

Board of County Commissioners  
Airport Department

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AIRPORT PROPERTY LEASING OPERATIONS  
August 18, 2004

**HERNANDO COUNTY CLERK OF CIRCUIT COURT**  
**Audit Services Department**  
**MEMORANDUM**

**TO:** Donald "Don" Silvernell, Airport Director

**VIA:** Karen Nicolai, CPA, Clerk of Circuit Court

**FROM:** Peggy Prentice, CIA, CISA, Audit Services Manager

**DATE:** August 18, 2004

**SUBJECT:** Airport Property Leasing Operations

The Audit Services Department's (ASD) Audit Projects Schedule included an audit of the Airport's property leasing operations. This audit is complete.

Although we exercised due professional care in the performance of this audit, this should not be construed to mean that unreported noncompliance or irregularities do not exist. The deterrence of fraud and/or employee abuse is the responsibility of management. Audit procedures alone, even when carried out with due professional care, do not guarantee that fraud or abuse will be detected. Specific areas for improvement are addressed later in this report.

The purpose of the audit is to furnish management independent, objective analyses, recommendations, counsel, and information concerning the activities reviewed. The audit report is a tool to help management discern and implement specific improvements. The audit report is not an appraisal or rating of management.

A copy of the report has been forwarded to the Board of County Commissioners as an agenda "correspondence to note" item.

If you have any questions, concerns, or need additional information in regard to the above or the attached report, please do not hesitate to contact me at (352)540-6235 or just stop by my office in Room 201.

**ATTACHMENT**

**copy: CLERK OF CIRCUIT COURT:**

Amy Gillis, CPA, Finance Director

**BOARD OF COUNTY COMMISSION:**

Commissioner Mary Aiken

Commissioner Thomas Mylander

Commissioner Hannah "Nancy" M. Robinson

Commissioner Diane Rowden

Commissioner Robert C. Schenck

Gary Adams, County Administrator

Kurt Hitzemann, Senior Assistant County Attorney

Larry Jennings, Growth and Development Director

George Zoettlein, Office of Management and Budget Director

**OTHER:**

Chip Jones, Partner, KPMG

Hernando Today

St. Petersburg Times - Hernando Edition

WWJB Radio Station

Hernando County Public Library

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## Airport Property Leasing Operations

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**Airport Property Leasing Operations**

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**ACKNOWLEDGMENT**

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## **Airport Property Leasing Operations**

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### **ACKNOWLEDGMENT**

Other minor findings, not included in this report, have been communicated to management and/or corrected during the audit process. We thank the management and staff for their cooperation throughout the audit.

Fieldwork was performed by:

Peggy Prentice, CIA, CISA, Audit Services Manager

Airport Department management response was provided by:

Donald Silvernell, Airport Director

Airport Department management response was reviewed and authorized by:

Larry Jennings, Growth and Development Director

Gary Adams, County Administrator

This audit report was reviewed and authorized by Karen Nicolai, CPA, Clerk of Circuit Court, on August 18, 2004.

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## **Airport Property Leasing Operations**

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### **PURPOSE AND SCOPE**

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## **Airport Property Leasing Operations**

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### **PURPOSE AND SCOPE**

**PURPOSE:**

The purpose of this audit project is to address the Airport's property leasing program's lease agreement monitoring controls; the adequacy of files, written policies and procedures or instruction manual(s), reporting, and record-keeping; and to analyze the wording, format, and terms and conditions of property leases.

**SCOPE:**

The audit period reviewed was from 2002 to May 30, 2004. The Audit Services Department performed the following:

- < Conducted interviews;
- < Reviewed written policies and procedures and/or instruction manual(s);
- < Observed actual practices;
- < Traced rental agreement transactions to record-keeping, recording, and reporting records;
- < Assessed the internal control structure;
- < Reviewed documentation relevant to fee and rent structure;
- < Assessed the basis for rent, rent escalations, and maintenance fees;
- < Assessed insurance documentation;
- < Assessed lease requirements; and
- < Addressed adherence to lease terms and conditions.

