



Calgary

City Auditor's Office

Real Estate & Development Services - Enhanced Rationalization Program Audit

December 5, 2022

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The City Auditor's Office conducted this audit in conformance with the *International Standards for the Professional Practice of Internal Auditing*.

Executive Summary

As part of The City's strategic approach to managing City land, the Enhanced Rationalization (ER) program was approved with a budget of \$3.9M¹ through One Calgary 2019-2022. The ER program was launched with the goal to accelerate the land rationalization process and identify additional surplus lands, which would be available for sale to generate revenues to finance future land acquisitions, support other corporate initiatives and increase the tax base.²

The objective of this audit was to assess the design and operational effectiveness of the ER program in achieving its mandate and objectives supporting the management of City-owned land. The assessment was completed by reviewing the design and operation of program processes that support the mitigation of key risks.

Overall, we determined that the ER program is generally effective in supporting the management of City-owned land.

The ER program mandate is to "increase revenue for the Revolving Fund by improving the land sales velocity". Its objectives are to:

1. Optimize the value of City's land inventory;
2. Increase the Social, Environmental and Economic return on investment of City land; and
3. Increase sales of general land.

We identified effective processes that support the mitigation of key risks, and the achievement of the ER mandate. ER's engagements with land stewarding business units classify the City's land inventory. Surplus properties are identified, and disposition strategies are prepared to provide options to increase the benefits and value to the City. ER monitors and provides regular updates to the Real Estate & Development Services (RE&DS) Management Team and Corporate Land Committee (CLC) on the implementation of the approved disposition strategies. ER has an established definition, plan, and annual targets, and monitors and reports on its objective to increase general land sales. ER estimates that the general land sales target will likely be achieved by the year 2025 or 2026 and expects it to exceed the target of \$40M.

However, a clear definition, targets and plan have not been established for the program mandate and the two objectives to optimize land inventory value and increase the social and environmental return on investment. The program's objectives are not measurable, attainable, or relevant to the purpose of the ER program. Neither the mandate nor any of the program objectives have an established risk assessment including risk tolerances and risk appetite.

To enhance the program, we raised a recommendation to refine the ER mandate and objectives and support them with a risk management strategy. To support future program success, we also recommended monitoring the resources assigned to ER, as the program does not have the dedicated resources initially planned.

¹ One Calgary 2019-2022, page 606

² Deputy City Manager's Office Report to SPC on Utilities and Corporate Services December 18, 2019 (UCS2019-1579 Attachment 1)

ER has agreed to the recommendations and has committed to set action plan implementation dates no later than December 31, 2023. The City Auditor's Office will follow up on all commitments as part of our ongoing recommendation follow-up process.

1.0 Background

Over time, The City of Calgary (The City) has acquired an inventory of over 8,300 parcels of land (34,442 acres²). These parcels support delivery of City services to business and citizens in the form of parks and natural spaces, community-focused services, affordable housing, administrative buildings, public works, and utility infrastructure. These lands are assets for The City, to be managed well in fulfilling its operational needs and leveraged to the benefit of all Calgarians.³

By definition, rationalization in business includes the reorganization and standardization of processes in order to increase operational efficiency.⁴ The City manages land required to deliver its services through the Executive Leadership Team approved standards set out in the 2015 Corporate Land Management Framework (CLMF). Included in the CLMF is the established Land Rationalization Standard requiring land stewards to regularly review the lands they manage and identify if land is required to support operations. If not, opportunity is provided to find other corporate uses for land and to sell surplus parcels, with sales revenues returned to the Revolving Fund for General Land Purchases (Revolving Fund) to support the acquisition of new land needed for City operations.² The Revolving Fund is an ongoing reserve fund used to acquire land required for City use in a timely manner for projects beyond the four-year budget cycle.¹

