

STATE OF LOUISIANA
ANALYSIS OF BENSON TOWER LEASE



FINANCIAL AUDIT SERVICES
INFORMATIONAL AUDIT
ISSUED SEPTEMBER 3, 2014

**LOUISIANA LEGISLATIVE AUDITOR
1600 NORTH THIRD STREET
POST OFFICE BOX 94397
BATON ROUGE, LOUISIANA 70804-9397**

LEGISLATIVE AUDITOR
DARYL G. PURPERA, CPA, CFE

**FIRST ASSISTANT LEGISLATIVE AUDITOR
AND STATE AUDIT SERVICES**
PAUL E. PENDAS, CPA

DIRECTOR OF FINANCIAL AUDIT
THOMAS H. COLE, CPA

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LOUISIANA LEGISLATIVE AUDITOR
DARYL G. PURPERA, CPA, CFE

September 3, 2014

The Honorable John A. Alario, Jr.,
President of the Senate
The Honorable Charles E. "Chuck" Kleckley,
Speaker of the House of Representatives

Dear Senator Alario and Representative Kleckley:

This informational audit report provides the results of our procedures relating to the state's lease agreement for office space in Benson Tower and the current impact of the lease. Our objective was to gain an understanding of the State of Louisiana's lease with Zelia, LLC, for state office space in Benson Tower and to determine if the leased space is fairly priced and fully used to ensure that the state is not incurring unnecessary lease costs. The scope of our audit was significantly less than an audit conducted in accordance with *Government Auditing Standards*. I hope this report will benefit you in your legislative decision-making process.

We would like to express our appreciation to the management and staff of the Division of Administration.

Sincerely,

A handwritten signature in blue ink that reads "Daryl G. Purpera". The signature is written in a cursive, flowing style.

Daryl G. Purpera, CPA, CFE
Legislative Auditor

GM:ETM:BQD:THC:ch

BENSON TOWER 2014

Louisiana Legislative Auditor

Daryl G. Purpera, CPA, CFE, Legislative Auditor



Analysis of Benson Tower Lease

September 2014

Audit Control # 80140118

Introduction

In 2009, the State of Louisiana and the New Orleans Saints reached an agreement that would keep the NFL franchise in New Orleans through 2025. As part of the agreement, the state agreed to furnish up to \$85 million toward the cost of improvements to the Superdome and Saints owner Tom Benson agreed to buy the vacant Dominion Tower and lease office space back to the state.

Act 432 of the 2009 Regular Session allowed the Office Facilities Corporation (OFC) to enter into a long-term lease agreement for office space in Benson Tower (formerly known as Dominion Tower) in New Orleans next to the Superdome, for the purpose of accommodating various state agencies.

On September 14, 2009, the State of Louisiana (through OFC) signed a lease for approximately 323,000 square feet of useable office space with Zelia, LLC (Zelia - managed by Mr. Benson). The first lease year began when the space was ready for occupancy on February 1, 2011, and the lease term ends on December 31, 2025. The state's office space includes floors 4 and 6 through 21 of the 26-story building.

OBJECTIVE: To gain an understanding of the State of Louisiana's lease with Zelia, LLC, for state office space in Benson Tower and to determine if the leased space is fairly priced and fully used to ensure the state is not incurring unnecessary lease costs.

Overall, we found that 24,872 square feet of state office space at Benson Tower is vacant at an annual cost of \$624,784. Lease costs, including amounts paid for vacant space, have nearly doubled since 2010 and exceed current market rates for comparable properties in the New Orleans area. Payments in excess of market rates for leases paid with federal funds may result in the federal government requiring the funds to be repaid

Appendix A contains the Division of Administration's response to this report and Appendix B provides our scope and methodology.

Comparison of Lease Costs

The lease for Benson Tower allows the state to sublease “with notice to but without the consent of lessor (Zelia, LLC) if the sub-lessee is any political subdivision or a public body of the State of Louisiana or any public commission, entity or regional authority created under the laws of the State of Louisiana.” OFC created a listing of potential tenants using then-existing leases in Orleans and Jefferson parishes. Potential tenants included state agencies and boards in the executive branch of state government.

Agencies that leased office space in the New Orleans area as of September 14, 2009, were subsequently relocated to Benson Tower. A comparison of lease costs prior to and subsequent to the agreement is presented in Exhibit 1. Exhibit 1 does not include vacant space leased by the state.

