



PORTLAND DEVELOPMENT COMMISSION:
Developers comply with Disposition and Development
Agreements, but PDC does not monitor adequately

A REPORT FROM THE CITY AUDITOR
September 2008



Office of the City Auditor
Portland, Oregon



CITY OF
PORTLAND, OREGON

OFFICE OF THE CITY AUDITOR
Audit Services Division

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September 24, 2008

TO: Tom Potter, Mayor
Sam Adams, Commissioner
Nick Fish, Commissioner
Randy Leonard, Commissioner
Dan Saltzman, Commissioner
Charles A. Wilhoite, Chairman, Portland Development Commission
Bruce Warner, Executive Director, Portland Development Commission

SUBJECT: *Audit – Portland Development Commission: Developers comply with Disposition and Development Agreements, but PDC does not monitor adequately (Report #358)*

Attached is Report #358 containing the results of our audit of Portland Development Commission's Disposition and Development Agreements (DDAs).

The Mayor and the Portland Development Commission Executive Director have responded to the audit, and we have included their written responses at the back of this published report.

We make several recommendations in the report, and as a result we ask the Executive Director of the Portland Development Commission through the Commission Chair and the Mayor to provide a status report on implementation of those recommendations within one year.

We appreciate the cooperation and assistance we received from Portland Development Commission staff as we conducted this audit.

GARY BLACKMER
City Auditor

Audit Team: Drummond Kahn
Fiona Earle
Shea Marshman

Attachment

PORTLAND DEVELOPMENT COMMISSION:

Developers comply with Disposition and Development Agreements, but PDC does not monitor adequately

Summary The Portland Development Commission (PDC) uses Disposition and Development Agreements (Agreements) to spur development related to economic growth, affordable housing, and urban renewal plans. PDC enters into these Agreements with developers and partner agencies to fulfill City goals.

We found that developers met many of the requirements of the 11 Agreements we reviewed. For example, they renovated three properties and 99 affordable housing units. Developers also constructed three commercial properties, fifteen market value residences, and one affordable home.

However, PDC was unable to consistently confirm that developers met the Agreements' basic requirements because PDC does not follow its own policy for certifying the completion of every Agreement.

In addition, PDC cannot demonstrate that Agreements fully accomplished other goals and purposes, such as finding and retaining commercial tenants.

Further, PDC is not monitoring the Agreements' goals sufficiently once projects are completed. Therefore, PDC cannot determine if Agreements have accomplished their intended purposes and justified the public investments.

Background PDC is the urban renewal and redevelopment agency for the City of Portland. As such, PDC is mandated to implement the vision and goals adopted by City Council relating to urban renewal, economic development and affordable housing.

PDC becomes involved in a development when the private market does not develop properties in Urban Renewal Areas (URAs) in ways that meet the City's public goals. Therefore, to encourage development that serves specific public purposes, PDC sometimes buys properties within URAs. These properties are intended to be sold to developers for projects such as commercial and housing developments.

One of the tools that PDC uses to achieve the City's development goals is a Disposition and Development Agreement (Agreement). Agreements are complex legal contracts used when a publicly-funded property owned by PDC is sold to a developer for the purpose of improvement or redevelopment.

Agreements set out unique terms under which PDC and developers make property improvements to meet specific development goals. Agreements define the timeline for construction, the continuing requirements, and the conditions of funding (by PDC or another lender) that will make successful project completion more likely. PDC enters into Agreements on behalf of the City and is responsible for ensuring that the City's interests in these Agreements are met.

PDC enters into Agreements with specific goals and purposes in mind. For example, some Agreements are primarily intended to encourage housing development, while others are intended to create retail development. These purposes are important – they show the reasons for a development, which may vary. Therefore, the success of an Agreement depends not only upon the immediate bricks and mortar requirements, but also on the achievement of broader, long-term goals and the demonstrated delivery of public benefits.

The Agreements list their specific purposes in one or more areas of the legal documents that approve them. The following examples (see Figure 1) illustrate how the purposes are described in three of the eleven Agreements we considered. Below each example are several elements that developers are expected to meet to achieve the Agreement's larger purpose.

