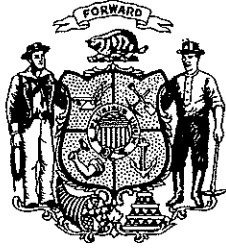


State of Wisconsin

SENATE CHAIR
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ASSEMBLY CHAIR
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Joint Committee on Finance

MEMORANDUM

To: Members
Joint Committee on Finance

From: Senator Howard Marklein
Representative Mark Born

Date: February 15, 2022

Re: 14-Day Passive Review Approval – DOA

Pursuant to s. 16.004(8), Stats., attached is a 14-day passive review request from the Department of Administration, received on February 15, 2022.

Please review the material and notify **Senator Marklein** or **Representative Born** no later than **Friday, March 4, 2022**, if you have any concerns about the request or if you would like the Committee to meet formally to consider it.

Also, please contact us if you need further information.

Attachments

HM:MB:jm



STATE OF WISCONSIN
DEPARTMENT OF ADMINISTRATION

Tony Evers, Governor
Kathy Blumenfeld, Secretary-designee

February 15, 2022

Senator Howard Marklein
Representative Mark Born, Co-chairpersons
Joint Committee on Finance
State Capitol
Madison, Wisconsin 53702

FEB 15 2022
St. Finance

Dear Senator Marklein and Representative Born,

Enclosed for your review is a report on proposed changes to the Department of Administration-maintained system of rental policies for state-owned housing administered by state agencies pursuant to s. 16.004(8), Wis. Stats. The existing system of rental policies was submitted to the Joint Committee on Finance for review and adopted by the Department in 1976. Since that time there have been significant statutory changes affecting state-owned housing and the system of rental policies have not been updated to reflect those changes. In December 2019, the Department's compliance with s. 16.004(8), Wis. Stats. was the subject of a Legislative Audit Bureau Report, which made several recommendations for updating the existing system of policies.

The Department has conducted an extensive review of the Bureau's Report, the existing system of rental policies and the statutory requirements of s. 16.004(8), Wis. Stats., working closely with those state agencies that maintain the majority of existing state-owned housing. Based on that review the Department has substantially re-written the existing system of policies and is submitting the proposed changes to the Joint Committee on Finance for review. Below is a summary of the recommendations contained in the Bureau's Report and the proposed changes that address those recommendations.

1. LAB's Recommendation: ensure that state agencies provide confirmation that the CPI rent adjustments are implemented.

The existing system of policies, which was written to reflect the statutory requirements of 1976, calls for a uniform biennial rental rate review and adjustment submitted to JCF for approval. In 1991 the legislature amended s. 16.004(8), Wis. Stats., to establish a formula for automatic biennial rental rate adjustments based on the consumer price index. While the existing system of policies does not reflect this change in adjustments the Department has nonetheless sent biennial letters to state agencies advising them of the applicable rental rate adjustment based on the consumer price index.

The proposed revisions include specific changes intended to reflect the statutory requirement for biennial rental rate adjustments based on CPI. These proposed changes include not only a requirement for agencies to apply such adjustments, but also a process for the Department to update the state-owned housing inventory on a biennial basis and notify agencies of the applicable rental rate adjustments to each specific property identified in the updated inventory. In addition, the proposed revisions include a

standard lease template for agencies to use that incorporates specific language to address biennial CPI-based rental rate adjustments.

2. LAB's Recommendation: work with agencies to reassess whether to retain state-owned residential properties, including recommending to SBC whether any properties should be sold, razed, or used for other purposes.

Section 16.004(8), Wis. Stats., requires that the system of policies include a procedure for the review of the need to retain state-owned housing units and possible disposition thereof, with the Department making recommendations to the State Building Commission for any potential sale. This requirement overlaps with section 13.48(14)(d), Wis. Stats., which requires state agencies to report to DOA on a biennial basis underutilized property, which in turn is reported to SBC.

The existing system of policies called for a general phase out of non-essential housing by the end of the 1987-81 biennium. The proposed revisions include specific changes directing agencies to include in their biennial underutilized property report the identification of state-owned housing they have determined is underutilized.

3. LAB's Recommendation: Improve administration by complying with statutes by periodically reviewing and formally revising applicable policies

Section 16.004(8), Wis. Stats., requires the Department to periodically review the system of rental policies for possible changes. As noted above, the system of policies has not been updated since 1976. The existing system of policies does not specifically address periodic review for possible changes. The proposed revisions include specific changes directing the Department to conduct a biennial review with solicitation of input from all agencies that administer state-owned housing.