Exhibit 1: Comparison of Previous Leases with Benson Tower Leases				
	Previous Lease		Benson Tower Lease	
	Average Cost per Square Foot	Total Cost	Total Cost	
		2010	2012	2014
			\$23.78/sq.ft.	\$25.12/sq.ft.
Department of Children and Family Services	\$20.57	\$1,051,868	\$1,431,651	\$1,512,324
Department of Health and Hospitals	16.66	2,464,053	3,868,863	4,086,873
Department of Public Safety	21.01	263,781	592,740	626,141
Public Service Commission	19.27	32,508	60,829	64,257
Office of Financial Institutions	20.00	53,780	78,973	83,424
Louisiana Workforce Commission	15.28	299,091	292,922	309,428
Department of Civil Service*		-	160,016	169,032
Department of Revenue	17.58	322,277	252,211	266,423
Office of Community Development	21.32	80,867	161,680	170,791
Office of Facility Planning and Control*		-	72,458	76,541
Mental Health Advocacy Service	7.00	11,900	69,033	72,923
Total	\$17.66	\$4,580,125	\$7,041,376	\$7,438,157

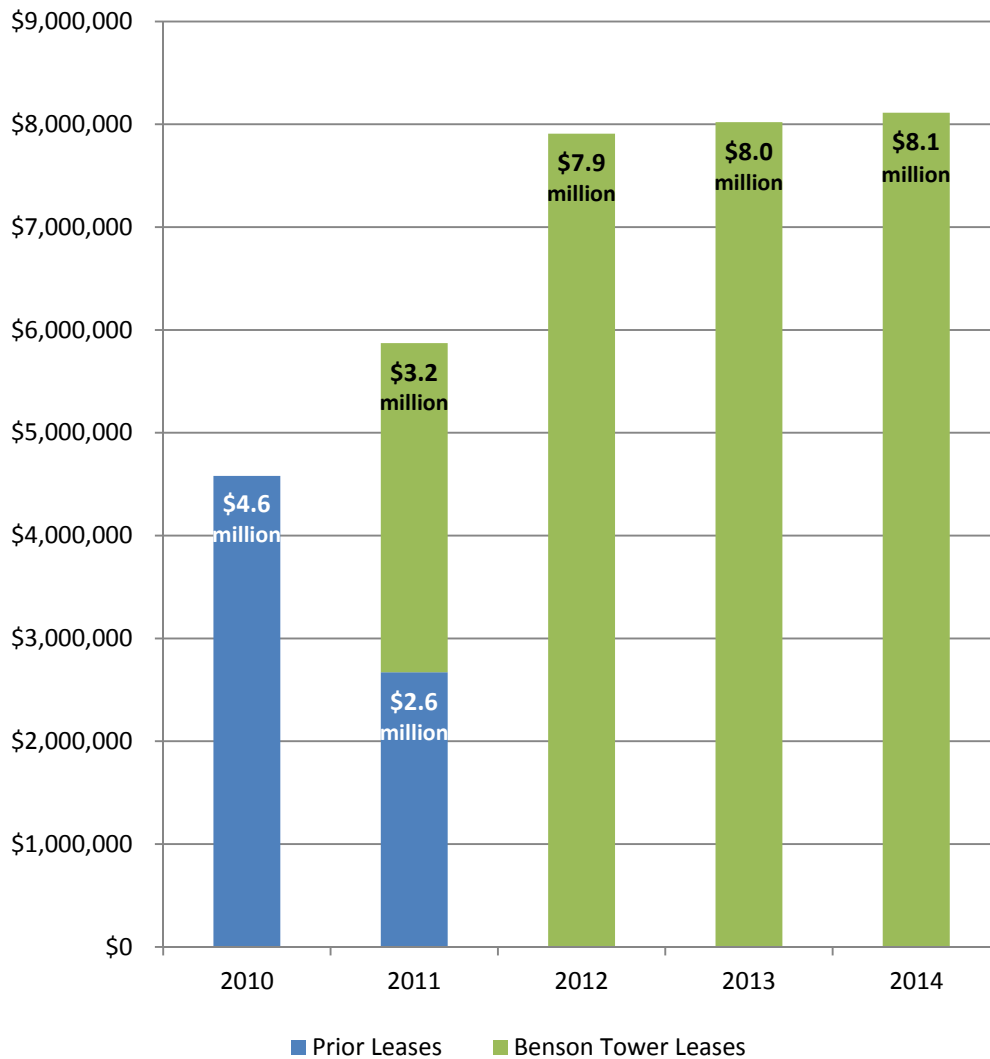
*There were no active leases for these two agencies in New Orleans prior to the Benson Tower lease.