Figure 1 Examples of Agreement purposes

Agreement 1 purpose
<p>"...redevelopment of the property, pursuant to this Agreement, will help achieve the community and City goals of neighborhood revitalization, wealth creation and creation of job opportunities."</p> <p><i>Examples of elements</i></p> <ul style="list-style-type: none"> ● Construction will include a safe and friendly pedestrian environment ● Developers will make a good faith effort to attract locally owned commercial tenants ● The creation of approximately 14 new jobs
Agreement 2 purpose
<p>"...restore and preserve an historic building, to rehabilitate a permanent single room occupancy hotel and create approximately 99 units of housing in the center of the City affordable to tenants with incomes at or below 40 percent of the area's median family income"</p> <p><i>Examples of elements</i></p> <ul style="list-style-type: none"> ● New plumbing ● Renovation of the lobby, interior details, and emergency exit ● 99 affordable housing units
Agreement 3 purpose
<p>"...redevelopment of the property, pursuant to this Agreement, will result in the creation of quality jobs, ... will encourage use of alternative modes of transportation, [and] serve as a model of well-designed, high quality urban mixed-use development"</p> <p><i>Examples of elements</i></p> <ul style="list-style-type: none"> ● A three story medical office building ● At least 1000 square feet of retail space ● Approximately 170 jobs

Source: Excerpts obtained by Audit Services from Disposition and Development Agreements

Some requirements of each Agreement are immediate (such as constructing 1,000 square feet of commercial space), while goals tend to be long-term (such as filling that commercial space with businesses).

PDC managers told us their efforts to monitor Agreements focus on whether developers met specific requirements, rather than an assessment of the Agreements' broader purposes and long-term goals.

This is a concern for two reasons:

- First, limiting monitoring to the requirements of the Agreements could exclude important purposes for the Agreement, as well as hinder overall monitoring of the Agreement's results. For example, the specific requirement of 1,000 square feet of retail space only helps meet the Agreement's purpose if the space is adequately occupied within a reasonable amount of time.
- Second, PDC's practice of only monitoring narrowly defined requirements overlooks important long-term goals and purposes that it should monitor. For example, monitoring the number of jobs created as a result of an Agreement can demonstrate progress toward the City's economic development goals.

Therefore, we considered the broader purposes behind the Agreements, whenever they are set out in the Agreement documents and appendices or in the authorizing PDC Board resolutions.

Although Agreements are not the only tools that PDC uses to facilitate development, managers told us that Agreements are very important development tools. Agreements can take years to complete and are managed by PDC project teams that include project managers, construction managers, financial specialists, and legal counsel. In addition, Agreements require the approval of PDC's Board of Commissioners and a PDC Resolution stating how the development will meet specific City goals.

Agreements we reviewed for this audit were tied to seven of the City's goals (see Figure 2).

Figure 2 City goals included in the Agreements Reviewed

Commercial Developments	Promote the City's economic development goals
Neighborhood Revitalization	Produce market rate (rather than affordable) housing as part of a larger development to improve livability in a geographic area
Revitalization / Renovation	Seed commercial and/or residential growth; renovate or re-use an existing property; and/or perpetuate revitalization of a specific URA
Affordable Housing	Provide low income housing
Employment / Job Creation	Promote economic growth through new jobs
Community Orientation / Access	Engage specific neighborhoods and/or increase public access and use in a geographic area
Transit Oriented Developments	Promote use of public transportation

Source: Audit Services' summary from PDC Board Resolutions

During this audit, PDC announced a major change in its organizational structure. We considered the impact of this change on our audit findings and concluded the change does not affect the Agreements we considered in this audit. Moreover, we conclude the organizational change does not affect PDC's core mandate or its capacity to fulfill the City's development goals through Agreements.

This audit was included in the City Auditor's FY 2007-08 audit schedule. The audit topic was suggested by PDC.