The Corporate Land Committee (CLC) is responsible for directional oversight of policy, standards on processes, and guidance for land management as well as the overall direction for the Corporate Land Strategy⁵. In 2018, the CLC determined that the sustainability of the Revolving Fund was at risk and that additional revenue was required to maintain and expand the impact and benefit of the Revolving Fund to The City.⁶

In 2019, as part of The City's strategic approach to managing City land, the Enhanced Rationalization (ER) program was approved with a budget of \$3.9M¹ through One Calgary 2019-2022. The ER program was launched with the goal to accelerate the land rationalization process and identify additional surplus lands, which would be available for sale to generate revenues to finance future land acquisitions, support other corporate initiatives and increase the tax base.²

The ER program is the third phase of the three-phase sustainability strategy implemented by the CLC to enhance the sustainability of the Revolving Fund. The ER program's mandate is to "Increase revenue for the Revolving Fund by improving the land sale velocity" and its objectives are to: 1) optimize the value of City's land inventory; 2) increase the Social, Environmental and Economic return on investment of City land; and 3) increase sales of general land.⁶

³ Deputy City Manager's Office Report to SPC on Utilities and Corporate Services October 10, 2018 (UCS2018-1141)

⁴ <https://www.investopedia.com/terms/r/rationalization.asp>

⁵ Deputy City Manager's Office Report to SPC on Utilities and Corporate Services December 16, 2020 (UCS2020-1307)

⁶ Enhanced Rationalization Program Charter

2.0 Audit Objective, Scope and Approach

2.1 Audit Objective

The objective of this audit was to assess the effectiveness of the ER program in supporting the management of City-owned land. The assessment was completed by reviewing the design and operation of program processes that support the mitigation of key risks.

2.2 Audit Scope

This audit assessed the design and operation of the plans and processes that supported the ER program in the various project steps completed to date.

The audit did not provide assurance on the assessment of land value process or its results.

2.3 Audit Approach

During the planning phase of the audit, we conducted a risk assessment of the ER program and identified the following key risks that could impact the ability of the program to achieve stated objectives:

- The ER program mandate and objectives are not well defined, targets are not established, monitored and reported, and risks are not identified and assessed.
- Engagement with land stewarding business units is not effective in accurately and completely identifying and classifying land inventory.
- Disposition strategies for surplus land are not prepared and implemented to realize optimal land value.
- Land market conditions are not monitored, limiting the ability to react and effectively manage land.

Our audit approach included interviews with key personnel, review of reports and supporting documentation, and testing a sample of projects and surplus land to assess the design and operation of the program processes that support the mitigation of key risks identified. We:

- Obtained the ER risk register and assessment to determine the identification, assessment, and mitigation of risks to the achievement of its sales objectives.
- Obtained a sample of two ER projects and two annual reports to determine if:
 - Land value optimization was defined, and targets established and monitored;
 - The engagement with land stewarding business units was effective in completing the identification and classification of land inventory;
 - Sales velocity indicators were established and tracked; and
 - Social and environmental return on investment was defined and targets established and monitored.
- Obtained a sample of ten surplus parcels and two implementation plans to determine the effective implementation of land disposition risk mitigation strategies.
- Obtained a sample of two disposition strategies to determine if land market conditions were monitored and the results used for land management.

3.0 Results

Overall, we determined that the ER program is generally effective in supporting the management of City-owned land.

We assessed the design and operation of ER program processes that support the mitigation of the following key risks:

- The Enhanced Rationalization program mandate and objectives are not well defined, targets are not established, monitored and reported, and risks are not identified and assessed.
- Engagement with land stewarding business units is not effective in accurately and completely identifying and classifying land inventory.
- Disposition strategies for surplus land are not prepared and implemented to realize optimal land value.
- Land market conditions are not monitored, limiting the ability to react and effectively manage land.

