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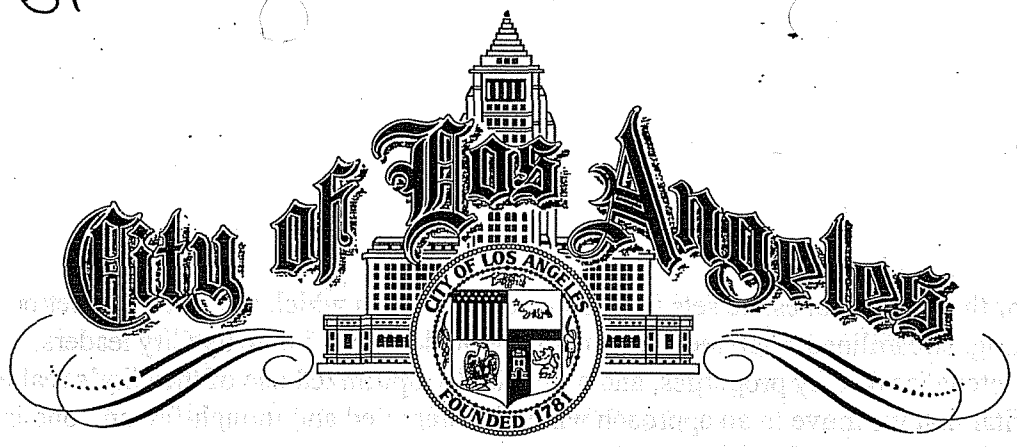

OFFICE OF
CONTROLLER

LAURA CHICK
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July 15, 2004

The Honorable James K. Hahn
The Honorable Rockard J. Delgadillo
The Honorable Members of the City Council
City Hall
200 North Main Street
Los Angeles, CA 90012

Dear Mayor Hahn, City Attorney Delgadillo, and Members of the City Council:

The City of Los Angeles owns thousands of pieces of property, totaling billions of dollars, from the fifth largest airport in the world to slivers of undeveloped surplus property. In August of last year, I conducted an audit of the City's management of its real estate assets. The audit found that the City has no overarching vision and no strategic plan, but instead handles its very valuable real estate on an ad-hoc, piecemeal, and transactional basis. Most troubling is the fact that the City does not even have a single, central database of what it owns.

In an effort to maximize the public's benefit of the vast properties we own, I am releasing, "A Vision and Strategy for the City's Real Estate."

The need for a comprehensive vision was certainly apparent during the City's deliberation on a new police headquarters and the purchase of the Transamerica building. These critical decisions occurred in the absence of a clear picture of what the City needs, and what the City already owns and leases.

AUDITS & GOVERNMENTAL
EFFICIENCY

JUL 19 2004

This vision for the City's real estate sets forward a new approach which will promote better decision-making, streamlined implementation of strategic decisions made by City leaders, improved maintenance of City properties, and a financially optimized use of the City's real estate assets. It is vital that we move to an approach which is integrated and thoughtful, and one in which we anticipate and plan for future needs.

I'm looking forward to the City's leadership using both the audit and the strategic vision to revolutionize the way the City does its real estate business.

Sincerely,

Laura N. Chick

LAURA N. CHICK
City Controller

A VISION AND STRATEGY FOR THE CITY'S REAL ESTATE
July 11, 2004

In April 2004, the City Controller of the City of Los Angeles asked KH Consulting Group (KH) to develop a vision for effective management and use of the City's real estate assets. Included in the vision were to be:

Guiding principles and policies which should govern the use and management of City owned or leased properties
Critical strategic goals to be achieved by the City
Ideal distribution of roles and responsibilities across City departments
Significant initiatives to be launched, including potential legislative directions to be considered over the coming year
Recommendations for the development of analytic tools, methods, and skill sets.

METHODOLOGY

In completing this vision, KH reviewed best practices in other jurisdictions and in the private sector to develop potential improvements to the systems in place. Building on KH's research completed for the "Performance Audit of the Asset Management Division (AMD) of the General Services Department (GSD) of the City of Los Angeles" (dated August 14, 2003)[1], the KH consulting team:

Benchmarked asset management functions of several other large and medium-sized cities to identify potential best practices that might be applied to the functions

Interviewed more than 21 key City leaders, including City Council members, senior City officials and staff responsible for key asset management decisions, and prominent members of the real estate community in the City of Los Angeles. Appendix A lists those interviewed.

Visited selected City properties and other facilities.

[1] Source: Posted on the website of the Office of the Controller, City of Los Angeles.