Objectives, Scope, and Methodology

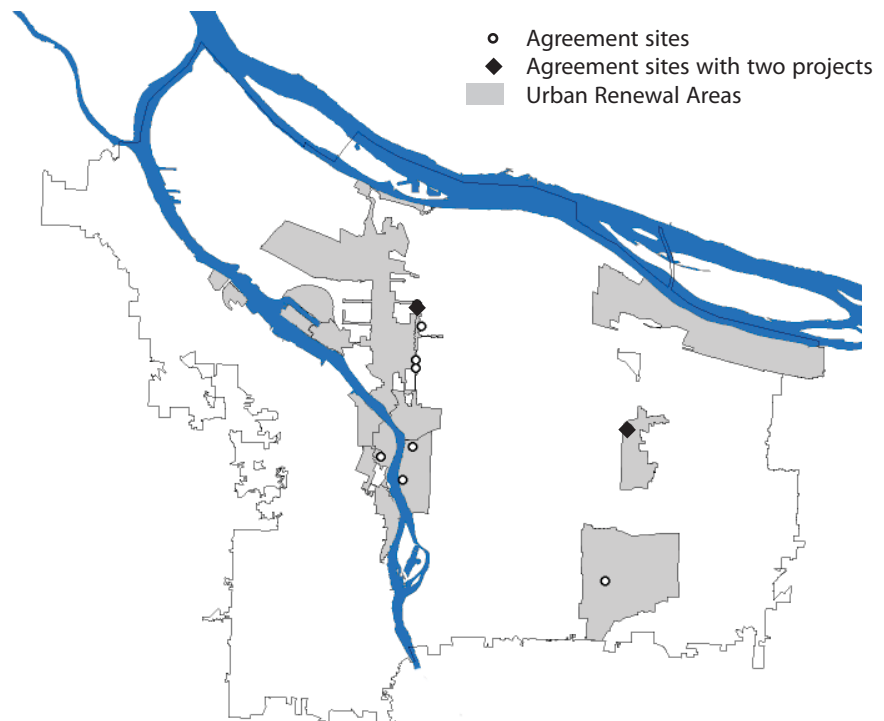
Our two objectives in conducting this audit were to:

- Determine whether PDC is receiving the contractual requirements from developers as stated in the Agreements
- Evaluate the adequacy of PDC's internal monitoring and compliance assessment processes for these Agreements

To achieve these objectives, we reviewed all eleven Agreements approved between 2003 and 2005¹. This time frame included Agreements that were substantially complete as well as more recent neighborhood-focused projects.

The Agreements reviewed include developments in five of Portland's eleven Urban Renewal Areas (see Figure 3).

Figure 3 Agreement sites and Urban Renewal Areas



Source: Geocoded map created by Audit Services

In order to gather information to answer our objectives, we reviewed the Agreement documents and visited the development sites. We also obtained a copy of each of the PDC Board Resolutions associated with the Agreements to identify the City goals the Agreements were designed to meet. We examined PDC's policies and procedures that relate to the Agreements.

¹ One of the Agreements PDC included in the list of Agreements approved between 2003 and 2005 is a Purchase and Sale Agreement rather than a Disposition and Development Agreement. We chose to include it in this audit because PDC staff explained that the project was essentially the same as a DDA in all but contract format.

In addition, we reviewed PDC documents so we could assess whether PDC monitored Agreements. We also interviewed project managers or project team members assigned to each Agreement, as well as senior managers from PDC's operational departments.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our 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.

PDC receives requirements from developers

Developers met many Agreement requirements

Developers and partner agencies met many Agreement requirements, which contributed to the achievement of some City goals.

Goal: Revitalization and Renovation - Under one Agreement, an old building was demolished and replaced by new construction. In other Agreements, three existing buildings were renovated.

Goal: Neighborhood Revitalization - Fifteen market value single family homes were built.

Goal: Affordable Housing - Ninety-nine affordable housing units in a historic building downtown were renovated and now house low income individuals, some of whom are in recovery from chemical dependency. One single family affordable home was built.

Goal: Transit Oriented Development - A new building with direct access to a light rail station, and a parking garage were constructed.

Goal: Community Oriented Development - Developers and PDC worked with community members to design the project plans for the Agreements.

A renovated commercial building now fully occupied by commercial tenants



Source: Audit Services Division

The site of a demolished building, this lot now houses a new commercial building



Source: Audit Services Division

A new parking structure
that provides access to
the light rail station



Source: Audit Services Division

PDC cannot demonstrate whether developers met some Agreement goals for commercial development

At the end of our audit fieldwork, we found that some commercial development goals were not fully met.

Commercial space remains unfilled - Of the seven Agreements that include commercial space, we found that four commercial buildings are partially empty and three are full. According to PDC estimates for building size and occupancy, the developments created approximately 304,000 square feet of commercial space, but about 42,000 square feet of commercial space were empty.