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## **Airport Property Leasing Operations**

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**BACKGROUND**

## **BACKGROUND**

Prior to the mid- to late-1940's, the War Assets Administration (WAA) owned the land and improvements currently referred to as the Hernando County Airport (including the industrial parks). During the late 1940's, the WAA transferred the property and improvements to the City of Brooksville through a series of quit claim deeds. The deeds contained recapture clauses, reverter clauses, maintenance clauses, and restricted the property to public airport use. The Federal Aviation Administration (FAA) has since modified the public airport use restrictions and released the recapture clause. Shortly after 1948, the City of Brooksville transferred the property to Hernando County. The acreage is currently used by the County for an airport, industrial park, land rentals, and tree farming.

The Airport's runways accommodate private and commercial aircraft, but the airport does not yet serve the general public with scheduled airline service. The airport has an onsite Corporate RailPark, Industrial Park, and AirPark. In these parks, the Airport leases raw land (i.e., ground leases), some properties that have been improved, and aviation hangar facilities. The Airport also leases a few out-parcels.

Pursuant to F.S. 125.35(1), the Board of County Commissioners ("Board") offers for lease on a continual basis various parcels of real property owned by the County in the Airport Industrial Park, Corporate AirPark, and other locations on the property of the Airport for aviation, industrial, commercial and/or institutional development. Lease terms depend on the location and quantity of real property and other factors, and are subject to review and approval of the Board. Use of leased property is subject to covenants, conditions and restrictions applicable to the particular property; laws, rules, regulations and orders of any state or Federal agency with jurisdiction over the property including the FAA, State of Florida, Department of Transportation, and applicable Florida Statutes and ordinances of the Board; as well as standard or negotiated lease terms.

Parties interested in obtaining a lease must transmit the offering of standard lease term documents to the Board for approval. Lease terms are subject to the bidding process for the specified property at the terms provided in the documents. If no other parties bid for the lease, the tentative lease documents are subject to approval and execution by the Board. The Board has the right to reject any bid for lease upon determination that the bid is not in the best interest of the County as determined by the Board.

**CORPORATE AIRPARK:** The Corporate Airpark is a 250-acre industrial park located adjacent to the Suncoast Parkway. The Airpark offers building sites for lease that range from 2 to 50 acres in size. Airside lots are available that provide aircraft access to the property.

**AIRPORT INDUSTRIAL PARK:** The Airport Industrial park is a 155-acre industrial park located adjacent to Spring Hill Drive. The building sites for lease range from 2 to 4 acres in size. Airside

lots are available to provide aircraft access to the property.

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**AIRPORT RAILPARK:** The Airport RailPark is located on the southeastern edge of the Airport adjacent to the Southwest Florida Water Management’s Headquarters. The RailPark offers “rainside” lots with access to trackside loading/unloading.

**AVIATION AUTHORITY:** The Hernando County Aviation Authority (HCAA) is an advisory committee to the Board. The HCAA consists of seven (7) residents of Hernando County, selected by the Board. Each member’s term in office is generally four (4) years. The HCAA’s meetings are held in a public forum. The HCAA provides recommendations to the Board regarding tenant lease agreements, Airport projects, and standard operating procedures. The actions of the HCAA are subject to Board approval.

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**DISCUSSION POINTS,  
RECOMMENDATIONS,  
AND  
MANAGEMENT'S RESPONSE**

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### **INTERNAL CONTROL STRUCTURE**

Based upon testing, interviews, and observations, it appears that the Airport's internal control structure in regard to the property lease approval process, the cash receipts process, and the general lease administration cycle is adequate. Taking into consideration the difficulty for a small department, such as the Airport, to fully segregate incompatible duties, the Airport has taken reasonable measures to do so. Above-normal automated file security and access controls are not required due to the minimal potential for business disruption if files are destroyed at the departmental level.

### **STANDARD OPERATING PROCEDURES (SOPs)**

The Airport's SOPs related to the leasing program are sufficient. Pertinent documents are exhibited. The SOPs appear to reflect the actual work performed. The SOPs have an effective or revision date, as applicable, and include the Airport Director's authorization.