We identified effective processes that support the mitigation of key risks related to engagement with land stewarding business units, disposition strategies and monitoring of land market conditions. We also identified effective processes that supported the achievement of the ER mandate. We recommended that refining the ER program mandate and objectives, and monitoring the resources assigned to the ER program would further support ER program achievement. Detailed results are set out below under the headings of the four risks: Program Mandate and Objectives, Engagement with Land Stewarding Business Units, Disposition Strategies, and Monitoring Land Market Conditions.

3.1 Program Mandate and Objectives

The ER program mandate is to “increase revenue for the Revolving Fund by improving the land sales velocity”. Its objectives are to:

1. Optimize the value of City’s land inventory;
2. Increase the Social, Environmental and Economic return on investment of City land; and
3. Increase sales of general land.

3.1.1 Program Mandate – Land Sales Velocity

We identified (Section 4.1) that a clear definition, plan, targets, and a risk assessment including risk tolerances and risk appetite have not been established for the ER program mandate to improve land sales velocity. We recommended that the Coordinator of ER refine the Enhanced Rationalization program mandate and objectives to be specific, measurable, attainable, relevant, and time-bound, and once approved by the Corporate Land Committee, prepare a risk management strategy to support program success (Recommendation #1).

We also identified (Section 4.2) that the ER program does not have the dedicated resources initially planned to support the program, and evaluation has not yet been completed to analyze whether the alternative resourcing will be sufficient to support the program in achieving its mandate. We recommended that the Coordinator of ER monitor and evaluate the resourcing assigned and determine if adjustments are required to fulfill the program mandate (Recommendation #2).

At the time of the ER program audit, ER started an evaluation with only a small dataset available (only two land sales completed) and determined that the sale of surplus land (from the point of initial circulation to disposition) through the ER program took 117 weeks, as compared to other land sales that took 207 weeks, a 43% increase in velocity for ER land sales. This early and very small analysis indicates that ER program efforts are having a positive impact on its mandate to improve land sales velocity even with its limited control over sales. These metrics indicate a positive trend. However, without an established target, it is difficult to measure ER's success in achieving its mandate.

Currently, the ER program does not report on the status of land sales velocity. With new data becoming available, the ER program plans to start reporting on sales velocity indicators in the mid-year and annual reports to CLC.

3.1.2 Program Objective - Land Inventory Value Optimization

We identified (Section 4.1) that the ER program has not established a definition of its objective to optimize the value of the City's land inventory. It does not have established targets or identified risks, risk appetite and risk tolerances for optimizing the value of land inventory, and as such does not monitor land optimization performance.

As explained by ER, disposing of surplus City-owned land has the following benefits:

- Reduction in maintenance expenses for the City;
- Broadening of the municipal tax base by creating a new taxable property;
- Generation of general land sales revenue for the Revolving Fund for General Land Purchases; and
- Activation of otherwise unused, likely poorly maintained orphaned parcels of land.

Once ER identifies surplus City-owned land with a land-stewarding business unit, the land is circulated to other land-stewarding business units to determine if there is another municipal use. If there is a better use with another business unit, then the land is transferred. If there is no other municipal use for the land, it is identified as City surplus and ER prepares a disposition strategy.

Each disposition strategy contains a feasibility study to determine the financial benefits of various alternatives for each parcel of land and ER makes a recommendation. The RE&DS Management Team reviews the ER disposition strategies and the recommendations and approves the alternative with the best generation of present value cash flow. ER reports how many parcels were identified as surplus and the benefits of their disposition.

We observed that ER determines that the optimal decision is made based on the expertise of those making the decision (the ER team and RE&DS Management Team). The ER program identifies surplus land and provides options to consider for alternate land use, and it can be demonstrated that land inventory value has increased. However, it is not clear if and how the optimal decision was made, as optimal has not been defined.

The success of the ER program in achieving this objective can be better assessed with a clear definition of the objective, established targets and identified risks, risk tolerances and risk appetite (Recommendation #1).