The average cost per square foot for agencies that leased office space in New Orleans under previous leases was \$17.66. In 2012, the first full lease year in Benson Tower, the cost per square foot was \$23.78. The Benson Tower lease provides for an annual CPI adjustment. As a result, the 2014 cost per square foot has increased to \$25.12. Lease costs, including amounts paid for vacant space, have nearly doubled since 2010.

Based on our review of the previous state leases and current 2014 available listing information in those buildings, the lease rates range, including quoted costs for parking, from \$16 to \$22 per

square foot, an average of \$19 per square foot, as compared to the Benson Tower rate to the state of \$25.12. The current available listing information for other space in Benson Tower shows space available for \$18.50 to \$19 per square foot, with an additional cost for parking. Exhibit 2 presents lease costs by fiscal year for all leased space, including vacant space.

Exhibit 2: Lease Costs, by Fiscal Year



Source: Agency lease documentation and supporting calculations

Vacant Lease Space

OFC currently has subleases to state agencies for 298,105 of the 322,977 square feet of available space in Benson Tower at an annual rent amount of approximately \$7.5 million. The remaining 24,872 square feet are vacant (including the entire 9th floor) at an annual cost of \$624,784 to the state.

Two offices of the Department of Justice (DOJ) were targeted for relocation to Benson Tower with the original group of tenants and were a part of the planning process in designing the ninth floor to meet their office needs. On multiple occasions, the DOJ provided written justification to the DOA for why it felt the Benson Tower space did not meet their needs. The DOJ contends that 24-hour parking access to the facility is a requirement and that this information was communicated to the DOA when the proposal was made, but no acceptable solution was offered. In addition, the DOJ stated that the increase in annual rental costs and the cost associated with moving offices were not budgeted and would negatively impact its operations.

The DOA contends that solutions were offered for the concerns voiced by DOJ regarding relocation to Benson Tower. DOA agreed to supplement DOJ's operating budget to cover the costs for the increased rentals and for additional 24/7 parking required in a garage located down the street from Benson Tower. In addition, DOA agreed to pay for additional furniture required to accommodate the needs of DOJ's relocation to Benson Tower and any moving costs incurred. Ultimately, the DOJ did not relocate to Benson Tower.

The lease allows the state to sublease to any political subdivision of the state of Louisiana or any public commission, entity, or regional authority. In addition, the lease allows the state to sublease to nongovernment entities with prior written consent from Zelia, which consent shall not be unreasonably withheld. Currently, the State of Louisiana has only subleased its space in Benson Tower to state agencies in the executive branch of state government.

Floor	Square Feet
9th	19,434
14th	3,881
6th	1,557
Total	24,872

Compliance with Federal Regulations

Louisiana Revised Statute (La. R.S.) 39:127(D) says that the state “shall comply with federal laws and regulations and with state-federal agreements with respect to the housing of any agency, or its personnel, operations, equipment, or activities, which receives or administers any federal funds.”

Office of Management and Budget Circular A-87, Attachment B, No. 37 (Rental costs of buildings and equipment) states, “rental costs are allowable to the extent that the rates are reasonable in light of such factors as: rental costs of comparable property, if any; market conditions in the area; alternatives available; and the type, life expectancy, condition, and value of the property leased.”

The following state agencies pay for at least a portion of their respective sublease with federal program funds:

- Department of Children and Family Services (DCFS)
- Department of Health and Hospitals
- Louisiana Workforce Commission
- Office of Community Development

State agencies have expressed concern with the Division of Administration that annual rental costs charged to federal programs may not meet the definition of reasonable and cost-effective under federal program guidelines. The Social Security Administration, for example, which funds 100% of the operations for DCFS- Disability Determination Services, denied the agency’s request to relocate to Benson Tower. This agency is currently targeted for vacant space at another state-owned building in the New Orleans area.

Based on lease rates for Benson Tower space, the lease costs may exceed current market rates for comparable properties in the New Orleans area. The lease rates for the properties where these agencies were originally located have an average rate of \$19 per square foot, including parking, in 2014. As a result, the current amounts paid for the state leases in Benson Tower appear to exceed market rates.

