



Department of the Interior  
Office of the Special Trustee for American Indians  
Office of Trust Review and Audit

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INDIAN TRUST INVESTIGATIVE REVIEW

PALM SPRINGS AGENCY  
COMMERCIAL LEASING ACTIVITIES

2007-043I

July 20, 2007

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## EXECUTIVE SUMMARY

According to the Secretary's Fiduciary Trust Principles for Managing Indian Trust Assets, Indian trust assets should be protected and safeguarded. Therefore, under direct delegation by the Secretary, it is the responsibility of OTRA to investigate the allegations. (300 DM2)

The Office of Trust Review and Audit (OTRA) performed an investigative review of commercial leasing activities of the Bureau of Indian Affairs' (BIA) Palm Springs Agency (Agency). We initiated this review because of recent allegations of mismanagement and a reported failure of the Agency to implement recommendations made in a prior Office of Inspector General (OIG) report.

Our objectives were to evaluate organizational performance for commercial leasing activities by the Agency to ensure the Department's trust responsibilities are being met and landowners are receiving proper benefit from leased lands.

We found the Agency should improve its administration of commercial leases in the areas of lease payment tracking and distribution, lease collections, site inspections, and compliance and operational effectiveness. We made eleven recommendations to correct identified deficiencies in the Agency's administration of commercial leases. Our findings are detailed in the *Results of Review* section of this report.

Findings are significant deficiencies identified during an examination that require management's attention and corrective action. Significant deficiencies are practices that deviate from sound fiduciary principles and are likely to result in deterioration or harm to Indian trust assets if not addressed and/or result in substantive noncompliance with laws, regulations, or court decisions. Overall, our findings and observations are provided to improve: (1) management of trust services; (2) compliance with applicable laws and regulations; or (3) internal controls.

We discussed the preliminary results of our review with Agency officials during the exit conference held on May 18, 2007.

The objective, scope, and methodology of our review are presented in Appendix 1.

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## BACKGROUND

The Palm Springs Agency is located in the City of Palm Springs. Agency staff provide real property, consulting, and land use planning services to 425 Indian allottees and the Agua Caliente Band of Cahuilla Indians (Band), who own a combined interest in about 28,000 acres primarily in and around Palm Springs, Cathedral City, and Rancho Mirage, California. Land uses on trust land within the reservation boundaries include more than 11,000 commercial, retail, and residential leases and subleases. Annual revenue from leasing on trust lands currently exceeds \$30 million. As of April 24, 2007, there were approximately 213 open Individual Indian Monies (IIM) accounts with an aggregate balance of approximately \$28.5 million.

Organization and staffing levels for the Agency has changed over the years. Approved staffing levels for the Agency have been as high as 31 during the 1990s. However, as of our review in May 2007, the Agency had only 10 employees and two vacant positions. In addition, the Agency currently has no accounting or legal staff.

In April 2007, a former Solicitor for the Agency alleged that the Agency had not yet implemented all recommendations made in the 1992 OIG audit and continuing management problems were costing the landowners because of delays on lease agreements, overdue payments, and the failure to properly assess annual rent increases.

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### PRIOR REPORTS

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In September 1992, the Office of Inspector General issued Report No. 92-I-1342, "Lease Administration, Palm Springs Field Office, Bureau of Indian Affairs." The report concluded that the Bureau had not provided sufficient management and assistance to the Agua Caliente Indian landowners to ensure that they received the proper benefits from leased lands. As a result, Indian landowners had not realized approximately \$2.1 million and might not realize an additional \$3.8 million over the remaining years of the leases. The report contained three recommendations to improve the overall management of business leases.

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In June 2005, OTRA conducted an examination of trust functions administered by the Agency (Examination Report No. 05-044). The examination included a review of management effectiveness, safeguarding of trust assets, proficiency of operations, and internal controls and compliance. The report contained seven findings with recommendations in the areas of safeguarding of trust assets, proficiency of operations, and internal controls and compliance.

Our analysis of the current status of prior recommendations related to leasing activities is presented in Appendix 2. Overall, we found the Agency has not fully implemented prior recommendations and improvements are still needed in lease administration.

