

**Arizona State University
Third Party Housing
Audit Report
February 9, 2018**

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Summary: The Third Party Housing audit was included in the Arizona State University (ASU) FY2018 audit plan approved by the Arizona Board of Regents (ABOR) Audit Committee and ASU senior leadership. The audit focused on the financial and operating provisions of the lease agreements for the Manzanita Hall and Villas at Vista del Sol student housing facilities on the Tempe campus and the Casa de Oro student housing facility on the West campus (facilities) for the fiscal years 2016 and 2017. This audit is in support of ASU's mission of effective management of financial resources and focus on efficient operations of all levels of the University.

Background: ASU entered into ground lease agreements with American Campus Communities (ACC) for student housing projects located on land owned by the University that is ground leased to ACC. Upon completion of the projects, ACC transfers title to the facilities to the University, subject to a leasehold interest under which ACC will maintain and operate the facilities. The University has no obligation to support the facilities financially or to guarantee occupancy.

Three such agreements were entered into during 2011 including the Manzanita and Villas at Vista del Sol facilities on the Tempe campus and the Casa de Oro facility on the West Campus. These agreements have specific terms by facility. In addition, there are combined revenue hurdles that tie the performance of the three facilities together for additional rent payments due ASU. To date, the combined revenue hurdles have not been met.

The Manzanita and Casa de Oro facilities are managed under a Marketing and Licensing agreement between ASU and ACC. As part of this agreement, ASU markets the properties and collects the rent from the students, which is remitted to ACC each term with ASU retaining a percentage of the rent. The Villas at Vista del Sol facility is managed under a sublease agreement which involves semi-annual payments to ACC. In addition, ASU is compensated to provide security and residential life support for each of these facilities.

Audit Objectives: The objectives of the engagement were to confirm compliance to the financial and operating provisions of the ground lease agreements and related marketing and licensing agreements. Specifically, the following areas were included:

- Ensure rent payments, as defined in the lease agreements, are made in a timely and accurate manner;
- Ensure payments related to security and residential life staff are received according to contractual terms;
- Ensure the restoration reserve is maintained at appropriate levels;
- Ensure compliance with the maintenance, operation, and management terms;

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- Ensure terms and conditions of relevant marketing and lease agreements are adhered to;
- Confirm advisory committee activities are occurring; and
- Identify opportunities for improvement.

Scope: The scope of the audit focused on the financial and operating provisions of the leases for the Manzanita Hall and Villas at Vista del Sol facilities on the Tempe campus and the Casa de Oro facility on the West campus for the fiscal years 2016 and 2017.

Methodology: Our audit consisted of tests and procedures necessary to provide a reasonable basis for expressing our opinion. Specifically, audit work consisted of interviews with representatives of University Housing, review of documents required under the leases to ensure operational compliance, and substantive tests including the following areas:

- Confirming rent payments were made to ACC based on contractual requirements by:
 - Verifying the accuracy of rent payments by recalculating rents due under the Marketing/Licensing and Master Sublease Agreements for the 2016 and 2017 Fall and Spring terms.
 - Ensuring rent payments were made timely.
- Confirming the 2016 and 2017 residential life fees and security fees were paid to ASU according to the terms of the leases.
- Confirming the advisory committee fulfilled its responsibilities by reviewing meeting agendas and supporting documentation for two meetings.
- Performing a physical walkthrough of each of the facilities to confirm properties are maintained in class A condition as defined by the lease agreements.
- Analyzing maintenance work orders for the time-period of September 2016 through August 2017 to ensure requests are managed according to lease requirements.
- Confirming the accuracy of the capital repair reserve accounts by performing the required reserve calculations and reviewing the schedules maintained by ACC including validating expenditure detail, and reviewing descriptions for expenditures for appropriateness.
- Confirming that the Manzanita facility met the LEED (Leadership in Environmental Energy and Design of the U.S. Green Building Council) requirements under the leases.

Conclusion: Overall, University Housing was generally in compliance with the key provisions of the leases. Rent payments are being accounted for in an accurate and timely manner. The advisory committee is meeting semi-annually ensuring appropriate oversight of the agreements. In addition, the properties are generally being maintained consistent with the

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lease terms including maintaining the capital repair and reserve accounts; however, processes to ensure maintenance requests are addressed in a timely manner require improvement.

Specifically, review of the maintenance requests indicated pervasive issues with timely response, repeat requests, and maintenance requests not being appropriately entered or closed in the maintenance tracking system. Inadequate tracking and monitoring of resident requests prevents management from ensuring that student requests are being addressed in a timely and effective manner as required by the lease agreement.

In addition, further controls are necessary to ensure the residential life fee is monitored and adjusted annually as required by the lease. Contractually, ASU has the right to pass on increased costs (up to 3% annually) to ACC related to the Residential Life costs to support the Manzanita and Casa de Oro Facilities. Likewise, if actual costs are less than the defined fee, ASU is required to reduce the subsequent year's fee by the proportional amount. ASU Housing has not administered certain lease provisions to ensure necessary adjustments were made on an annual basis.

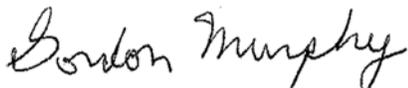
The control standards we considered during this audit and the status of the related control environment are provided in the following table.