INTRODUCTION

The City of Los Angeles owns thousands of pieces of property, ranging

> *from* the unique and magnificent City Hall *to* slivers of undeveloped surplus property slated for transfer to neighboring land owners,
>
> *from* the fifth largest airport in the world *to* pocket parks around which neighborhoods form,
>
> *from* Police and Fire stations sited to optimize response times *to* maintenance yards that provide room for storage of critical materials,
>
> *from* offices housing administrative and management personnel *to* public use facilities visited daily by hundreds of residents in need of City services.

In the midst of this diversity, no one is consistently and thoroughly considering policy direction for the use and management of City real estate. As displayed in Exhibit 1, the City's oversight responsibilities are complex because some departments are:

> Council-controlled departments with commissions (e.g., Fire, Parks and Recreation, Police)
>
> Council-controlled departments without commissioners (referred to as line departments)
>
> Proprietary departments with commissions (Los Angeles World Airports (LAWA), Harbor Department, and Department of Water and Power (DWP)).

Only sporadic review is provided of key City real property issues. Elected and professional City leaders, City Council members, and appointed commissioners are presented with a bewildering array of transactions for approval without a context for good decision-making and its long-term implications.

The recent proposed acquisition of the Transamerica-Broadway building is symptomatic of the lack of policy and direction in City real property management. The City Council was considering acquiring the property before a consensus had formed about which City Departments and employees would be housed in the facility. Within a few weeks of its anticipated closing date, competing proposals for the use of the property included: 1) temporary space for Police Administration and Headquarters while a permanent facility is to be built, 2) permanent space for Police Administration and Headquarters, and 3) replacement of leased City office space.

The credibility of the City in the commercial real estate marketplace can be called into question because a predictable and expeditious review process does not occur, even after negotiations have been conducted in good faith.

Transactions of this size should be reviewed in a context that considers such issues as:

What is the City's strategy for occupying office space? What are the criteria for leasing space?

Has the deal been structured to offset maintenance costs or generate revenues through retail leases or other agreements?

How does this acquisition fit into a five-year plan for property management?

- What other acquisitions are anticipated, and what will be the impact on the City's budget or debt capacity?

- What are the programmatic implications of relocating City offices, and how will this fit into the current and projected need for City residents to have convenient access to critical services?

The current process requires three well-informed and well-intentioned City officials – the Mayor's Chief of Staff, the Chief Legislative Analyst (CLA), and the City Administrative Officer (CAO) – to consider <u>all</u> transactions that involve the movement of City staff, and to make recommendations to the Information Technology and General Services (ITGS) Committee of the City Council on dozens of small transactions. Their attention could be better devoted to consideration of major directions and policy issues, or to offer guidance on decisions about deferred maintenance, which has a direct impact on the long-term value and the safe and efficient operations of City agencies. Central policy issues associated with property management are not systematically or routinely raised, analyzed, and addressed.

Acquisition, disposition, and leasing of properties, while important, are only part of a comprehensive asset management approach to the administration of real property. The City can only provide services to its residents in safe, well-managed properties. Planned and effective maintenance and operation of City property are also central to financially responsible asset management. Identifying opportunities for revenue generation using City properties will ease budget constraints, thereby helping the City meet the needs of its residents.

The purpose of this paper is to outline an alternative approach to management and use of City property, which will permit better decision-making, streamlined implementation of strategic decisions made by City leaders, improved maintenance of City properties, and a financially optimized use of the City's real estate assets.

IMPROVEMENTS TO CITY REAL PROPERTY ASSET MANAGEMENT

On the basis of best practices proven effective in both the public and private sector, the City of Los Angeles should address four key areas that would dramatically improve the asset management of the City's real property.

1. ***Establish Guiding Principles for Property Decisions Supported by the Mayor and City Council.***

While some individuals involved in the process have articulated approaches to issues of property management, there are no officially approved guidelines, which can be applied to frame decisions. The City Council and Mayor should adopt policies that are consistent with overarching Real Property Guiding Principles that they have been debated and approved. For example, the following six overarching guidelines would provide a structure within which property policy decisions and transactions are considered:

Suggested Real Property Guiding Principles

1. ***City Property is located to maximize accessibility, safety and security, and convenience of residents and users of City services.***
2. ***City Property maximizes safety and security, efficiency, and effectiveness of City workers.***
3. ***City Property is acquired, disposed of, and managed based on life-cycle cost methodologies.***
4. ***City Property produces revenues where appropriate.***
5. ***City Property is designed to be a permanent community asset where appropriate.***
6. ***City Property is environmentally responsible.***

Within these guiding principles, individual policies can be formed, and major transactions can be proposed and reviewed. For example, policies in support of the life-cycle cost methodology would change how the City considers donations of property, and should lead to changes in the way the City budgets for maintenance. Major transactions, such as the example of the acquisition of the Transamerica-Broadway building, would be governed by at least Guidelines 1, 2, and 3.