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## RESULTS OF REVIEW

We found the Agency should improve its administration of commercial leases in the areas of lease payment tracking and distribution, lease collections, site inspections, and compliance and operational effectiveness. We made eleven recommendations to correct identified deficiencies in the Agency's administration of leases. We further noted other areas where either performance or proficiency in the delivery of trust services could be improved.

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### LEASE PAYMENT TRACKING

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The Agency did not actively track the payment status of leases. 25 CFR § 162.108(a) requires that BIA ensure that lease tenants meet their payment obligations to Indian landowners, through the collection of rent on behalf of the landowners and the prompt initiation of appropriate collection and enforcement actions. However, we found that the Agency did not always identify and/or follow-up on unpaid lease rentals as they came due. For example,

- One tribal lease calls for a one-time payment of \$21,760 per condo unit sold. However, the lease files contained no evidence as to whether the lessee paid a total of \$217,600 to the Band related to 10 condo units already sold by the lessee. In addition, there was no evidence that the lessee paid a \$36,000 annual rental payment due as required by the lease on August 29, 2006. The first lease payment (due "in advance" on August 29, 2005) was waived by tribal resolution. However, there was no record of payment either in the lease files or in the Trust Funds Accounting System (TFAS).
- Another lease file did not evidence whether the lessee paid the first lease rent payment of \$22,500 due on August 31, 2006. We found no record of payment in TFAS or Trust Asset and Accounting Management System (TAAMS).

Since the Agency did not always obtain copies of the checks for lease payments made directly to landowners, we could not determine if lease payments were made timely, accurately and in accordance with the lease agreement.

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25 CFR § 162.108(a) also requires that BIA assist landowners in the enforcement of payment obligations that are direct payments to the individual landowner. However, for three direct pay leases, we found no evidence the lessee paid late fees and interest as required by the lease agreement. For example,

- A \$74,346 annual rent payment was made directly to the landowner 18 days past the due date, but no fees or late payment interest was assessed by the Agency.
- For another lease, two \$50,000 annual rent payments were made directly to the landowner approximately two and seven months past the due date, respectively, but no fees or late payment interest was assessed.
- For a third lease, we found no evidence that the lessee paid late fees and interest as required by the lease agreement for a \$58,100.80 annual rent payment made directly to the landowner 18 days past the due date.

According to an internal Agency report, the Agency receives lease payments of about \$30 million annually, but the Agency has no accounting staff to verify the accuracy of payments. Realty staff also stated that TAAMS is not an accounting system and cannot be used to determine the amounts due for leases. Despite the implementation of TAAMS, manual intervention is required for lease accounting and billing activities. TAAMS does not accrue late fees and interest based on the specific requirements of each lease agreement. Agency staff stated they must "work around" TAAMS so that adjustments to lease payments can take effect. Furthermore, there is no tickler system in TAAMS, so the Agency relies on the landowners to notify the Agency if a payment is not received. Since payment amounts for most of the leases change over time, the realty staff believes that hiring an accountant would be helpful to maintain the accuracy of the TAAMS lease data. At a minimum, Agency staff should be trained in extracting reports from TAAMS to identify overdue lease payments.

## **RECCOMENDATIONS**

We recommend the Agency:

1. Perform a reconciliation of lease payments to determine whether the lessees have submitted all required rental payments in accordance with the lease agreements.

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2. Provide training on extracting reports from TAAMS to identify overdue lease payments.

### **LEASE PAYMENT DISTRIBUTION**

Our review of one 2006 gross percentage lease payment and related TFAS distribution disclosed that a "contra" amount of \$58,399 was used by the lessee (Mission Hills Country Club) to offset the lease payment due to one landowner for charges incurred at the Country Club. However, we found that the contra amount was not taken into consideration when the distribution occurred in TFAS. As a result, the contra landowner received \$33,782 more than he should have and the other landowners received less (\$33,782 collectively). Offsetting lease payments by using a contra amount is a poor accounting practice that is more likely to lead to accounting errors. In addition, using this practice, BIA could be held responsible for any errors in the lessee's billing of the landowner's Country Club account.

### **RECOMMENDATION**

3. We recommend the Agency disallow use of an offset for rent payments and require the lessee to bill the landowner directly for charges incurred at the Country Club.