In addition, the average cost per square foot prior to moving to Benson Tower was \$17.66, including parking, and the cost per square foot in the first year of the Benson lease was \$23.78 per square foot, including parking, an increase of \$6.12 per square foot. The additional cost associated with the increase in lease rates may not meet the definition of reasonable and cost-effective. The leases prior to Benson Tower provided more parking spaces than the current lease. In its efforts to retain the Saints in Louisiana, the State appears to be paying higher than market rates for office space in Benson Tower.

Grant funds may be due back to the federal grantor agencies if determined that lease rates exceed market rates and/or the additional costs associated with the new space are not considered reasonable and cost effective.

Recommendations

1. **The state should minimize its vacant space under lease by considering lease agreement options with entities outside of state government.** The state has only considered subleases with state agencies and boards and commissions and has not considered the possibility of subleasing to any other governmental entity (i.e., regional authorities, local governments, or public commissions).
2. **The DOA should ensure that annual lease costs charged to federal programs are “reasonable” as defined under federal program guidelines by evaluating current market rates for comparable space.**

Management agreed with the recommendations but said that it faces other challenges not outlined in this report. See management’s full response in Appendix A.

APPENDIX A: MANAGEMENT'S RESPONSE

BOBBY JINDAL
GOVERNOR



KRISTY H. NICHOLS
COMMISSIONER OF ADMINISTRATION

State of Louisiana
Division of Administration
FACILITY PLANNING AND CONTROL

August 27, 2014

Daryl G. Purpera, CPA
Louisiana Legislative Auditor
Post Office Box 94397
Baton Rouge, LA 70804-9397

Re: Analysis of Benson Tower Lease

Dear Mr. Purpera:

The New Orleans Saints are an important part of Louisiana's culture as well as an economic driver for New Orleans and the rest of the State. That's why in 2009, Louisiana reached an agreement with the franchise that would keep the Saints in New Orleans through 2025. The deal saved the State more than \$280 million through 2025 in addition to adding nearly \$400 million in revenue expected to be generated over the life of the agreement. The agreement also included Saints owner Tom Benson purchasing a vacant property and leasing some of the office space back to the State. The lease agreement with Zelia, LLC began February 1, 2011 and ends December 31, 2025. If the New Orleans Saints extend their term, the lease may be extended accordingly.

The Division of Administration (DOA) and the Office of Facility Planning and Control (FPC) agree with the recommendations in your report and have been working towards these recommendations since the lease was signed. Practically, however, there are challenges in achieving those goals that are not addressed in your report. Those challenges are outlined below:

Recommendation

- 1. The state should minimize its vacant space under lease by considering lease agreement options with entities outside of state government.**

Response

FPC has been focused on subleasing vacant space since the lease was signed. Currently, space in Benson Towers is subleased to a variety of state organizations, including the Department of Health and Hospitals, Department of Children and Family Services, Department of Public Safety, Office of Financial Institutions, Public Service Commission, South Central Louisiana Health Services District, Department of Revenue

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Space is also being leased to the Fleur de Lis Federal Credit Union, formerly the Public Health Workers Federal Credit Union.

In 2010, FPC targeted the New Orleans area Department of Justice (DOJ) staff for relocation to Benson Tower. DOJ staff worked with FPC and Zelia's architects to develop space requirements for their offices. As a result, 19,434 square feet of space on the ninth floor of Benson Tower was renovated to house DOJ operations. The space was available for occupancy in February 2011. However, as noted in your report, DOJ has not relocated to the 9th floor space. DOA attempted to fill the space with other tenants, and has had success moving all other appropriate local state agencies into the building, including the additional Alcohol and Tobacco Control within DOR and LWC functions.

In addition to state agencies, DOA and FPC have worked with the City of New Orleans on the possibility of subleasing space in the building. While the City doesn't have a current need, FPC is in the process of developing a list of other future prospects outside of state government it plans to begin targeting.

FPC will continue to market the space to appropriate entities to reduce the financial burden on the State. However, because of the challenge in customizing the space for tenants, it may take additional time to find suitable sub-lease partners.

Recommendation

- 2. The DOA should ensure that annual rental costs charged to federal programs are "reasonable" as defined under federal program guidelines by evaluating current market rates for comparable space.**

Response

Rental rate adjustments for Benson Tower go into effect each July. Rates will increase if the U.S. Consumer Price Index (CPI) increases during the preceding year. In addition, FPC will compare market lease rates to the current lease rates being charged to tenants in Benson Tower. The comparison of market lease rates will be accomplished by:

- Reviewing the Office Occupancy and Absorption Survey where rental market rates for Class A office buildings in the New Orleans Central Business District (CBD) are published each quarter.
- Surveying pass through expenses for other Class A buildings in the New Orleans CBD.
- Factoring in additional costs for parking in other Class A Buildings in the New Orleans CBD.