4. LAB's Recommendation: Improve administration by tracking rental properties and monitoring rental payment amounts state agencies charge employees.

As discussed above, after the adoption of the existing system of policies in 1976 the legislature amended s. 16.004(8), Wis. Stats., to establish a uniform statutory methodology for determining rental rates for state-owned housing. Those statutory requirements include the biennial CPI-based adjustments already mentioned, as well as appraisal-based adjustments every ten years or as needed in the event of major renovations.

The existing system of policies does not contain specific language requiring agencies to provide periodic updates to the Department regarding their inventory of state-owned housing units. The proposed revisions: 1) include specific changes directing agencies to provide updated state-owned housing inventories to the Department on a biennial basis; 2) direct agencies to make biennial CPI-based rental rate adjustments and decennial appraisal-based adjustments; 3) provide a standard lease template for agencies to use that incorporates language regarding the mandatory rental rate adjustments; and 4) directs agencies to deposit rental revenues from state-owned housing into statutorily required accounts that the Department can cross-reference against the biennial housing inventory agencies submit to the Department.

5. LAB's Recommendation: Improve administration by complying with statutes to conduct appraisals of state-owned residential properties.

The existing system of policies does not specifically call for decennial appraisals of state-owned housing as required by s. 16.004(8), Wis. Stats., because such statutory requirement did not exist at the time the

system of policies was adopted. The proposed revisions replace the existing system of policies' provisions, which call for annual individual unit assessments, with provisions consistent with s. 16.004(8), Wis. Stats., regarding appraisal-based rental rate adjustments. More specifically, the proposed revisions establish procedures for the Department to conduct appraisals to determine decennial rental rate adjustments and to have agencies apply those adjustments to each housing unit.

6. LAB's Recommendation: Ensure the system of rental policies sets forth clearly defined responsibilities of DOA and state agencies.

As discussed above, the proposed revisions involve a wholesale rewrite of the existing policy to address statutory changes, the specific findings in the Bureau's Report, and the Department's general review of the existing system. These proposed revisions incorporate several changes intended to set forth clearly defined responsibilities of the Department and the state agencies that maintain state-owned housing. The instances in which Department and agency responsibilities are specifically delineated are too numerous to enumerate, but the following are representative examples:

- IV.A.1.i. (Decennial Appraisal-Based Rental Rate Adjustments)
 - o Sets forth procedures for the Department to obtain the necessary appraisals
 - o Requires the Department to provide written notice to the agencies that the appraisals will be conducted and that rental rates will be adjusted accordingly
 - o Directs the agencies to notify tenants of any applicable changes to their rental rates
- IV.A.1.iii. (Biennial CPI-Based Rental Rate Adjustments)
 - o Directs the Department to send notice to agencies to provide biennial updates to their housing inventory
 - o Directs agencies to provide updated inventory information
 - o Directs the Department to calculate CPI-based rental rate adjustments and notify the agencies
 - o Directs the agencies to notify tenants of any applicable changes to their rental rates
- IV.A.2. (Procedures for Obtain Appraisals)
 - o Sets forth specific procedures the Department must follow in obtaining appraisals
 - o Directs agencies to notify their tenants that an appraisal will be taking place
- IV.A.3. (Adjustments to Base Rental Rates)
 - o Establishes procedures for the Department and agencies to work collaboratively to make certain adjustments to rental rates based on certain permissible factors on a case-by-case basis.
- IV.D. (Future Acquisitions)
 - o Directs agencies to promptly notify the Department of the acquisition of new housing units.
 - o Directs the Department to appraise the property for purposes of determining applicable rental rates.

7. LAB's Recommendation: Increase responsibility for monitoring lease agreements with state employees.

The existing system of policies does not include specific language addressing monitoring of lease agreements with state employees. The proposed revisions incorporate changes intended to provide the Department with periodic updates on such agreements. Specifically, as part of its response to the Bureau's Report the Department requested all state agencies to provide it with copies of existing lease agreements as well as an updated inventory of all housing units. The proposed revisions: 1) require agencies to provide biennial updates on housing inventory, including occupancy and any changes in tenancy; 2) establish automatic procedures for biennial and decennial rental rate adjustments; 3)

provide direction to state agencies with regard to where rental revenue must be deposited; and 4) establish a standard lease template for agencies to use that incorporates the required rental rate adjustments.