2. ***Implement a Strategic Property Management Approach to City-Owned Real Property.***

When a city adopts a Strategic Property Management Approach (coupled with the six guidelines), it can expect that property will support the city's programs and policies; property will be safe, clean, and useful for residents, visitors, and City employees; and property will cost less per-square-foot to build and maintain. There are five major elements of Strategic Property Management that the City should adopt. Responsibility

for these elements should be shared by the City's General Services Department (GSD), the Mayor's Office, the three proprietary departments, and, in some cases, the line departments.

a. Complete the Property Database So That It Includes All City Property.

A property database is a necessary and fundamental prerequisite for effective management of City-owned real property assets. It must include information about all properties owned by the City, be it Council-controlled or under the purview of proprietary departments. The database should include:

- Location
- Square footage or acreage
- Tenants and percentage of occupancy
- Purpose
- Improvements
- Date of acquisition
- Major maintenance
- Deferred maintenance

This database will permit the accumulation of benchmarking data to facilitate decision-making while implementing property management decisions, and provide documented institutional memory in the face of changes in personnel. It will form the basis for planning, maintenance, and operational decisions. The database must be kept up to date, available to all interested City staff, and coordinated and managed by GSD's Asset Management Division (AMD).

Maintaining the value of properties in the database would be a difficult and expensive task, as property value can change quickly. Such information may be necessary, however, with the advent of grant funding criteria under programs administered by the U.S. Department of Homeland Security.

b. Establish a Lease Management Program.

The City should have a consistent approach to the management of leases. The Harbor Department and Los Angeles World Airports (LAWA) can be viewed as large real estate operations, serving as landlords responsible for security and operations of facilities that house transportation firms. Managing and negotiating leases are central to their mission. For most other City departments, lease management is a task that needs to be managed well, but is not critical to their operations. From a City-wide perspective, however, effective lease management:

- Facilitates informed decision-making about lease versus buy decisions
- Improves the City's bargaining position regarding terms and conditions and costs

- Helps assure space will be available for program needs.

All lease programs, which generate revenues for the City and regardless of who manages them, should include:

- A continually updated database with standard information, including:
  - Tenant information
  - Start and end dates for leases
  - Revenue information
  - Other terms and conditions relevant to the operation of the lease
  - Termination/renewal options
- A system to trigger needed actions to be taken at least six months before the options expire
- Regular market rate reviews
- Links to the City-owned property database

Where the City is a tenant, staff should keep track of landlord information, lease costs and payment history, termination and renewal options, and operational terms and conditions. The City should develop a space plan, and conduct market rate reviews to be better positioned when the time comes to renegotiate the leases. Well before lease renewal, the City should consider:

- Whether it is preferable to lease or purchase, including consideration of such issues as cost, planned expiration of grant-funded programs, and projected staffing changes

- Under what conditions incurring the considerable disruptions and expenses associated with moving would be preferable to renewing the leases

- Projected space requirements for all departments, including short- and medium-term projections of staff

Finally, the City should standardize and streamline the processes for leasing property, coordinating efforts of the Mayor, the City Attorney, the responsible departments, and the City Council.

c. *Establish a Preventive Maintenance Program.*

The City should assure that properties, once acquired, remain assets and do not become liabilities with an ever-increasing backlog of unfunded maintenance. To do this, effective asset managers implement a regular preventive maintenance program. For properties with major structures, replacement of major building systems should be scheduled and priced so that considered decisions can be made

regarding investing in or disposing of the properties. All major building systems should be included, especially:

- Roofing
- Exteriors
- Windows
- Elevators, escalators
- Heating, ventilation, and air condition (HVAC) systems
- Electrical
- Plumbing
- Fire protection
- Communications
- Interiors, paint, carpeting, floors, built-ins, etc.

All City-owned buildings should be included in the program. These investments in building systems are cost-effective because:

- City properties will retain their value.
- Properties will be less expensive to maintain and will last longer.
- The negative impact of downtime on critical City programs will be minimized.
- Preventive maintenance programs can accelerate money-saving retrofit projects that generate real savings in energy efficiency.