One PDC manager told us that it is sometimes difficult to fill commercial space in URAs because negative public perception of the neighborhood and lack of other businesses in the area make commercial tenants hesitant to lease the space. We recognize the difficulties that PDC faces in developing URAs and acknowledge that project teams assist developers in their efforts to fill the properties.

However, at the time these Agreements were signed, PDC did not clearly define realistic expectations for the time frame in which commercial space will be filled.

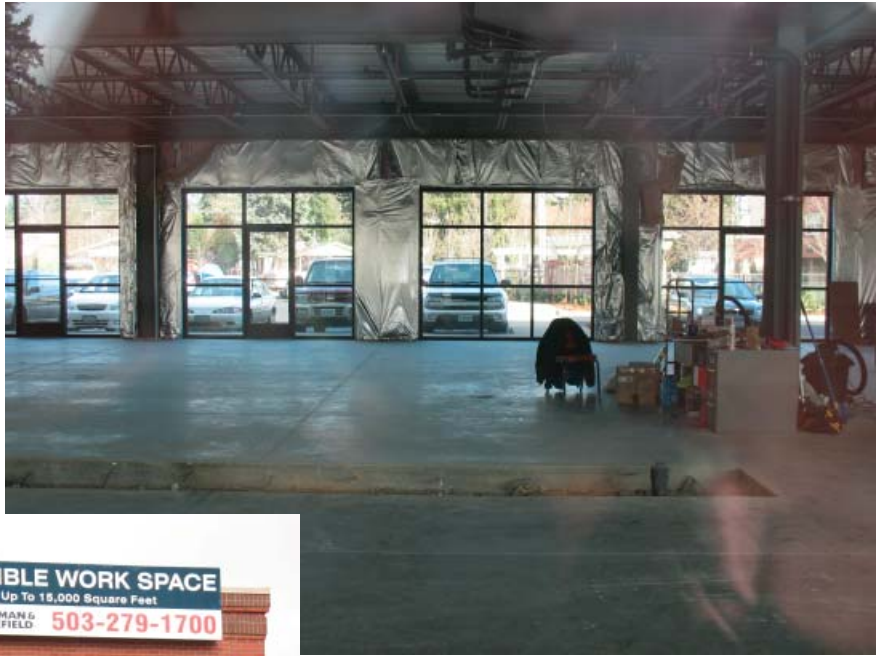
Currently, PDC judges the post-construction success of a commercial development according to the professional opinion of PDC development staff, rather than assessing the development against formal standards. If PDC underestimates the time it will take to lease commercial space, significant problems may result. For example, an inability to fill the commercial space in one of the Agreements we considered has caused the developer to pursue reorganization under the rules of Chapter 11 bankruptcy.

Job creation numbers are unconfirmed - PDC is also unable to demonstrate whether the Agreements created the number of jobs expected. Under the Agreements, a total of 484 jobs were anticipated based on estimates related to the size of the buildings.

By the end of our audit fieldwork, PDC was unable to provide evidence of job creation. However, when we visited the Agreement sites, we saw people working. Therefore, we attempted to verify the anticipated jobs through sources outside PDC. We were able to confirm the existence of 166 jobs. PDC told us as many as 520 jobs may have been created, but only provided evidence of 212 jobs.

PDC managers told us that some additional job creation information is collected for Agreements that are partially funded through the Quality Jobs Program, but that this information is not shared with project management staff due to concerns about the release of confidential employee information. Further, PDC considers the creation of new jobs to be a long-term goal rather than a specific legal requirement that should be monitored.

While some individual employee information may be sensitive and kept confidential, there is no reason that data on the number of employees hired as a result of the Agreement should be protected. If PDC is unable to demonstrate whether long-term job creation goals were met, they will be unable to ensure that developers met the goals or to evaluate project success.



Empty commercial space in Agreement properties

Source: Audit Services Division



PDC is not adequately monitoring Agreement compliance

As the urban renewal agency for the City of Portland, PDC enters into Agreements on behalf of the City and is responsible for ensuring that the City's interests are met. PDC policy requires that they monitor the fulfillment of requirements contained in the Agreements during as well as after construction. Monitoring construction compliance and other conditions helps PDC ensure that the responsible parties in the Agreement perform required tasks.