3.1.3 Program Objective - Social and Environmental Return on Investment

As described in Section 4.1, the ER program objective to increase the social, environmental, and economic return on investment of City land has not been clearly defined. Targets, risks, risk tolerances and risk appetite have also not been established.

Examples of social and environmental returns on investment of City land include selling property through the non-market affordable housing land strategy or creating green space for Calgarians. Value-added work may also provide a social or environmental return on investment, for example, providing a safe pedestrian connection as a condition with the sale of surplus land. The ER program generates revenue for the Revolving Fund, which enhances its sustainability and enables the City to take advantage of unfunded, time-sensitive opportunities that contribute to Council's social and environmental objectives.

After review of the ER Program Charter, project charters, project inventory analysis and summary reports, and disposition strategies, we determined that there is not an established plan to achieve this objective. We recommended (Recommendation #1) that the ER program mandate and objectives be defined to support program success.

3.1.4 Program Objective - General Land Sales

We identified that the ER program has established a definition, a plan, annual targets and monitors and reports on the increase in general land sales. The ER program revised targets for increasing general land sales for the four-year period are: \$0M in 2020, \$5M in 2021, \$15M in 2022, and \$20M in 2023. These targets were initially set for the period 2019-2022, but the ER program implementation was delayed due to the Covid-19 pandemic, a City hiring freeze and a change to a teleworking structure all occurring at the same time.

The ER program is not on track to achieve its general land sales annual targets, resulting in delayed sustainability of the Revolving Fund. There were no general land sales realized in 2020 or 2021 and ER estimates \$3M-\$5M will be realized in 2022. It took longer than expected to identify surplus land, however, the ER program continues to create sales opportunities that generate revenues and benefits to The City. The ER program estimates that the general land sales target will more likely be achieved by the year 2025 or 2026 and expects to exceed the target of \$40M. The CLC and RE&DS Management Team are aware of, and supportive of, the ER program's general land sales forecast.

ER has identified and communicated the risks to achieving the general land sales targets through various mediums, such as the ER Program Charter, project charters, inventory analysis strategies, disposition strategies, implementation plans, the recently approved draft Corporate Land Strategy Portfolio Risk Management Plan, weekly ER meetings, and meetings with RE&DS Management Team, Corporate Land Administration Team, and CLC. However, there is not a single risk register that captures and tracks all of the key risks (Recommendation #1).

3.2 Engagement with Land Stewarding Business Units.

ER's process for identifying and disposing of surplus land is completed at a project level and is as shown in Illustration 1 below with blue headings. The projects coincide with the City's land stewarding business units, for example, Roads, Transportation Infrastructure, Water Resources, etc.