GSD should be responsible for planning and overseeing preventive maintenance for building structures on all City property with the exception of the proprietary departments. The only exception to this assignment should be for departments that choose to establish separate Facilities Divisions with staff specifically trained to plan and manage preventive maintenance programs that GSD has reviewed and approved. Finally, the Mayor and City Council should appropriate sufficient funds to assure that building systems are maintained as planned.

d. Assign Responsibility for Day-to-Day Building and Property Management.

The City needs to assign responsibility for day-to-day management of each of its real property assets. Through this effort, the City's properties would remain safe; and, attention to minor repairs would reduce theft and liability for accidental injuries. Good day-to-day building management makes properties look welcoming, comfortable, and attractive. A welcoming environment for the public is created, improving the perception of the City. Most importantly, small problems stay small, and do not grow through neglect.

Large real estate operations typically assign responsibility for buildings to property managers, who have offices in the buildings managed, and oversee

everything from planning of major maintenance, to contracting for unplanned repairs, to assuring that space is completely leased.

- For large buildings owned by the City, a full-time manager is appropriate.
- Multiple smaller buildings can be combined under a single full-time manager, or can be individually assigned to a part-time manager.
- Property-related responsibilities for large facilities, such as large parks, should be consolidated under the overall facility manager.

As the City centralizes preventive maintenance planning, the minimal typical responsibilities would be:

- ***For office space housing City employees***, the responsible staff member would oversee day-to-day operations and routine maintenance.
- ***For facilities that are built, leased, and operated by tenants***, such as airline terminals, the responsible staff member would assure that the City's property rights and residual values are maintained.
- ***For facilities, such as police and fire stations, libraries, and parks***, the responsible staff member would assure that the building or property is safe; regular maintenance and routine upkeep are performed, including cleaning, landscaping, and HVAC systems; and voice and data communications are maintained.

Although there may be exceptions, in general the staff members responsible for this function should report to the departments responsible for the preventive maintenance planning for the property or facility.

e. Present for Approval a <u>Five-Year Capital Plan</u> and an Annual Real Estate Capital Program, Which Reflects Guidelines and Policy Directives.

Property decisions will impact City departments, staff, residents, and service providers for many years. Decisions are interrelated and good decisions must consider, for example:

- Whether other space is planned for acquisition or disposition that affects the property being discussed
- Whether space in properties leased by the City should be increased or decreased
- What programmatic or policy decisions have been made that will impact property needs

- Whether the affected property has significant deferred maintenance or other liabilities that will affect its continued financial viability.

The City should develop and annually update a property plan that:

- Identifies property requirements
- Allows the establishment of priorities in asset management that respond to the guiding principles
- Addresses programmatic or policy needs.

This plan will permit analysis of alternative uses of property to assure they are put to the best use, and will provide a structure for leaders to exercise policy direction and guidance for medium- and long-term decisions. The plan will include consideration of major maintenance program needs and costs so that transactional decisions will take into account the overall condition of the portfolio.

GSD should develop the ***Five-Year Capital Plan*** for Council-controlled departments. GSD should work collaboratively with these departments to:

- Identify existing and projected program-related property needs, including replacement of inadequate facilities
- Detail the criteria used to prioritize real estate programs.

The proprietary departments should develop and present similar plans for approval.

Annually, a one-year Real Estate Capital Program should be prepared and presented to the City Council and Mayor that implements the first year of the rolling five-year Plan. The approval of the program would include approval of all property transactions thereafter that meet agreed-to standards and limits. In this way, for example, additional transactional reviews would not be required for:

- Amendments to existing leases that do not increase costs by more than $25,000 per year and are co-terminous with the existing lease
- Disposition of surplus property valued at less than $50,000
- Office space changes affecting less than 30 staff members.

3. Focus Elected City Decision-Makers on Real Property Strategic and Policy Issues.

The City must consistently and thoroughly consider policy directions in dealing with its real estate. The City's real property transactions range from complex, high-profile, costly, and important ones (such as the acquisition of the Transamerica-Broadway building), to a high volume of minor ones (such as the amendment of leases in small buildings to augment existing spaces): The extensive and time-consuming review of

these transactions – whether major or minor transactions – must be replaced by consideration and resolution of such critical policy issues as:

> What should the City's strategy be for leasing versus buying property?
>
> How can the City best use proceeds from the sale of property, so that one-time revenues are devoted to capital programs that benefit the City as a whole, and are not diverted to meet short-term, local operating needs?
>
> How can the City change its budgeting process to assure that adequate funds are set aside to maintain owned property, especially new property developed using bond proceeds?