### **LEASE FILE MAINTENANCE, RECORDKEEPING, RECORDING, AND REPORTING**

Using the holistic approach, it appears that the Airport's lease file maintenance, record-keeping, reporting, and recording practices are adequate. Testing provided a reasonable level of assurance that electronic records are reliable.

Overall, rent rates and escalation criteria appear to be in compliance with the FAA Order. No material concerns were identified regarding the accuracy of the Airport's financial records related to tenant rent payments and maintenance fee payments. Using the cost benefit approach, the Department does not enforce the collection of small dollar value tenant late fees. During fieldwork, the Department implemented an SOP that authorizes certain waivers of late fees. These waivers require management's authorization.

Finance's role in recording and reporting Airport lease revenue includes obtaining and processing Airport daily collections, reconciling daily work to validated bank deposit slips, tracking three-part, pre-numbered receipts issued by the Airport to record cash collections, scanning financial support documents, and desk checking Airport grant compliance. Airport revenue is booked in its own fund. Only Airport expenditures are charged to this fund. The Airport utilizes project-accounting to record financial transactions.

No material concerns were identified with the wording, format, terms, or conditions of the currently-used lease template. It appears that this template provides the County with some level of assurance that the Airport lease program is in compliance with the FAA Order/grant criterions. A combination of adequate tenant insurance coverage and lease language provide the County with some assurance against potential liability. The Airport has taken reasonable measures to obtain approval by the appropriate in-house and external entities. The Airport's lease templates were reviewed and approved by the County Attorney's Office. This oversight provides some assurance that these templates are in compliance with FAA guidelines and protects the County from potential

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liability. During fieldwork, the lease templates were sent to the FAA for review and approval. The FAA response has not yet been received.

It appears that the Airport reasonably ensures that tenants maintain the appropriate insurance coverage based upon the terms and conditions in their lease agreement. Per Risk Management, the significant difference between *listing* versus *naming* the County as additional insured has changed in recent years. The Board now accepts being *listed* or *named* as additional insured.

It was very recently brought to management's attention (by Risk Management) that in addition to requiring a certificate of insurance, the Airport should also require an endorsement from the insurance carrier.

Risk Management also indicated that there are potential liability risks when allowing tenants to improve leased land (i.e., building construction). Risk Management suggested that the Airport consider requiring tenants that lease Airport property and build on that property to submit a waiver of subrogation. The Airport addressed this potential concern with the County Attorney's Office who has indicated that this is not a material concern based upon the strength of the lease template provisions.

Although, based upon communications with management, the Airport has begun implementation of requiring an endorsement from the insurance carrier, not enough time has passed for the Airport to edit their lease template (if necessary) and revise their standard operating procedures.

***Recommendation:*** *Consideration should be given to following through on the commitment to fully implement this new insurance requirement.*

***Management Response:*** *The Airport lease template has been revised to include the requirement of a copy of an endorsement along with the certificate of insurance. The Airport will revise the "Lease Payment and Insurance Procedures" policy to include verification of the endorsement in the section on Insurance Certificates.*

Although recently-written leases appear to minimize the County's potential for liability, leases written years ago may not. The ASD recognizes that the County may not have the authority to rewrite leases that are in effect. The County may be able to renegotiate lease terms when leases expire.

***Recommendation:*** *Consideration should be given to reviewing leases when they are renegotiated or come to term (expire). Renegotiated or expired leases should be updated with the most recent lease template. This will minimize the County's potential for liability.*

***Management Response:*** *Currently, any time a request is made to assign, exercise an option or extend a lease, the Airport attempts to negotiate a new lease utilizing the new lease template. Any*

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*extension beyond the original term of the lease will be on the new lease template.*

No material concerns were identified regarding tenant adherence to lease agreement financial terms and conditions, or with what level of County personnel approve lease agreements.

### **FAA COMPLIANCE**

The expenditures from Airport revenue-producing property must have a direct and immediate benefit to the Airport. Rates based on the fair market value (FMV) must be tied to an index. The lease rates must be equitable. Any exceptions must be justified.