8. LAB's Recommendation: Identify potential statutory changes as necessary regarding the frequency of appraisals.

This particular recommendation falls outside of the scope of submitting this Report to JCF, the purpose of which is to propose changes to the existing system of policies. Nonetheless, the proposed changes do incorporate language directing the Department to periodically review the system to determine the need for any changes, which may include the need for statutory changes. The Department has reviewed existing statutes and has determined that at this time there is no need for any specific changes.

9. LAB's Recommendation: Consider how to establish base rental payment amounts for new property and how to adjust amounts for factors that significantly affect the fair value of the property.

The existing system of policies does not specifically address the establishment of rental rates for newly acquired housing. The proposed revisions include a specific section on new housing, which requires agencies to promptly notify the Department, and for the Department to obtain an appraisal of the property to establish a base rental rate for the new unit in the same manner as rental rates are established for existing housing every decennial.

With respect to the Bureau's recommendation for establishing how to adjust rental amounts for factors that significantly affect the fair value of property, in the Department's response to the Bureau's Report we noted that s. 16.004(8), Wis. Stats., only permits two types of adjustments to base rental rates in between the decennial appraisal-based adjustments: 1) biennial CPI-based adjustments; and 2) appraisal-based adjustments when a property has been affected by a major renovation. Nonetheless, the proposed revisions include a section requiring agencies to provide the Department with notification in the event that any change in circumstances may affect housing units, including change in status of occupancy, significant damage, lease termination, change in tenant, renovations, change in use, or any other change that the agency reasonably believes may affect the rental rate charged for the unit.

10. LAB's Recommendation: Work with state agencies to determine the tax implications, if any, that result from instances in which rental payment amounts charged to employees who opted to reside in state-owned properties were less than fair value.

The existing system of policies does not specifically address tax implications for employees who are provided state-owned housing at below market rates. Nonetheless, the existing system of policies contains several provisions that allow agencies to subsidize rent based on various factors. These provisions are no longer consistent with the statutory formulas established under s. 16.004(8), Wis. Stats.

The proposed revisions include wholesale changes to the manner in which rental rates are determined to comply with s. 16.004(8), Wis. Stats., which effectively requires agencies to charge employees market rate rents. The proposed revisions also include wage-based rental caps for employees living in mandatory housing, specific parameters for what constitutes mandatory housing, and limits on the amount of reduction agencies can apply. The Department conducted extensive analysis of applicable tax laws to ensure that these wage-based rental caps for mandatory housing do not result in reportable income to affected employees.

The proposed revisions also give agencies discretion to provide rent reductions for employees who perform certain duties related to their occupancy of such housing. As an example, by virtue of their proximity to campers DNR Park Rangers who live in state-owned housing with state parks may be expected to provide services outside of normal working hours. The proposed revisions make it clear that agencies are responsible for determining any tax implications for employees and requires them to provide the Department with documentation showing the work or services to be performed by the employee, the expected number of hours the employee will spend each month performing such work, and the hourly wage rate used to determine the rental rate adjustment. The proposed revisions also set forth procedures for determining tax implications for employees paying below-market rent and withhold and reporting requirements.

11. LAB's Recommendation: Develop policies that specifically address how University of Wisconsin System Administration should determine rental payment amounts for employees who opt to reside in state-owned properties.

The existing system of policies does not contain any provisions that specifically address non-mandatory housing for university employees. In response to this recommendation the Department has chosen to establish uniform policies applicable to all state agencies, including UW System employees, that are consistent with s. 16.004(8), Wis. Stat. Thus, under the proposed revisions UW System employees will be charged fair market rent based on decennial appraisals and biennial CPI-based adjustments and will be required to enter into lease agreements with UW System using the standard lease template proposed in these revisions.