### **LEASE COLLECTIONS**

Our review of lease collection processes and procedures for the Agency disclosed deficiencies and the need for improvements in the following areas:

- As of July 2, 2007, the Trust Funds Receivable (TFR) system identified 590 unpaid invoices totaling \$856,084 for the Agency. Many of these invoices date back to October 2006 and may be due to errors related to the TAAMS conversion process which occurred during October 2006 for the Agency.
- The Agency did not timely post one remittance. The remittance was received at the Agency on September 1, 2006 and deposited at the lockbox on September 5, 2006. We noted that the deposit was not posted to TFAS until September 18, 2006 (10 business days).
- For two direct pay leases we reviewed, the "pay status" was not properly identified as direct pay in TAAMS. Consequently, the Trust Funds Receivable System incorrectly identified the lease payments as collected by the Agency.

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## **RECOMMENDATIONS**

We recommend the Agency:

4. Work with OST to resolve the outstanding invoices and develop procedures to ensure that invoices recorded in the Trust Funds Receivable system are kept current.
5. Ensure that remittances are posted to TFAS within two business days after receipt at the lockbox facility.
6. Review TAAMS pay status for direct pay leases and ensure that status is correctly identified as direct pay.

## **SITE INSPECTIONS**

The Agency is not proactive in performing site inspections to monitor land use for leased lands and/or identify trespass on unleased lands. Instead, the Agency relies on the landowners to notify the Agency of any potential issues related to land usage. However, 25 CFR § 162.108(b) states that BIA will ensure that tenants comply with the operating requirements in their leases, through appropriate inspections and enforcement actions as needed to protect the interests of the Indian landowners. By conducting site inspections, the Agency would have a better knowledge of lease activities (such as construction) and other potential issues that could impact either lease performance or land values. For example, site inspections could identify payments due such as the condo units discussed above, required performance bonds, potential bankruptcies, and any trespass on unleased lands.

## **RECOMMENDATION**

7. We recommend the Agency perform periodic compliance inspections of properties in order to determine if the tenant(s) comply with the requirements of the lease agreement.

## **COMPLIANCE AND OPERATIONS**

In an Agency-prepared report, "Organizational Restructuring and Staffing Needs Analysis," dated April 13, 2007, Agency staff identified risks in the areas of (1) lease collections and revenue; (2) lease compliance monitoring; and (3) residential sublease recording. Our review of lease administration compliance and operational processes and procedures for the Agency disclosed deficiencies and the need for improvements in the following areas:

## **LEASE FILE DOCUMENTATION**

- The Agency did not document evidence of review by solicitor or legally qualified personnel. Agency officials stated that all leases have gone through a legal review as recommended in the 1992 OIG report. However, the

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lease files contained no approval signature or other documentation to evidence this review.

- We also found that the Agency did not clearly document justification for approval of lease payments at below fair market rental value. For example:

A review performed by the Regional Office for one proposed lease noted that the lease rental (\$1,827,953) was below the appraised rental value (\$1,923,000). The Agency Realty Officer stated that this was discussed with the landowners on more than one occasion, but the landowners "just didn't care." At a minimum, we believe the lease files should contain a signed and notarized statement by the landowners to document in writing that they were aware of the difference between the appraised value and the lease rental.

One tribal lease appeared to qualify for the fair | annual rental exception clause contained in 25 CFR 162.604(b) (3). However, the Agency did not clearly document why the lease was in the best interest of the Band.

- We noted that lease files did not always contain information addressing surety and/or bonding requirements. Specifically, one lease file did not provide evidence that a rental surety was secured to assure performance of contractual obligations under the lease, as required by the lease agreement and 25 CFR 162.604(c). Another lease file did not document whether a performance bond was executed prior to construction, as required by the lease agreement.

### LEASE CLAUSES

- We determined the Agency did not ensure that all lease agreements contained certain required clauses, in accordance with federal regulations. Specifically, we found that:

Lease agreements did not adequately provide for escalation of rents as required by regulation. For example, one lease agreement called for rental adjustment at the end of 10 years and every 5 years thereafter. However, the 10-year review period is not in compliance with 25 CFR 162.607 which requires a periodic economic review at not less than 5-year intervals. Also, a second lease agreement

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called for rental adjustment at the end of seven years rather than the required 5-year interval.