### **INTERPRETATION OF FAA CRITERION**

Airport management requested an interpretation of FAA rules that relate to impact fees, fleet-pooled vehicles/equipment, use of non-aviation Airport property, and cost allocation. The ASD was asked to assist with these interpretations not because of any immediate and/or significant impact to the County, but rather, to provide some level of assurance that the Airport's activities are in compliance with the FAA criteria.

***Impact Fees*** - Although there does not appear to be a history of noncompliance with the Airport's payment of standard impact fees, an interpretation of the FAA rules was considered. Utility impact fees were not addressed. Any impact fees paid by the Airport must have a direct and immediate benefit to the Airport. Rather than using the standard impact fee table, which may not be in compliance with the FAA criteria, the County should use an independent calculation for each Airport development project. The calculation must consider the project's soft and hard impact on County's resources. This analysis must be well-documented to show that the County attempted to comply with FAA criteria.

***Fleet Pooled Vehicles/Equipment*** - Any expenditures from Airport revenue-producing property must have a direct and immediate benefit to the Airport. The Airport has exclusive use of their fleet-pooled vehicles/equipment. The Airport pays repairs and maintenance (including overhead) costs for vehicle/equipment upkeep. Based upon the ASD's interpretation of the FAA criterion, it appears that repairs and maintenance expenditures have an immediate and direct benefit to the Airport.

The Airport contributes to the fleet replacement program. These monies are held until an Airport vehicle or piece of equipment is replaced. The Airport pays a replacement rate equivalent to the other governmental units participating in the program. Per Finance, if the fleet replacement program were to be discontinued, the Airport's contribution into the program would revert back to the Airport. These monies are disclosed separately at the sub-ledger level of the financial records and are held strictly for the Airport's use. Based upon the above, it appears that the Airport's participation in the fleet replacement program is in compliance with the FAA criterion. This interpretation is based upon two key issues: first, the contributions are not expended until there is an immediate and direct benefit to the Airport and second, the contributions resemble a cash reserve rather than an expenditure.

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During fieldwork, the Airport Director committed to obtaining an FAA opinion on this matter.

***Use of Non-Aviation Airport Property*** - Hernando County Fire Rescue (HCFR) occupies non-aviation Airport property rent free. General legal principles for government surplus property dictate that Airport rental facilities cannot be rented below the market rate. The FAA requires that Airports not allow favoritism to government and/or not-for-profit entities. The Airport must be as self-sustaining as possible. The FAA requires anyone using non-aviation property to pay the fair market value or its equivalent. The rental rate must be equivalent to that charged to other tenants. In-kind services may offset some or all of the actual rent charged.

***Recommendation:*** *Consideration should be given to recovering the Airport's revenue from the HCFR to which it has been diverted for non-airport purposes. The Airport should attempt to obtain fair market value for any non-aviation use of Airport property.*

***Management Response:*** *The Airport is working with the County Attorney's Office to draft an agreement with HCFR to show that the Airport will receive fair market value for the use of Airport property. Any future use of Airport property will require an agreement approved by the County Attorney's Office, which will include payment of fair market value for the use of the property.*

***Cost Allocations*** - Payments of Airport revenue to other units of government must be for services or goods of comparable value. The Airport is charged for services rendered by other Hernando County governmental units. Based upon communications with Finance and the Office of Management & Budget, it appears that cost allocation charges are assessed based upon actual expenditures from the prior year. This method proportionately distributes expenses among the users (County government units) and is generally allocated based upon volume and/or operating expenditures. For example, Finance's costs are distributed based upon the number of transactions processed on behalf of the Airport; Human Resources costs are distributed based upon the Airport's staffing level; Technology Services' costs are distributed based upon the number of computers and network devices used by the Airport; and Purchasing & Contracts' costs are distributed based upon the dollar amount of (non-grant related) purchase orders processed on behalf of the Airport. Using reasonableness and the holistic approach to determine compliance, this method of distributing costs reasonably ensures that the Airport receives an immediate and direct benefit for the costs incurred. The cost allocation method appears to be in compliance with the FAA Order.