12. Other Notable Revisions

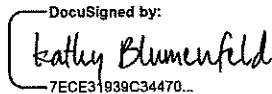
In addition to addressing the Bureau's recommendations the proposed revisions are reflective of the Department's overall review and analysis of the existing system of policies, applicable law, and changes in the housing market over the last forty-five years. Such proposed changes include the following:

- Increasing the wage-based salary cap from 12% of an employee's monthly wages to 25%, which more accurately reflects the average percentage of an employee's income spent on housing in 2021.
- Removal of provisions in the existing system of policies establishing separate rental rates for apartments, duplexes and dormitory rooms. Under the proposed revisions rental rates for all state-owned housing units, regardless of type, will be determined using uniform methods prescribed by s. 16.004(8), Wis. Stats. The revised policy would allow for an exception for employee occupancy in multi-unit facilities open to employees and non-employees alike, provided that employees are not given any preference with respect to occupancy or rental rates, and the agency can demonstrate that the units are leased at market rates.
- Removal of provisions in the existing system of policies establishing procedures for review and updating of rental rates. These provisions are supplanted in the proposed revisions by uniform methods prescribed by s. 16.004(8), Wis. Stats.
- Removal of provisions in the existing system of policies establishing procedures related to the phase-out of unnecessary housing. These provisions were included in the 1976 system of policies to accomplish the specific task of disposing of what at the time had been a large surplus of unnecessary state-owned housing. The Department developed and implemented a five-year plan that resulted in a significant reduction in state-owned housing. The proposed revisions incorporate

provisions requiring agencies to include any state-owned housing they manage in their biennial underutilized property report to the Department as appropriate.

In accordance with s. 16.004(8) the JCF chairpersons have fourteen days from the date or receipt of this report to notify the Department of its intent to schedule a meeting for the purpose of reviewing the recommended changes in rental policies. If no such notice is provided the Department may implement any recommended changes contained in this report.

Sincerely,

DocuSigned by:

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Kathy Blumenfeld
Secretary

- Enclosures:
- 1) Proposed DOA State-Owned Housing Rental Policy
 - 2) 1975 DOA State-Owned Staff Housing Report
 - 3) 2019 LAB Report on State-Owned Rental Housing
 - 4) DOA Response to LAB Audit Report on State-Owned Housing Rentals
 - 5) Attachment A-State Owned Housing Rental Inventory Worksheet
 - 6) Attachment B -DOA State-Owned Rental Housing Lease Template

Rental Policies for State-Owned Housing

(Date 2.9.2022)

I. PURPOSE

The purpose of this document is to set forth a system of rental policies for state-owned, employee occupied housing administered by State of Wisconsin agencies and the University of Wisconsin pursuant to section 16.004(8) of the Wisconsin Statutes.

II. HISTORY

The State-Owned Housing Rental program originated with the Laws of 1975 – Chapter 39 – Section 716(5), which required the Department of Administration (DOA) Secretary, in conjunction with other state agencies, to develop a plan for improving the efficiency in the utilization of staff housing. The plan called for criteria for the designation of housing for mandatory and optional housing; uniform policies for rental rates for each of the categories of mandatory and optional occupancy; procedures related to the phase-out and disposition of unnecessary state-owned employee housing; and procedures for reviewing and updating approved rental rates. Later that year the legislature added subsection (8) to Wisconsin Statutes section 16.004, which required the DOA Secretary to establish and maintain a system relating to the rentals charged for state-owned housing, review the system for possible changes every two years, and submit such recommendations to the Joint Committee on Finance (JCF) every two years. Subsection (8) required DOA to include in its system a procedure for review of the need to retain state-owned housing units and possible disposition of such units.

Subsection (8) was revised in the 1981-82 and 1987-88 biennia. The 1981 revision specified that JCF's review of DOA's biennial recommendations had to include approval of a rental rate structure for the following two-year period. The 1987 revision clarified that the reports to JCF were to include proposed changes to rental rates and added passive approval if a meeting to review the recommendations was not scheduled within 14 working days after submission by DOA.

Subsection (8) was revised again during the 1991-1992 biennium. The requirement for DOA to submit a biennial report of changes to the rental rates and/or policies to JCF was removed and replaced with a requirement to submit such proposed changes (other than changes to rental rates) to JCF only when the DOA Secretary determines that such changes are necessary. The changes also removed the requirement for DOA to submit proposed rental rate changes to JCF for review and approval and replaced it with statutory procedures for adjusting rents. Under this statutory framework rents are adjusted in three ways (explained in more detail in IV.A.1. of this policy):

- 1) Once every ten years based on appraisals of the fair market value of the housing units.
- 2) From time-to-time as is necessary, based on appraisal of the fair market value when a housing unit undergoes major renovation; and
- 3) Every two years (excluding those years where an adjustment is made based on the 10-year appraisal) based on changes to the consumer price index.

