsequent to a public Request for Proposal (RFP) process, in 2012 TCHC entered into contracts with third party property managers to subcontract property management of 12,017 units in 58 communities, including 2 seniors' buildings¹. This was the continuation of a property management subcontract program from prior years. These buildings are known throughout TCHC as the 'contract managed buildings' (CM buildings).

Prior to TCHC issuing the next RFP for contract managed buildings, management asked Internal Audit to do a review of the contract managed buildings.

The signed contract (CM contract) for each of the four vendors (the CM vendors) selected includes a right-of-audit as well as full access to the premises. This is the first time TCHC exercised the right-of-audit. All agreements are for three years, plus two one-year renewals. As at the date of this report, the agreements with the CM vendors are in the last one-year renewal period.

The CM buildings contracts are administered and monitored by the TCHC Contract, Compliance & Delivery Unit (CM Unit) of the Asset Management Department.

Audit Objectives

The objectives of this assignment were to provide CM vendors and TCHC management with an objective and independent assessment of the vendor's compliance with the terms of the contract in the following areas:

- Rent Geared to Income (RGI) calculations;
- Finance;
- Work orders; and
- Daily operations of the buildings.

In addition, we looked at the content and effectiveness of the following during the course of our review:

- The Corporation's RFP and CM contracts; and
- Key Performance Indicators.

Resources did not permit us to review arrears, vacancy management, and annual unit inspections of the CM buildings.

Methodology and Scope

Our methodology included, but was not limited to:

- Reviewing policies, procedures and forms relevant to the process;
- Interviewing staff;
- Examining documents; and
- Performing analytical work.

¹ In 2012, via a RFP, 427 additional units were added to the CM building portfolio to bring the number of units in the CM building portfolio to 12,444.

Sample sizes for work order and RGI calculations assessment were identical for each vendor. Samples were chosen randomly.

Sample sizes were chosen to provide an indication of a vendor's (i) compliance or non-compliance with certain terms of the contract and (ii) ability to meet certain performance measurements. As such, we caution the reader that there are inherent limitations in the results set out in this document.

Findings

Vendor Performance

We found that the CM vendors:

- Were not in compliance with the Key Performance Indicators (KPIs) that we reviewed; and
- Consistently exceeded annual operating budgets.

Key Performance Indicators

With respect to the KPIs we reviewed we found that:

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More importantly, there was no clear direction from TCHC to the CM vendors on the delineation between operating expenses and capital expenses. As such, there is an incentive for CM vendors to delay making operating repairs so that operating repairs turn into a capital expenditure.

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We have recommended that a thorough review of the 'CM building value proposition' be made prior to issuing the next RFP for CM buildings.

Recommendations

We have made six Recommendations in this report to address the matters noted above.

More importantly, the Recommendations in this report address issues relating to

- (i) The development, structure and oversight of the current CM contract for the purpose of strengthening the accountability of a future contract, as well as
- (ii) Addressing the value for money and strategic implications of the CM building initiative.

Management's Action Plan with respect to our Recommendations is attached to this report as Appendix A.

As well, the CM vendors have acknowledged our detailed findings, and the CM Unit has indicated that improvements have been ongoing.

We would like to take this opportunity to thank the staff and management of the TCHC Asset Management Department, particularly the CM unit, and the Finance Department for their cooperation and assistance during this audit.

The same appreciation is extended to the CM vendors' site staff and Head Office staff.

Prepared by:

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Manager, Internal Audit

Approved by:

Michael Vear, CPA, CA, CPA (Illinois)
Chief Internal Auditor, Internal Audit Department

#	Recommendation	Agree/Disagree	Management's Action Plan	Timeline
	<p><i>b) The savings realized to TCHC by using CM vendors to operate certain TCHC buildings.</i></p>		<p>Financial performance of CM vendors relative to direct-managed properties.</p>	
5	<p><i>With respect to CM vendor contracts, TCHC Management</i></p> <p><i>a) Formally align responsibility for all aspects of the CM vendor contracts (administration, monitoring, performance assessment, RGI calculation reviews, financial performance, etc.) under one unit;</i></p> <p><i>b) Assess the staffing complement required to properly and adequately administer, monitor, and assess performance of the CM vendor contracts, and staff accordingly.</i></p>	Agree	<p>Assessment of requirements to monitor CM vendor contracts is ongoing. The assessment involves evaluating resources to monitor the CM vendors under the framework of the new contracts.</p>	May 1, 2017
6	<p><i>TCHC Management consider the value for money proposition and strategic implications of the CM buildings initiative prior to issuing the next RFP for CM vendors.</i></p>	Agree	<p>Action is completed and business case for contract management to be provided to the Business, Investment, Finance, and Audit Committee on October 19, 2016.</p>	October 19, 2016