PDC does not adequately monitor Agreements during construction

Monitoring during construction helps to ensure that contract provisions are met and that physical structures are built to meet immediate building requirements contained in the Agreements. To evaluate the degree to which monitoring takes place, we compared requirements listed in the Agreements with documents that demonstrate requirements were met.

PDC's administrative policies require that PDC issue a certificate of completion (CC) that is signed by the Executive Director upon project completion. This certificate is intended to certify that developers have completed all construction obligations contained in the Agreement. Nine of the eleven Agreements we reviewed required a CC. At the end of our audit fieldwork, PDC was only able to provide three of the nine certificates, even though the buildings were completed. However, by the time this report was published, a CC had been completed for each of the Agreements we reviewed.

Lack of timely evidence to support the completion of Agreement requirements makes it difficult for PDC to demonstrate that the requirements were met. It also makes it difficult to demonstrate that PDC was monitoring during construction.

PDC does not adequately monitor Agreements after construction

Monitoring after construction helps to ensure that all the purposes of developments continue to be met. For example, in order for the City to meet affordable housing goals, it is important that low income housing remain available to tenants at certain income levels over time. In addition, to meet both housing and economic development

goals, buildings need to be maintained to ensure that they continue to benefit the community.

If PDC is not monitoring Agreements post-construction, they would not know whether Agreement purposes are being met. Post-construction, PDC should have appropriate policies in place to direct the monitoring process. Information collected through monitoring can then be used to demonstrate success or identify areas for improvement.

Our review of PDC's post-construction monitoring identified two areas of concern.

In some cases, PDC lacks policies to monitor the achievement of City goals after construction is completed - PDC development resources are dedicated to the construction phase of projects, but none are specifically directed toward post-construction monitoring. This means that (unless the development includes affordable housing units) once a project is complete there is no formal expectation for PDC to assess the physical condition of the building. For Agreements with strong community involvement, managers told us that they anticipate that community members will inform them if the property begins to deteriorate. However, PDC managers told us PDC has little authority to respond to problems even if local residents complain.

Although PDC does not monitor most Agreement goals, they record the continuing requirements for Agreement properties in the title deeds. For example, one of the Agreements restricts the types of commercial businesses that may occupy the building. However, if developers or future property owners fail to meet the requirements, PDC depends on community members to ensure that properties continue to be used as intended. This means, for instance, that individual residents or neighborhood groups would have to take legal action against the owner.

In other cases, PDC has adequate policies in place to monitor delivery of some long-term Agreement requirements post-construction, but lacks internal controls to ensure that monitoring occurs - We found three areas of concern. First, PDC policy requires that the Executive Director sign

a CC for every Agreement project. As discussed earlier, PDC did not fully comply with this policy. Managers told us PDC policy requires a CC for each Agreement, but does not specify the timeframe in which the certificate will be signed.

Second, PDC monitors affordable housing developments to help ensure that they are maintained and managed professionally. However, as currently structured, the monitoring program does not fulfill this function.

A renovated building
containing single
resident occupancy
affordable housing units

Source: Audit Services Division



We visited the site of an Agreement that provides affordable housing units. We observed that the building, which was renovated in 2005, appeared well-maintained and was serving low income residents. However, the most recent report that PDC received from the property management showed problems that PDC had not taken action to address.

Only one year after completion of the Agreement, PDC discovered the management agency's operating costs were about \$42,000 over budget. It took almost two years for PDC to receive a building

inspection report they requested from the management agency. Further, as of the end of our audit fieldwork, PDC had not yet reviewed the annual management report for 2007.

Third, in an attempt to promote economic development, several Agreements required the creation of jobs. PDC includes job creation tools such as loans and tax incentive programs in these Agreements, and is responsible for making sure that the programs are monitored.

As described earlier in this report, PDC was unable to demonstrate whether the jobs anticipated in the Agreements were created. We found that PDC has tools they could use to gather some employment data. However, we found that PDC only collects job creation and employment information for a few of its Agreement projects. In addition, when job creation data is tracked, the information is not routinely shared with the project management staff responsible for including programs to promote employment in the Agreements. Therefore, employment data cannot be used to improve Agreements in the future.