III. DEFINITIONS

In this policy the following terms, when capitalized, have the meanings set forth in this section unless otherwise specified:

- A. **“Adjusted Rental Rate”** means the monthly rental rate for a Housing Rental Unit as determined by applying the adjustments set forth in section IV.A.3. to the Housing Rental Unit’s Base Rental Rate.
- B. **“Base Rental Rate”** means the monthly rental rate for a Housing Rental Unit as determined pursuant to section IV.A.1. before making adjustments thereto under to section IV.A.3. & 4.
- C. **“Fair Market Rental Rate”** means the amount of money that a Housing Rental Unit would rent for per month as determined pursuant to section IV.A.2.
- D. **“Fair Market Resale Value”** means the amount of money that a Housing Rental Unit would sell for as determined pursuant to section IV.A.2.
- E. **“Housing Rental Unit”** means a residential dwelling, including a single-family house, a single-family unit in a duplex, multi-family or multi-purpose property, a condominium or cooperative housing unit, a sleeping room, a mobile home, or other residential unit, whether furnished or unfurnished, that is owned by a state agency or the University for the purpose of providing a primary place of residence to state agency or university officers or employees.
- F. **“Mandatory Housing Rental Unit”** means a Housing Rental Unit that meets all the following conditions:
 - 1) Is leased by an agency to an employee-tenant who is required to accept such lodging as a condition of his/her employment;
 - 2) Is located on property owned by the agency leasing the Housing Rental Unit; and
 - 3) Is provided to the employee-tenant for the convenience of the agency.

For purposes of this definition requiring an employee-tenant to accept lodging as a condition of his/her employment is only a satisfying condition if the employee-tenant must live in the Housing Rental Unit to be able to properly perform his/her duties.

For purposes of this definition the provision of housing to an employee-tenant is for the convenience of an agency if the agency has a substantial business reason other than to provide the employee-tenant with additional compensation.

- G. **“Non-Mandatory Housing Rental Unit”** means a Housing Rental Unit that is not a Mandatory Housing Rental Unit.
- H. **“Rental Rate”** means the monthly rental rate for a Housing Rental Unit as determined by section IV.A.4.
- I. **“Wage-Based Rental Cap”** means the maximum amount of monthly rent an agency or the University can charge an employee-tenant when leasing a Mandatory Housing Rental Unit. An employee-tenant’s Wage-Based Rental Cap is determined by taking the employee’s annual salary, dividing it by 12 and then multiplying it by 25%. The wages of Employee-tenants

occupying Mandatory Housing Rental Units Wage shall be reviewed annually in July prior to receiving the CPI adjustment rate increases that occurs August 15th.

IV. UNIFORM RENTAL RATE STRUCTURE POLICY

A. Establishment and Adjustment of Rental Rates

Rental Rates are determined by first establishing a Base Rental Rate and then applying certain adjustments as applicable to determine an Adjusted Rental Rate. For Non-Mandatory Housing Rental Units, the Rental Rate shall be the Adjusted Rental Rate. For Mandatory Housing Rental Units agencies must take the additional step of determining the employee-tenant's Wage-Based Rental Cap. For Mandatory Housing Rental Units, the Rental Rate shall be the lesser of the Adjusted Rental Rate and the Wage-Based Rental Cap.

1. Determining Base Rental Rates

Section 16.004(8) of the Wisconsin Statutes sets forth three ways for establishing and updating Base Rental Rates for state-owned housing.

i. Appraisal-Based Rental Rate Adjustments Every Ten Years

No later than July 1 of the 2nd year following each federal decennial census DOA must obtain appraisals of the fair market value of all Housing Rental Units. DOA is required to determine and fix Rental Rates for such units based on those appraisals, with the new rates taking effect on the following August 15.

DOA shall provide a written reminder to all agencies that own Housing Rental Units that DOA will be conducting appraisals on such units and that Rental Rates will be adjusted accordingly. Once the appraisals have been completed DOA shall determine the applicable Base Rental Rate for each unit and notify each agency of such determination. DOA and the agencies will then work collaboratively to determine if any adjustments to the Base Rental Rates should be made in accordance with section IV.A.3-4. The agency shall be responsible for notifying its employee-tenants of any applicable changes to their Rental Rates.

ii. Appraisal-Based Rental Rate Adjustments for Major Renovations

If DOA determines that a Housing Rental Unit has been affected by a major renovation DOA **may** obtain an appraisal of the fair market value of the renovated unit, and if it does so **must** determine and fix a new Rental Rate based on the appraisal. If the appraisal is obtained prior to July 1 of any year, the rate shall take effect on August 15 of that year; otherwise, it shall take effect on August 15 of the following year.