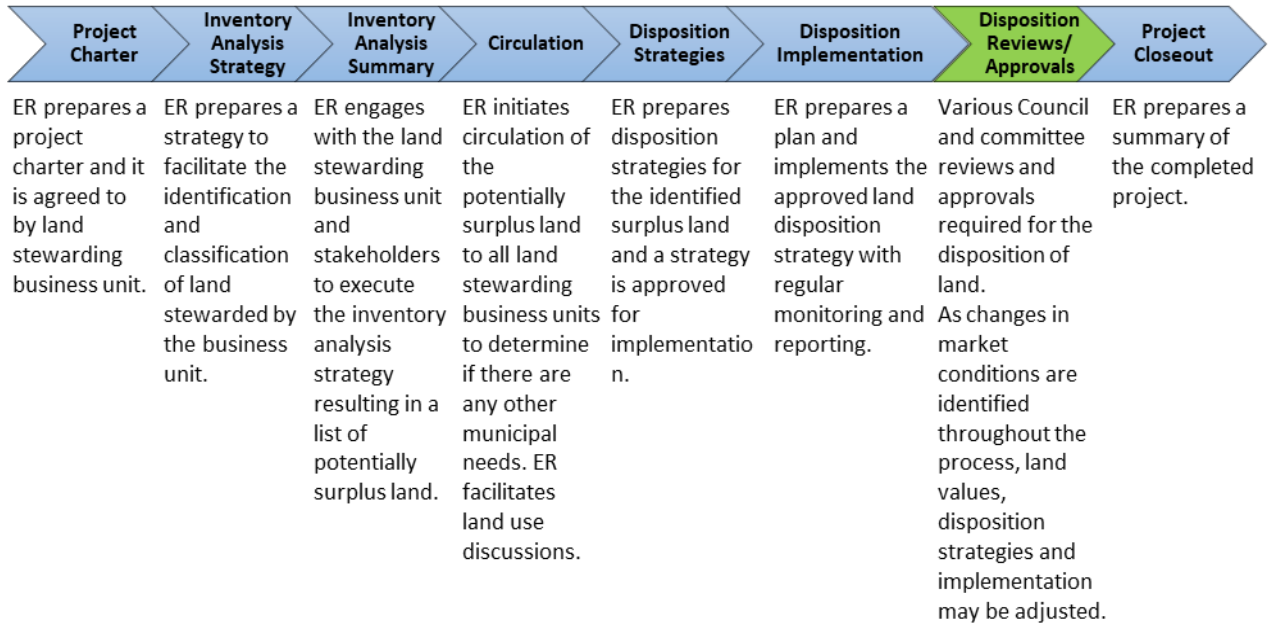


Illustration 1: The Enhanced Rationalization’s land management process created by City Auditor’s Office based on information provided by the ER program.

The ER program is dependent on the subject land stewarding business units' engagement in project charter approval, establishing criteria for surplus inventory identification, identification of relevant stakeholders, and confirmation and approval of parcels surplus to business unit needs. Once the surplus inventory has been approved by the subject land stewarding business unit, it is circulated to identify interest by other land stewarding business units.

We concluded that ER program processes are effective in mitigating the risk that engagement with land stewarding business units is not effective in accurately and completely identifying and classifying land inventory.

ER engages the Corporate Project Management Centre (CPMC) to facilitate the engagement sessions with subject land stewarding business units to establish land inventory criteria. CPMC utilizes engagement software to guide business unit participants through the Criteria Establishment Meeting. ER uses the results of the Criteria Establishment Engagement session to inform the Inventory Analysis Strategy, which groups similar criteria into categories that reflect “Why the subject business unit requires City owned land.”

We examined three projects and determined that ER effectively engages with the land stewarding business units to obtain the required information within the required timelines. Knowledgeable business unit participants were selected, they were informed of the ER program, the project charter, and the inventory analysis strategy, and the criteria were based on participant feedback with a final confirmation by the business unit participants and the Executive Sponsor.

The ER program monitors its project progress through weekly staff meetings and reports at CLC and RE&DS Management meetings. ER also has processes and escalation mechanisms in place to ensure business units prioritize the completion of tasks. We determined that all three projects examined were on schedule as compared to their respective project charter.

3.3 Disposition Strategies

Disposition strategies and implementation plans contribute to the effectiveness of the land value enhancement process. Surplus properties are identified, and disposition strategies are prepared to provide options to increase the benefits and value to the City. Progress in the implementation of the disposition strategies is monitored and reported to CLC.

We concluded that the design and operation of ER program processes are effective in mitigating the risk that disposition strategies for surplus land are not prepared and implemented to realize optimal land value.

We confirmed that the sample of 12 surplus parcels identified through the Roads project all had a corresponding disposition strategy. The disposition strategies provided alternatives to increase the benefits and value to the City. An analysis summary was provided for financial impacts (tax, lease revenue, fees & internal charges), business impact, and geodemographics for surplus properties. The disposition strategies also noted their ER program alignment and the benefits.

3.4 Monitoring Land Market Conditions

The ER program establishes market value estimates for potential land sales revenue anticipated for the alternatives considered in each disposition strategy. Once a disposition strategy has been reviewed and approved, there are multiple stages in the land disposition process where changes to market conditions are identified and land values are adjusted, right up until the sale of the land is complete.