**TIMELY LEASE APPROVAL PROCESS**

- We noted the Agency has not always processed business lease approvals in a timely manner. For example, one business development lease took approximately eight months for the BIA to approve.

**ENCUMBRANCE RECORDATION**

- We found one approved lease was not submitted timely to the Land Titles and Records Office (LTRO) for recordation. Per 25 CFR § 150.6, "All title documents shall be submitted to the appropriate Land Titles and Records Office for recording immediately after final approval, issuance, or acceptance." However, over eight months after the August 31, 2006 approval, the lease had not been submitted to LTRO.

**COMPLIANCE WITH LEASE REQUIREMENTS – AUDITED FINANCIAL STATEMENTS**

- We noted a lease file did not contain annual audited financial statements required by the lease agreement. The file did contain compiled financial statements; however, audited financial statements are examined using procedures prescribed under Generally Accepted Auditing Standards and help to ensure the accurate reporting of gross receipts which are used to calculate rent due.

**TRESPASS ON SUB-LEASES**

- Lease rents for three residential sub-leases have not been paid since at least May 2004. This condition has existed because the Agency has not actively enforced lease compliance. As a result, at least \$14,000 due to the Indian landowners has not been collected. The Agency is required to enforce lease terms and conditions (25 CFR 162.108) and to treat unauthorized use as a trespass, take action to recover possession on behalf of Indian landowners, and pursue any additional remedies available under applicable law.

Although the Agency is ultimately responsible for enforcing lease compliance, collection of lease rents for the residential sub-leases is managed by Trust Enforcement Support Activities (TESA), a tribally-contracted entity, under a memorandum of understanding (MOU) between the Agency and the Band. However, the MOU does not clearly define responsibilities for enforcing lease compliance. The MOU will expire in September 2007 and will need to be re-negotiated.

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## **RECOMMENDATIONS**

8. We recommend the Agency develop and implement adequate compliance and operational policies and procedures to manage commercial leasing activities, including:
  - Ensure lease files clearly document legal review and rationale for approval at below fair market value, as applicable.
  - Ensure lease files contain all surety and bonding documents, as required by the lease agreement. If such documents do not exist, the lease files should provide information as to what actions the Agency is taking to ensure compliance with the lease terms.
  - Establish internal controls to ensure all lease agreements contain required clauses and conform to federal regulations.
  - Review their approval process and work towards improving the efficiency of the process to provide more timely service to the landowners.
  - Ensure approved leases are submitted to LTRO for recordation in a timely manner.
  - Ensure audited financial statements are obtained, as required by the lease agreement, and reviewed to ensure landowners are receiving fair lease rental payments.
9. We recommend the Agency take action to recover possession on behalf of the Indian landowners and/or pursue additional remedies available under applicable law.
10. We recommend the Agency ensure that the re-negotiated MOU contain provisions to address enforcement of lease compliance.
11. We recommend BIA conduct a workload analysis and develop a strategic plan to obtain and, subsequently, fund any identified needed resources. The workload analysis should review the organizational structure and current and future staffing needs, including critical skill sets to adequately manage the leasing program and fulfill trust responsibilities given the volume, complexity, and projected growth of the service area. An analysis of critical skill sets should include consideration of the need for on-site Solicitor/attorney, paralegal staff, accountants, and trust records clerk. Agency personnel have prepared a report titled "Bureau of Indian Affairs, Palm Springs Agency Organizational Restructuring and Staffing Needs

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Analysis," dated April 13, 2007. This report could provide the groundwork of a thorough workload analysis.

**OTHER MATTER**

We reviewed and compared the 18 Whereabouts Unknown (WAU) account holders identified in TFAS to selected business leases for the Agency. We found that at least three of the WAU account holders had business leases managed by the Agency. We suggest that the Agency compare its leases with the WAU accounts to identify the addresses for the WAU account holders and update TFAS accordingly.