We reported similar concerns about PDC's internal controls and monitoring in three earlier audit reports;

- We raised concerns about insufficient internal controls as they relate to PDC's staff compliance and internal practices in our September 2005 audit report, *Portland Development Commission Internal Controls: Policies are in place, but authorizations and documentation are often lacking.*
www.portlandonline.com/shared/cfm/image.cfm?id=92322
- Findings in our June 2006 audit report, *Portland Development Commission: Economic development efforts effective, but improvements needed to measure and manage future success,* showed data used in PDC's monitoring of job creation was unreliable.
www.portlandonline.com/shared/cfm/image.cfm?id=118133
- Findings in our July 2008 audit report, *Housing Tax Abatements: Oversight inadequate to ensure program goals,* showed that PDC does not adequately monitor affordable housing.
www.portlandonline.com/shared/cfm/image.cfm?id=204795

Recommendations

As a result of only monitoring requirements, PDC is unable to determine whether goals and purposes of the Agreements have been met. Therefore, PDC cannot determine if developers complied with all the terms of these Agreements, nor whether PDC is meeting the City's development goals through Agreements.

We recommend that the Mayor and the PDC Board of Commissioners ensure that PDC:

1. Develop specific policies for monitoring Agreement projects post-construction.

PDC has a general policy statement that they will monitor compliance with Agreement requirements. More specific, detailed policies and procedures are needed to ensure monitoring of both Agreement requirements and goals takes place. PDC's monitoring of an Agreement's success should include its broader purpose and goals to fully demonstrate the delivery of public benefit. In addition, since PDC depends on members of the community to inform them if developers fail to meet the Agreement terms, PDC should make sure that staff are available to act upon community concerns.

2. Develop and communicate realistic timeframes to fill commercial space at the time an Agreement is signed.

We acknowledge that filling commercial space in some parts of the City can be a challenge. Clearly defining realistic expectations for the timeframe in which commercial space will be filled may help PDC hold developers accountable for meeting Agreement goals and may help PDC to meet the City's goals.

3. Develop a policy that requires the collection of data for all job creation anticipated under an Agreement and regularly communicate findings within PDC as well as to the public.

Collecting and reporting job creation data will help PDC evaluate and assess performance, identify problems and solutions, and communicate results to management and the

public. This, in turn, may help PDC adjust and revise efforts for future Agreements so they can make informed decisions about the employment programs for use in future development projects.

4. Ensure that established monitoring systems and policies are carried out and functioning as intended.

If PDC is to hold developers accountable for the requirements contained in Agreements and ensure that City goals are met, it is essential that PDC carry out its requirements in the Agreements as well. As identified in this and three prior audits, PDC's monitoring policies are not adequate to ensure that monitoring takes place. PDC's monitoring policies and systems should be individually assessed to make sure they are adequately designed and effectively implemented.

RESPONSES TO THE AUDIT



Office of Mayor Tom Potter
City of Portland

September 10, 2008

Mr. Gary Blackmer
City Auditor
City of Portland
1221 SW 4th Avenue, Room 310
Portland, Oregon 97204

Dear Auditor Blackmer:

Thank you for the opportunity to review the Development Agreement Audit conducted by your office at the request of the Portland Development Commission.

I have reviewed the four recommendations:

1. Develop specific policies for monitoring DDA's post construction.
2. Develop and communicate realistic timeframes to fill commercial space.
3. Identify a better way to measure job creation.
4. Ensure established monitoring systems and policies are able to measure effectively.

Given this work was initiated by the PDC, I am confident they will take whatever steps are necessary to address your recommended improvements. Their track record for follow-up is solid. From your September 2005 and June 2006 audits, which contained a total of 17 recommendations, 13 have been completed, 3 are in progress and one is under review.

As evidenced in this audit, it is clear that PDC continues to strive to ensure DDA's meet their policy and regulatory objectives. Through improved communication, management controls and the recent reorganization of the agency, PDC is constantly improving its service delivery and seeking better methods to ensure performance agreements are met.

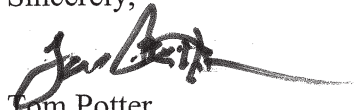
I am particularly interested in how the Auditor's Office may assist PDC in finding a more reliable mechanism to measure job creation. Since job creation is one of the City's top priorities, I am asking City auditors to help identify indicators to ensure a more

dependable assessment of our success in creating new jobs. I encourage PDC and the City Auditor's Office to work together toward that end.