While the City Council can and should establish the policies that will support effective City property management, the Council needs support in:

> Developing policies that support the guiding principles for City properties
> Assessing the impact of potential policy initiatives on the portfolio
> Reporting on the effectiveness of the City in meeting property objectives.

Examples of policies that have been considered and passed include:

> The Historic Core policy, which sought to locate City offices in a specific area in downtown Los Angeles so that the City could act as an anchor tenant spurring local economic development of the area
>
> The Non-Profit Leasing policy, which requires that leasing City property to a non-profit organization be documented as the highest and best use of the property, and spells out the anticipated responsibilities for property management by the non-profit lessee
>
> The Space Standards Policy, which provides guidelines for space occupancy.

These three examples should serve as models of practices to be emulated. (Note: While some currently view the Historic Core policy as outmoded, it is nevertheless an example of a policy direction approved by the City Council that helped guide selection of many leased properties.)

As policies and guiding principles are debated and passed giving better direction regarding the intent of the City Council to staff, the City Council can delegate the implementation of transactions below a designated, small dollar threshold to the implementing departments.

4. *Maximize Financial Value of or Return on Properties.*

Practices used in commercial real estate to develop and maximize the value of land and buildings are, in many cases, entirely viable for the City of Los Angeles to research and consider. Typical examples implemented by other municipalities include:

Ancillary commercial uses of city properties
Trade of higher value city property in exchange for property developed to meet specific city needs
Commercial leases of property rights, easements, and entitlements.

The City of Los Angeles does not currently take sufficient advantage of such opportunities, however. The primary means of generating revenue through property lies in the disposal of surplus property, although City policy goals of housing, park space, and economic development are properly considered more important than revenue generation. Proceeds from the sale of surplus property are one-time revenues; the proceeds of these sales should be considered capital funds.

More lucrative to the City are revenue streams that extend beyond a single year. The City should also look for opportunities where the highest and best use of occupied and fully used property calls for the transfer or sale of the asset to developers or other Governmental agencies. Incentives should be established so that City departments that occupy property actively consider how their property can generate the greatest value for the City. Without strong incentives, departmental staff struggling to achieve the departmental mission view property changes as at best a distraction, and at worst as an impediment to being able to accomplish identified goals and objectives.

VISION

The City of Los Angeles owns or controls one of the largest and most significant portfolios of real estate in the United States. The renovated Los Angeles City Hall, preserved with future generations in mind, provides a clear example of a municipal policy and decision coupled with a strategic vision. This study has found that realistic and efficient management of City real property can serve similar ends by:

Fostering an economic renaissance in the community
Establishing important civic assets that are embraced by neighbors
Forming community and cultural hubs with parks, libraries, government service centers, meeting places, and accessible transportation
Nurturing a place where City workers can serve both the needs of the public and visitors with pride
Leaving a legacy for future generations to enjoy and value.

The ancient Greeks and Romans understood the value of such a vision in building infrastructures that have lasted more than two millennia. For centuries, Europe has understood this strategic approach, creating beautiful plazas around government buildings for residents and visitors to gather, relax, and enjoy. U.S. examples of investments in civic centers are in Phoenix, Seattle, Minneapolis, New York City, and Washington, D.C. – all of which have recognized that they will be in the business of government for many generations and, accordingly, have made investments in their facilities that will stand the test of time. When the Port Authority of New York-New Jersey embarked on building the World Trade Center in an area that was economically blighted, many debated if the investment was viable. Despite the tragedy of September 11th, the World Trade Center reaped its return-on-investment multi-fold, while revitalizing the southern end of Manhattan, stimulating residential and commercial expansion, serving as a junction for more than 250,000 commuters every day, and attracting visitors from all over the world.

An ongoing criticism of the City of Los Angeles is that it lacks a center. This criticism is even harder to overcome when the City has not strategically invested to form community and civic centers – possibly forming mini-centers – throughout the diverse geographic area. The Marvin Braude San Fernando Valley Constituent Service Center in Van Nuys is an example of the potential of one of these types of complexes. The technological age may make it easier for City employees to telecommute and residents to access City services electronically, thereby, making the City less dependent on brick-and-mortar infrastructure. The value of investments in government facilities, however, can be recouped and such facilities have multiple purposes in serving the public and forming community hubs.