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## OBJECTIVE, SCOPE, AND METHODOLOGY

Our objective was to evaluate organizational performance for non-agriculture /commercial leasing activities by the Bureau of Indian Affairs' Palm Springs Agency (Agency) and ensure the Department's trust responsibilities were met and fiduciary trust operations were reliable, successful, and beneficiary focused. As part of our evaluation, an additional objective was to determine whether the Agency was adequately managing commercial leases and providing sufficient assistance to the landowners to ensure landowners receive proper benefits from leased lands.

The scope of the assignment was limited to the Agency's non-agriculture/commercial leasing activities since 1992. Our review was conducted in May 2007 at the Palm Springs Agency located in Palm Springs, California. To assess the adequacy and effectiveness of the Agency's policies and practices, we:

- Reviewed Federal statutes and other guidance applicable to trust leasing functions.
- Interviewed Agency officials regarding trust leasing activities and the processing of lease transactions.
- Performed tests of the Agency's internal controls and compliance with applicable laws and regulations related to leasing activities.
- Reviewed lease files and other applicable data and reports.
- Obtained, analyzed, and tested trust-related data from the Trust Fund Accounting System and the Trust Asset and Accounting Management System.

Our review included such tests and evaluation procedure that were considered necessary to accomplish our objectives. Because our review was limited, it would not necessarily have disclosed all internal control, compliance, or other deficiencies that may exist.

We conducted our review in accordance with the *Quality Standards for Inspections* issued by the President's Council on Integrity and Efficiency.

## RESULTS OF REVIEW OF PRIOR RECOMMENDATIONS

As part of our review, we reviewed prior audit/report findings and recommendations made by the OIG and OTRA related to commercial leasing activities at the Palm Springs Agency. To the extent possible in our limited scope investigative review, we evaluated the current status of prior recommendations related to leasing activities. The purpose of this analysis was to determine the validity of allegations regarding failure of the Agency to implement prior recommendations, thus allowing management deficiencies to continue.

**Office of Inspector General Report No. 92-I-1342, issued September 1992**

Recommendation:

1. Require area and field office directors to ensure that leases are approved at fair market value and include escalation clauses for inflation.

OTRA Determination:

We determined the Agency still has deficiencies relating to documenting exceptions to the fair market value requirements and ensuring escalation clauses comply with regulations for all of its leases. Although improvements have been made, corrective actions are still needed for full implementation.

Recommendation:

2. Assign a solicitor or legally qualified personnel to assist the Agency in performing a detailed review of all lease files and to bring lessees into compliance with lease terms.

OTRA Determination:

We determined an on-site Solicitor was assigned to the Agency after the OIG recommendation. However, currently, the Agency does not have a Solicitor on-site for detailed reviews of its leases. In fact, the former Solicitor at the Agency made the recent allegations of lease mismanagement. Agency personnel stated that leases were being sent to the Solicitor for review. However, we found that lease files did not have evidence of review by a solicitor or other legally qualified personnel. Thus, we could not confirm that the recommendation is implemented.

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Recommendation:

3. Develop and implement compliance and collection policies and procedures to administer business leasing activities.

OTRA Determination:

Based on our review of lease collection processes and procedures for the Agency, we determined the Agency still has deficiencies and the need for improvements in the areas of lease collections and administration. Although the deficiencies are not as pervasive, the recommendation has not yet been fully implemented.

**Office of Trust Review and Audit Report No. 05-044, issued November 2005**

Recommendation:

1. Prepare and distribute a template of requisite provisions to outside attorneys submitting lease agreements for approval and use a checklist of required provisions during its review of submitted leases to ensure they contain mandatory provisions.

OTRA Determination:

We determined that the Agency does use a checklist. We did not verify if the template was distributed and used. Although, we identified no specific instances whereby required lease provisions were missing from a lease document, we found the Agency did not always enforce and/or document lease provision requirements.

Observation:

- Maintain an comprehensive inventory of leases that provides management with lease name, number, start and end dates, payment amounts and due dates to allow management to have better control over the administration and enforcement of leases.

OTRA Determination:

With implementation of TAAMS, the Agency should now have the ability to produce an inventory, and with the development of adequate processes and controls should have the ability to better monitor and enforce lease payments. The recommendation has not been fully implemented.