In light of the many improvements made at PDC in the past three years, it is important to note that there remain external market factors which are beyond PDC's control. The slowing economy, the weakening condominium market, and recent failures of major financial institutions have affected the City's and our private partner's ability to fulfill policy goals. I am sure these are having an effect on PDC's abilities to ensure some of the compliance variables – specifically building occupancy. These factors should all be taken into consideration when evaluating whether the development projects are successful or not.

Again, thank you for your work on this audit.

Sincerely,

A handwritten signature in black ink, appearing to read "Tom Potter", with a long horizontal flourish extending to the right.

Tom Potter
Mayor

Charles A. Wilhoite
Commission Chair

September 4, 2008

Bertha Ferrán
Commissioner

Mr. Gary Blackmer
City Auditor
City of Portland
1221 SW 4th Avenue, Room 310
Portland, Oregon 97204

John C. Mohlis
Commissioner

RE: Response to Audit Report - PDC Disposition and Development Agreements

Position 4 (vacant)
Commissioner

Dear Mr. Blackmer:

Position 5 (vacant)
Commissioner

Thank you for the opportunity to respond to this audit.

Tom Potter
Mayor

Beginning in 2004, PDC undertook a major effort to update our policies, procedures and business processes related to our real estate acquisition, disposition and redevelopment activities. We have continually reviewed and updated these internal controls and processes to keep current with best practices and business needs.

Bruce A. Warner
Executive Director

In June 2007, I began discussing with the PDC Audit Committee the merits of having the City Auditor's Office conduct a compliance review of our financial assistance agreements to provide additional perspective on how well these controls were working and what improvements could be made. The Audit Committee endorsed this idea and we were pleased that in September 2007 the Auditor's Office agreed to conduct this compliance review to "determine whether recipients have complied with the terms of their contracts with PDC, and have delivered the performance specified in their contracts."



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Subsequently, the universe of financial assistance agreements was narrowed to focus only on disposition and development agreements (DDAs) approved between 2003 and 2005. These types of agreements represent a key tool that PDC uses to control and manage the redevelopment of PDC-owned property to construct projects that support achievement of the City's and PDC's housing, economic development and redevelopment goals within our urban renewal areas. We looked forward to the results of this audit helping us assess how effective DDAs are in our overall property disposition business process.

With regard to Audit Objective #1, to "determine whether PDC is receiving the contractual requirements from developers as stated in the (development) Agreements," your conclusion that "developers comply with Disposition and Development Agreements" (DDA) reinforces our own assessment that PDC has implemented, and continues to implement successfully our executed DDAs with private developers.

With regard to Audit Objective #2, to "evaluate the adequacy of PDC's internal monitoring and compliance assessment processes for these (development) Agreements" we find the conclusion that "PDC is not adequately monitoring (development) Agreement compliance" perplexing in light of your above finding that developers comply with DDA requirements. Based on information presented in the audit report and conversations with your staff, it is obvious this conclusion was



based on a misplaced focus on non-contractual requirements outlined in staff reports and Board documents. It is true that PDC does not normally monitor these non-contractual requirements to the same extent that we monitor DDA contractual requirements. This is a business decision PDC has made that reflects devoting limited resources to monitoring those elements of a DDA with the highest risk.

While we recognize your interest in commenting on the overall public benefits to be derived from PDC-supported redevelopment projects, the assessment of our efforts to monitor non-contractual requirements was not an objective of this audit and it appears you have substituted your judgment on what "should" be monitored instead of what is "required" to be monitored. This substitution distorts the assessment of how well we monitor actual contractual requirements of development agreements. In addition, the report leaves me with little idea of what specific DDA contractual requirement monitoring efforts are working well, or not so well – or the extent of any deficiencies.

The report points out that of the nine DDAs in your sample requiring a certificate of completion (Certificate), you found only three completed Certificates but you acknowledged that the remaining six were completed shortly after your initial research. You appear to rely on that evidence to draw the conclusion that "PDC does not adequately monitor Agreements during construction." As we explained to your staff, there is not always a direct correlation between the timing of issuing a Certificate and the end of construction, nor should the absence of a Certificate lead to a presumption that all underlying construction monitoring activities, such as an architect's completion notice or the city's certificate of occupancy have not been completed.