General Control Standard (The bulleted items are internal control objectives that apply to the general control standards, and will differ for each audit.)	Control Environment	Finding No.	Page No.
Reliability and Integrity of Financial and Operational Information			
<ul style="list-style-type: none"> • Gross Revenue hurdles are monitored appropriately. 	Reasonable to Strong Controls in Place	N/A	N/A
<ul style="list-style-type: none"> • Security Fees and Residential Life Fees due ASU from ACC are appropriately reimbursed to ASU. 	Opportunity for Improvement	2	7
<ul style="list-style-type: none"> • Capital Repair Reserve Accounts are maintained at correct levels by ACC. 	Reasonable to Strong Controls in Place	N/A	N/A
<ul style="list-style-type: none"> • Rent payments are accurate based on the Marketing/Licensing and Master Sublease Agreements with ACC. 	Reasonable to Strong Controls in Place	N/A	N/A
Effectiveness and Efficiency of Operations			
<ul style="list-style-type: none"> • The Advisory Committee has appropriate oversight of lease performance. 	Reasonable to Strong Controls in Place	N/A	N/A

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<ul style="list-style-type: none"> Maintenance requests are managed in a timely and effective manner. 	Opportunity for Improvement	1	5
Safeguarding of Assets			
<ul style="list-style-type: none"> The facilities are maintained in Class A Condition as required by the leases. 	Reasonable to Strong Controls in Place	N/A	N/A
<ul style="list-style-type: none"> ACC designed and constructed the facilities according to the LEED requirements in the leases. 	Reasonable to Strong Controls in Place	N/A	N/A
Compliance with Laws and Regulations			

We appreciate the assistance of University Housing representatives during the audit.




Gordon Murphy, CPA, CFE, CGMA
Internal Auditor Senior

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Executive Director

Audit Results, Recommendations, and Responses

1. Processes to ensure maintenance requests are addressed in a timely manner require improvement, especially as it relates to Villas at Vista del Sol.

Condition: ACC is responsible to make reasonable efforts to respond to resident submitted work orders within 24 hours of receipt; however, review of the ticketing system (TMA) resulted in several data integrity and processing issues indicating that requests are not being addressed appropriately.

Criteria: Students have the ability to enter work orders directly into TMA or to call ACC directly who then enters the work order into the system. ACC personnel is responsible for managing the work queue including assigning tickets in order of prioritization and ensuring that necessary work is completed and updated in the system accordingly.

Cause: Consistent management of TMA is not occurring to ensure that maintenance requests are addressed in a timely and effective manner.

In addition, various data integrity issues were noted related to tickets within TMA including the following items:

- 17 work orders were entered with a close date prior to the request date.
- 194 work orders were closed on a single day due to the system not being updated appropriately when the work was completed.
- Due dates are not consistently updated within the system.

Effect: Maintenance requests are not addressed in a timely manner resulting in a high volume of repeat requests, especially related to the Villas at Vista del Sol facility. For example, 128 of the 845 (15%) work orders submitted from September 2016 through August 2017 related to this facility were repeat requests. In addition, due to the inconsistent use of the system, ACC is not able to effectively track and monitor the status of open maintenance requests or calculate average days to close requests.

Recommendation: Existing processes related to entering maintenance requests should be reviewed to ensure that defined processes are in place governing entering, updating and closing maintenance requests. Additional reporting and monitoring of repeat requests should be implemented to identify potential service or system issues in a proactive manner.

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Management Response: University Housing has re-evaluated, improved and implemented an updated internal process to ensure maintenance requests are addressed in a timely manner, which will reduce duplicate requests, improve service delivery and enhance the learning environment for ASU students. Moreover, it will better enable ACC to effectively track and monitor open maintenance requests. The new process includes, enhanced staffing, more robust scheduling and an accountability processes. To ensure success, University Housing has established a plan for quarterly reviews of our collective progress with ACC.

More specifically, our team within University Housing and ACC staff are conducting quality assurance checks and mutually agreeing the room passes the inspection after a work order has been completed. Further, the Housing facilities staff will review Duty Reports and follow up with on call staff (ASU & ACC) about facility issues that happened over night, weekend, and break to ensure all are aware of issues, progress and resolution.

Additionally, University Housing is developing additional steps:

- Create turn board for ACC properties
- TMA training, best practices, access with ACC
- TMA Dashboard monitoring by Director of Facilities & Sr. Coordinator
- Updated the room inspection checklist
- We are in the process of exploring the feasibility of Mobile TMA and other software programs that can enhance our historical data tracking.
- Definition of level A – Recommend change to APPA to create measurable standards comparable to ASU owned buildings.
- Creating student worker positions to walk, inspect, create WO and track all common spaces level of cleanliness and damage.
- Monthly meeting with ACC to review reports to Housing director on various KPI'S.

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2. ASU Housing is not administering certain lease provisions to ensure necessary adjustments are made on an annual basis related to the Manzanita and Casa de Oro Facilities.

Condition: ASU Housing is not administering certain lease provisions as described in the lease. Specifically, sections 9.1.3 of the lease agreements define the “Res Life Fee” due to ASU annually. This amount should be adjusted up or down in each subsequent year based on reasonably estimated costs of the prior year; however, this is currently not being done.

Criteria: The defined “Res Life Fee” should be increased or decreased based on reasonably estimated costs on an annual basis subject to contract limitations. Any such adjustment is due to ACC by August 15th for the subsequent year’s payment.

Cause: ASU Housing has not administered the lease provisions to ensure necessary adjustments were made on an annual basis.

Effect: As a result of not administering the lease provisions, ASU may have lost potential revenue related to increased operational costs.

Recommendation: ASU Housing should develop a procedure to administer this provision of the lease and implement processes to adjust the annual fee based on the defined calculations by August 15th of each year or if necessary, amend the lease to provide additional direction.

Management Response: University Housing accepts the recommendation and will develop a new procedure to administer this provision of the lease and implement processes to adjust the annual fee based on the cost allocation within the aforementioned lease by August 15th of each year. We plan to implement the procedure before August 15, 2018.

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