These comparisons will allow FPC to review current market rates in the New Orleans CBD and adjust rates in Benson Tower accordingly. FPC will also forward the results of the rate comparisons to all Benson Tower tenants to determine compliance with rental costs allowed by federal guidelines.

Daryl G. Purpera, CPA
August 27, 2014
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In making comparisons to market rates in the New Orleans CBD, the above stated factors should be considered. Class A space in the New Orleans CBD currently ranges from \$17.50 to \$21.00 per rentable square foot. Most commercial leases in Class A buildings, however, include "pass through language" which requires tenants to pay a proportionate share of operations and maintenance expenses that exceed the base year expenses established in the lease. Pass through rates vary depending on operating and maintenance expenses for each individual building as well as pass through expense terms negotiated in tenant leases. Pass through expenses can also vary depending on the occupancy rate for the building. Tenants would pay less in annual pass through expenses in a building with 100% occupancy as opposed to a building which is only 70% occupied. Pass through expenses do vary widely by space and are not published, making this component of market rates difficult to compare. The Benson Tower lease does not include pass through language, but it does allow for an annual rate increase if the CPI increases during the previous 12-month period.

Another factor to consider when comparing Benson Tower rental rates with market rates in the New Orleans CBD is the number of parking spaces included in the lease rate. Parking rates currently range from \$175 to \$200 per space per month in the heart of the New Orleans CBD. Commercial Class A buildings typically include 1 to 2 parking spaces per 1,000 square feet under lease. Parking information was not presented in the Legislative Auditor's informational report. Based on the approximate 323,000 square feet of space under lease at Benson Tower, the standard commercial lease rate would include between 323 and 646 parking spaces. The rental rate for Benson Tower, however, includes 900 parking spaces in the Superdome garages. Parking for Benson Tower tenants is also available in the state owned Health Education Authority of Louisiana (HEAL) garage which is located one block from Benson Tower. The rate charged to state tenants of Benson Tower by the HEAL garage is \$50 per space per month. This rate is approximately 50% less than the current market rates in the New Orleans CBD area.

Summary

Overall, your recommendations align with DOA and FPC's long-term goals for Benson Tower. We will continue to take steps designed to meet these guidelines, though it's important to note that fully meeting the recommendations requires the participation of forces outside of DOA's control.

Sincerely,



Mark A. Moses
Director

Daryl G. Purpera, CPA
August 27, 2014
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C: Kristy Nichols, Commissioner of Administration
Ruth Johnson, Deputy Commissioner
Meghan Parrish, Director of Communications
Marsha Guedry, Internal Audit
Randy Janies, Facility Planning and Control

APPENDIX B: SCOPE AND METHODOLOGY

We conducted procedures for this informational audit to gain an understanding of the State of Louisiana's lease with Zelia, LLC, for state office space in Benson Tower and to determine if the leased space is fairly priced and fully used to ensure the state is not incurring unnecessary lease costs. The scope of our audit was significantly less than an audit conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States.

To achieve our objective, we reviewed relevant information and performed the following steps:

- Interviewed Division of Administration (DOA), Office of Facility Planning and Control (OFPC) personnel and obtained the Benson Tower master lease and information relating to the sublease of office space by other state agencies.
- Interviewed DOA, Office of Finance and Support Services (OFSS) to obtain information relating to sublease receipts from state agencies and lease payments to Zelia, LLC.
- Reviewed and analyzed the master lease and additional documentation obtained from OFPC and OFSS.
- Obtained floor plans from the DOA, OFPC and conducted a site visit of the state office space in Benson Tower.
- Performed follow-up interviews with OFPC to obtain information relating to Benson Tower tenant selection and efforts to fill vacant space.
- Obtained information from state agencies occupying space in Benson Tower to compare prior leases to the current Benson Tower lease and determine the source(s) of funding for current Benson Tower lease payments.
- Obtained information from the Department of Justice regarding its discussions with the DOA relating to Benson Tower.
- Obtained real estate listing information to analyze current lease rates for previous leases in New Orleans, including current costs for parking.