Agencies that own Housing Rental Units shall notify DOA in writing of any renovations to such units upon completion thereof. DOA will then determine whether to appraise the unit for the purpose of adjusting the Rental Rate. DOA shall notify the agency in writing of its determination. If DOA chooses not to appraise the unit, then no rent adjustment will be made. If DOA chooses to appraise the unit, then the new Base Rental Rate shall be determined as set forth in this section, and DOA shall notify the agency of such determination. DOA and the agency will then work collaboratively to determine if any

adjustments to the Base Rental Rate should be made in accordance with section IV.A.3-4. The agency shall be responsible for notifying its employee-tenants of any applicable changes to their Rental Rates.

iii. Biennial Rental Rate Adjustments Based on Cost-of-Living Adjustments

If no appraisal of a Housing Rental Unit is made during the 24-month period ending on July 1st of any even-numbered year, the current Rental Rate for the unit must be subject to a biennial cost-of-living adjustment. Six months prior to notifying agencies of the applicable cost-of living adjustments DOA shall request an updated list of all Housing Rental Units. Agencies shall provide responses within 60 days using the State-Owned Housing Rental Unit Inventory Worksheet attached hereto as **Attachment A**. In addition to completing the worksheet agencies that have made any modifications to leases since the last 24-month period shall provide copies of such leases to DOA.

To determine the adjustment, DOA will reference the 12-month change in the consumer price index for all items, U.S. city average, from the U.S. Bureau of Labor Statistics for December of the preceding year, multiply the current rental rate by that percentage, then add the product to the current rental rate and round to the nearest whole dollar. DOA will then notify the agencies in writing of the applicable cost of living adjustment to rent for each affected Housing Rental Unit. The new rental rate must take effect on August 15th.

Cost-of-living rental rate adjustments made pursuant to this section shall not be subject to section IV.A.3 adjustments, provided, however, that in the case of Mandatory Housing the CPI-based rental rate adjustments shall not result in a rental rate that exceeds the Wage-Based Rent Cap. The agency shall be responsible for notifying its employee-tenants of any applicable changes to their Rental Rates.

2. Determining Fair Market Value of Housing Rental Units

A Housing Rental Unit's Fair Market Rental Rate shall be determined by appraisal. For the decennial appraisal of all Housing Rental Units DOA shall request an updated list of such units from agencies. Once DOA has verified the inventory, or in the case of an appraisal arising from a major renovation of a unit, once DOA has determined that a rent adjustment is necessary, DOA shall be responsible for procuring a qualified appraiser or appraisers to perform an appraisal or appraisals of such unit(s). DOA shall charge the cost of such appraisals to the appropriation specified in section 16.40(19) of the Wisconsin Statutes or, if there is no such appropriation, to the appropriation or appropriations which fund the program in connection with which the housing is utilized.

DOA will provide instructions to appraisers that the purpose of the appraisal is to determine the Fair Market Rental Rate of the unit(s) being appraised, and that the preferred method for making such determination is an economic approach that examines the rental rate of comparable housing rental units in the community.

Under certain circumstances an appraiser may advise DOA that this economic approach may not be a suitable method for determining fair rental value (e.g., when a housing unit is in a remote location, or when a housing unit is so unique that there are no other comparable units in the community). In such instances DOA may advise the appraiser to determine the Fair Market

Resale Value of the unit using whatever methodology, in the appraiser's professional judgment, will most accurately reflect the unit's resale value. DOA will then multiply the unit's Fair Market Resale Value by the State of Wisconsin Investment Board's expected nominal rate of return on real estate investments as reported in the Department of Employee Trust Funds' most recent Wisconsin Retirement System Financial Report. The result will be determinative of the annual fair market value rental rate of the unit, which shall be divided by 12 to determine the monthly Fair Market Rental Rate.

Agencies shall be responsible for notifying their employee-tenants who occupy Housing Rental Units that an appraisal will be taking place and shall coordinate with the appraiser(s) and employee(s) to schedule any necessary appraisal appointments once DOA has procured such services.