We concluded that the design and operation of ER program processes are effective in mitigating the risk that land market conditions are not monitored, limiting the ability to react and effectively manage land.

We observed this process for the sale of land recommended in two disposition strategies. The process included the review and approval of the RE&DS Management Team, a land valuation report prepared by a Sales Agent, review and approval by the Valuation Review Committee, review and approval by Council (or delegated authority as per Bylaw 52M2009), a public listing of the property (and the reserved price approved by the Valuation Review Committee), review and approval of offer to purchase by Council (or delegated authority) and an agreement of purchase drafted by the Law Department to finalize the land sale transaction. At each of these stages in the land disposition process, market conditions are reviewed and an amendment to the land value and the disposition strategy may be made.

We would like to thank the staff from RE&DS for their assistance and support throughout this audit.

4.0 Observations and Recommendations

4.1 Program Mandate and Objectives

The ER program mandate and its objectives have not been fully articulated to support program success. Specific, measurable, attainable, relevant, and time-bound mandate and objectives support program success as defined targets, and associated risk mitigation can be developed and implemented to assist the program in achieving its mandate.

The ER mandate is to increase revenue for the Revolving Fund by improving the land sales velocity.

The ER objectives are to:

1. Optimize the value of City's land inventory;
2. Increase the Social, Environmental and Economic return on investment of City land; and
3. Increase sales of general land.

Mandate/Objective	Audit Analysis
Improve Land Sales Velocity	<p>A clear definition, plan, targets, and a risk assessment including risk tolerances and risk appetite have not been established for the ER program mandate to improve land sales velocity.</p> <p>Land sales timeline estimates stipulated in ER project disposition strategies and implementation plans are provided by RE&DS Sales, not the ER program. At the time of the audit, ER initiated an evaluation of the velocity of land sold through the ER program in comparison to the velocity of other land sold by RE&DS Sales. Tracking ER land sales velocity only provides a record of ER's influence on RE&DS Sales, as it is not ER that manages the Sales Agents. Tracking land sales velocity is meaningless if a target is not established. However, establishing a target for improving land sales velocity may prove to be challenging considering ER's limited control over land sales and their inability to action any land sales deficiencies.</p>
Optimize the Value of City's Land Inventory	<p>A clear definition, plan, targets, and a risk assessment including risk tolerances and risk appetite have not been established for the ER program objective to optimize the value of City land inventory.</p> <p>The ER program monitors and reports on its objective to optimize the value of the City's land inventory as the volume of land identified as surplus and available for disposition or alternate municipal use. It is not clear if and how the optimal decision is made, as optimal has not been defined. Defining the optimal value for land may be difficult to articulate and beyond the purpose of the ER program.</p>
Increase the Social, Environmental and	<p>A clear definition, plan, targets, and a risk assessment including risk tolerances and risk appetite have not been established for the ER</p>

<p>Economic Return on Investment of City Land</p>	<p>program objective to increase the social and environmental return on investment.</p> <p>The ER program reports on the social and environmental return on investment as the incidental resulting benefits of project implementation (e.g., affordable housing opportunity from a non-market land sale or alternate municipal land use that created additional Park amenities). The resulting benefits are not planned nor intentional.</p>
<p>Increase Sales of General Land</p>	<p>The ER program has established a definition, a plan, annual targets and monitors and reports on the increase in general land sales. However, a risk assessment has not been established to support ER in managing the risks to achieving its objective. A risk register noting key risks is not established, a mitigation approach is not clearly described, the accountable party is not noted, there are no plans to update/revisit risks, and risk tolerances and the associated risk appetite have not been established.</p>

Recommendation 1

The Coordinator of Enhanced Rationalization refine the Enhanced Rationalization program mandate and objectives to be specific, measurable, attainable, relevant, and time-bound and once approved by the Corporate Land Committee, prepare a risk management strategy to support program success.