It is also inaccurate to presume that the absence of a Certificate is evidence that all contractual requirements of a development agreement have not been completed. Moreover, the lack of a Certificate in itself does not expose PDC to additional risks or financial liabilities. Typically the developer or developer's bank drives the timing of PDC issuing this Certificate in order to formally acknowledge the satisfaction of the developer's construction obligations under the DDA. Until a Certificate is issued, the DDA requirements simply stay in place on the property title extending PDC's ability to enforce provisions of the DDA.

And as we demonstrated to your staff, since the 2003-2005 time period of the DDAs reviewed in this audit, PDC has established a new DDA tracking system that specifically notes and facilitates real-time monitoring of all DDA contractual requirements, including a certificate of completion when applicable. Your report makes no mention of this highly relevant fact.

Your report draws the conclusion that "PDC does not adequately monitor Agreements after construction" and infer that what you think isn't being done, such as "monitoring the achievement of City goals," should be the responsibility of PDC – apparently in perpetuity. We share your office's passion for performance measurements and have recently expanded our own internal efforts to establish, monitor and report on such metrics. However, we believe this conclusion overlooks the reality that after-construction monitoring of city development goals, building uses and conditions, and neighborhood nuisance issues is generally the responsibility of other city bureaus through established processes, and not PDC.

Mr. Gary Blackmer
Page 3
September 5, 2008

I am concerned that if PDC converted all of the City's and PDC's aspirational goals for a project into hard contractual DDA obligations with long-term scrutiny of a project's operations, private interest in investing in our projects would assuredly decline. Furthermore, private developers willing to endure such extended obligations would likely request greater public financial subsidies to offset the additional contractual risk and expense they would be assuming.

Given that the scope of the Audit was on compliance with DDA contractual requirements, we find distracting and misplaced the Report's discussion of projects where "some commercial development goals were not fully met." The Report's recommendation to "have more realistic timelines" regarding tenant occupancy in project schedules is a fair point, but given the uncertainty of economic conditions which will exist when a project is finally completed (up to 2-3 years after a DDA is entered into), such specificity about tenant occupancy is rarely a contractual requirement of a DDA. And as you point out, PDC-supported projects are typically in depressed areas where the community is looking to PDC to create or expand the market which makes leasing forecasts even more difficult.

The reality of virtually any commercial development is that it takes time for the space to be leased and that periodically there will be vacancies (the Portland-Metro retail vacancy rate is currently 5-6%). The incentive – and the financial risk – to fill commercial space rests with the private developer, and not PDC. Since DDAs are often entered into several years before a project is actually completed, defining "realistic expectations" is a simplistic recommendation to address a complex issue unrelated to our use of DDAs.

Finally, your comments about prior audit recommendations fail to point out that of the recommendations made in the September 2005 and June 2006 audits, PDC has completed implementation of steps to address 13 of the 17 recommendations. Work is underway on three that require more extensive and long-term system modifications, and the PDC Audit Committee is still considering whether or not to act on the remaining outstanding recommendation.

Again, thank you for allowing me to provide this response to your report. I will take your report and recommendations under advisement, and forward to the PDC Audit Committee for further review and consideration.

Sincerely,



Bruce A. Warner
Executive Director

cc: PDC Audit Committee

tag

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Portland Development Commission: Developers comply with Disposition and Development Agreements, but PDC does not monitor adequately

Report #358, September 2008

Audit Team Members: Fiona Earle, Shea Marshman

This report is intended to promote the best possible management of public resources. This and other audit reports produced by the Audit Services Division are available for viewing on the web at: www.portlandonline.com/auditor/auditservices. Printed copies can be obtained by contacting the Audit Services Division.

Gary Blackmer, City Auditor
Drummond Kahn, Director of Audit Services

Other recent audit reports:

Street Paving: Office of Transportation improved quality assurance, but is resurfacing fewer streets (#359, August 2008)

Downtown SmartMeters: Most goals met, but cost-benefits and reliability need further review (#352B, July 2008)

Housing Tax Abatements: Oversight inadequate to ensure program goals (#362, July 2008)

Office of Neighborhood Involvement: Clearer goals and more comprehensive measures needed to improve accountability (#363, June 2008)