Los Angeles can and should be a national leader in the management of real property assets. This vision can be realized when leaders of the City of Los Angeles:

Consider the value of the investment in property
Assess the long-term implications of real estate decisions
Begin to articulate plans for the effective use of the City's real property to contribute to the needs of City departments, its communities and their residents, and visitors.

EXHIBIT 1
CITY OF LOS ANGELES:
CURRENT ASSIGNMENT OF
RESPONSIBILITY FOR ASSET MANAGEMENT

RESPONSIBILITY	INITIAL ANALYSIS	REVIEW/ RECOMMENDATION	APPROVAL	IMPLEMENTATION
Council-Controlled Departments With Commissions (Fire, Parks, Police, etc.)				
Development of Policy	NA[2]	#Commission #ITGS[3]	#Commission	#Department
Acquisition of Property (leasing, purchase)	Department	#MFC[4] #ITGS #Commission #Proposition Q, F, etc. #Committees	#City Council #Mayoral Veto Power	#GSD #Department #City Attorney #Engineering
Property Improvements	Department GSD	#MFC #ITGS #Proposition Q, F, etc. #Committees	#City Council	#Engineering
Disposal of Property	Department GSD	#MFC #ITGS #Commission	#City Council #Mayoral Veto Power	#GSD #Department #City Attorney #Engineering
City Personnel Movements	Department	#MFC	#City Council #Mayoral Veto Power	#GSD #Department
Property Maintenance and Operations	Department	NA	Budget Review	#Department
Council-Controlled Departments Without Commissions				
Policy Development	GSD	#MFC #ITGS	#City Council #Mayoral Veto Power	#GSD
Acquisition of Property	GSD	#MFC #ITGS	#City Council #Mayoral Veto Power	#GSD #Department #City Attorney #Engineering
Disposal of Property	GSD	#MFC #ITGS	#City Council #Mayoral Veto Power	#GSD #Department #City Attorney #Engineering
Property Improvements	GSD	#MFC #ITGS	#City Council #Mayoral Veto Power	#Engineering

[2] NA = Not Applicable
[3] Information Technology and General Services (ITGS) Committee of the City Council
[4] Municipal Facilities Committee (MFC), consisting of the Mayor (or his Chief of Staff), CLA, and CAO.

RESPONSIBILITY	INITIAL ANALYSIS	REVIEW/ RECOMMENDATION	APPROVAL	IMPLEMENTATION
City Personnel Movements	Department with GSD	#MFC #ITGS	#City Council #Mayoral Veto Power	#GSD #Department
Property Maintenance and Operations	GSD	#CAO	Budget Review	#GSD #Department #City Attorney
Proprietary Departments (LAWA, Harbor, DWP)				
Policy Development	Department	#Commission	#Commission #City Council with Mayor Veto Power for certain policies	#Department
Acquisition of Property	Department	#Commission	#City Council #Mayoral Veto Power	#Department #City Attorney
Property Improvements	Department	#Commission	#City Council #Mayoral Veto Power	#Department
Disposal of Property	Department	#Commission	#City Council #Mayoral Veto Power	#Department, #City Attorney
City Personnel Movements	Department	NA	NA	#Department
Property Maintenance and Operations	Department	#CAO	Budget Review	#Department

APPENDIX A
INTERVIEWS CONDUCTED

MUNICIPAL FACILITIES COMMITTEE (MFC)	
Tim McCosker	Office of the Mayor
Ron Deaton	Office of the Chief Legislative Analysis (CLA)
William Fujioka	Office of the City Administrative Officer (CAO)
MFC STAFF	
Gerry Miller	Office of the Chief Legislative Analysis (CLA)
Jody Yoxsimer	Office of the City Administrative Officer (CAO)
David Mora	Mayor's Office of Economic Development
CITY COUNCIL	
Wendy Greuel	City Council Member
Bernard Parks	City Council Member
PRIVATE SECTOR	
Alan Aufhammer	CB Richard Ellis
David Kluth	Studley
Mark Weinstein	MJW Investments
Jerold Neuman	Allen Matkins
Dan Rosenfeld	Urban Partners, LLC
CITY GOVERNMENT	
Alvin Y. Blaine	General Services Department (GSD)
David Pascal	General Services Department (GSD)
Reginald Jones-Sawyer	Asset Management Division (AMD) of the General Services Department (GSD)
Jon Kirk Mukri	Department of Recreation and Parks
Julianna Cheng Fontayne Holmes	Department of Libraries
Spencer Ballard Paul Green (by telephone)	Los Angeles World Airports (LAWA)
OTHER GOVERNMENT	
Office of the Director of Real Estate	City of Seattle