Management Response

Agreed.

Action Plan	Responsibility
<p>The Coordinator of Enhanced Rationalization will:</p> <p>a) Engage with Enterprise Risk Management on the Integrated Risk Management Audit from 2021 to align with Executive Leadership Team’s (ELT) desired level of risk management maturity and consolidate all identified risks and mitigation strategies contained within existing Enhanced Rationalization Program documents into a single risk register for the Enhanced Rationalization Program.</p> <p>b) Review the mandate and objectives of the Enhanced Rationalization Program and recommend changes that address the recommendation of The City Auditor’s Office for</p>	<p><u>Lead:</u> Coordinator of Enhancement Rationalization</p> <p><u>Support:</u></p> <ul style="list-style-type: none"> • Manager Land & Asset Management • Enterprise Risk Management <p><u>Commitment Date:</u></p> <p>a) March 31, 2023 b) June 30, 2023 c) December 31, 2023</p>

Action Plan	Responsibility
<p>review and approval by Corporate Land Committee (CLC).</p> <p>c) Complete a CLC approved risk management strategy for the Enhanced Rationalization Program that identifies any new or emerging risks to the amended or confirmed program mandate and objectives and aligns with the Integrated Risk Management Policy (CC-011), ELT’s desired level of maturity, and The City’s desired level of risk tolerance & appetite.</p>	

4.2 Resource Management

The ER program does not have the dedicated resources initially planned to support the program. Evaluation has not yet been completed to analyze whether the alternative resourcing will be sufficient to support the program in achieving its mandate to “increase revenue for the Revolving Fund by improving the land sales velocity”.

In response to the CLC request for a dedicated tactical team to evaluate the City’s land stewarding portfolio, the ER program was designed as a “tiger team” project based organizational structure. The ER Program Charter describes the resourcing approach as a “tiger team” of seven full-time employees dedicated to ER. Two of these full-time employees were planned to be Sales Agents responsible to dispose of surplus land identified by the ER program, thus fulfilling the ER program mandate.

In 2019, this approach was approved by the RE&DS Management Team and the General Manager of the Deputy City Manager’s Office and by the CLC in subsequent business cases and ER program plans. Council approved the \$3.9M budget request for the ER program as part of One Calgary 2019-2022.

In April 2021, after the other ER employees had already been recruited and it came time for ER to recruit the two Sales Agents, a decision was made by the RE&DS Director to instead have the Sales Agents report directly to RE&DS Sales with a dashed line of reporting to the ER program. As a result, ER has limited control over when land sales files are assigned to Sales Agents, their priority, or the pace of sales once land is identified as surplus and ready for disposition.

The Coordinator of ER has not yet formally evaluated the impact of the resourcing change on the program to determine whether the adjustment in resourcing approach impacts the ability of the ER program to achieve its mandate.

Recommendation 2

The Coordinator of Enhanced Rationalization monitor and evaluate the resourcing assigned to the Enhanced Rationalization program and recommend additional actions to the RE&DS Management Team if adjustments are required to fulfill the program’s mandate.

Management Response

Agreed.

Action Plan	Responsibility
<p>The Coordinator of Enhanced Rationalization will:</p> <ul style="list-style-type: none"> • Implement approved resourcing plans; • Monitor and evaluate resourcing needs of the Enhanced Rationalization Program as it matures and evolves to ensure it has sufficient resources to accomplish the amended or confirmed program mandate and objectives; and • Complete and present a report to RE&DS Management Team on Enhanced Rationalization resources, including recommendations for additional actions required to address any new or emerging resourcing risks to the program mandate and objectives. 	<p><u>Lead:</u> Coordinator of Enhancement Rationalization</p> <p><u>Support:</u></p> <ul style="list-style-type: none"> • Manager Land & Asset Management • Real Estate & Development Services Management Team <p><u>Commitment Date:</u> December 31, 2023</p>