3. Adjustments to Base Rental Rates

Once the Base Rental Rates for Housing Rental Units have been determined DOA and the agencies will then work collaboratively to determine if any adjustments to such rates should be made.

i. Permissible Factors to Consider in Making Adjustments to Base Rental Rates (All Housing rental units)

The following factors may be taken into consideration by DOA and the agencies in adjusting applicable Base Rental Rates for all Housing Rental Units:

- a) A reduction to the Base Rental Rate if a portion of the unit is included in the demised premises but is not accessible or usable to the employee-tenant for dwelling purposes or is required by the agency to be used to conduct agency business. Any portion of the demised premises to which this section applies must be specifically designated in the lease agreement. Reductions must be calculated by dividing the gross square footage of the portion of the demised premises to which this section applies by the total gross square footage of the entire demised premises.
- b) An adjustment to the Base Rental Rate may be permitted if the employee-tenant performs work or services related to the agency's ownership of the rental unit (e.g. exterior painting,) and the reduction in rent is intended to compensate the employee-tenant for such work in lieu of wages. The agency shall be responsible for compliance with any applicable IRS and DOR rules regarding the treatment of such rent reduction as income to the employee and shall provide DOA with documentation showing the work or services to be performed by the employee-tenant, the expected number of hours the employee-tenant will spend each month performing such work or services, and the hourly wage rate the agency is using to determine the rental rate adjustment.

ii. Permissible Factors to Consider in Making Adjustments to Base Rental Rates for Mandatory Housing

In addition to the factors enumerated in section IV.A.3.i. DOA and the agencies may take into consideration the following factors when adjusting applicable Base Rental Rates for Mandatory Housing Units:

- a) An inconvenience to the employee and benefit to the State where the employee lives in mandatory housing. Occupants performing additional duties beyond normal working hours that may cause a lack of privacy or disruption related to providing services required of their employment (e.g., a park ranger who has visitors stopping at his/her residence during non-working hours.).
- b) An adjustment to the rental rate may be permitted if the dwelling is poorly insulated or weatherized and the employee incurs unreasonable heating or cooling costs.

4. Application of Rental Rate Adjustment Factors

Once DOA and the agency have determined which section IV.A.3. factors are applicable to a Housing Rental Unit and the extent to which such factors impact the Base Rental Rate the agency shall make adjustments to the Base Rental Rate for the unit.

- i. **As applied to Non-Mandatory Housing Rental Units**, such adjustments shall not result in Rental Rate that is less than 50% of the Base Rental Rate.
- ii. **As applied to Mandatory Housing Units**, the agency shall first make the applicable adjustments to the Base Rental Rate to determine the Adjusted Rental Rate, which shall not be less than 50% of the Base Rental Rate. The agency shall then determine the employee-tenant's gross monthly wages, multiplied by 25%, to determine the Wage-Based Rent Cap. The Rental Rate shall be the lesser of the Adjusted Rental Rate and the Wage-Based Rent Cap.

The new Rental Rate shall go into effect as set forth in section IV.A.1.

B. Charges for Provided Amenities

The following costs shall be charged by the agency to its employee-tenants, as applicable, in addition to rent:

1. Utility services, including telephone, should be furnished by a third-party provider, and billed directly to the employee-tenant wherever possible. If direct billing from and payment to the provider is not possible, then the agency shall determine the housing rental unit's actual usage and bill the employee-tenant. If a utility service is provided to a Housing Rental Unit and the employee-tenant uses the utility service for both personal and business use the agency may prorate the amount it charges to the employee-tenant based on the agency's determination of the extent to which such utilities are used for business-related purposes, and in a manner consistent with any applicable guidance from the IRS and DOR relating to the treatment of such payments as income for tax purposes.
2. Convenience maintenance services, such as lawn mowing, trash removal, snow removal or gardening, that are provided to a Housing Rental Unit shall be paid by or charged to the employee-tenant. Agencies may prorate such charges where the services are provided to a multi-tenant facility, or where the Housing Rental Unit is part of a facility for which such

services must be provided for all or part of the remainder of the facility. Prorations shall be calculated based on gross square footage.

3. To the extent that an agency provides certain amenities to an employee-tenant in connection with occupancy of a Housing Rental Unit, such as meals or cleaning service, the agency shall charge the employee-tenant for such amenities separately from rent.

C. Rental Rate Changes Due to Changes in Circumstances

In addition to any other information agencies are required to provide to DOA as set forth in this policy, agencies must provide an update upon request on any change in circumstances that may affect Housing Rental Units, including the following:

1. Change in status of occupancy (mandatory to non-mandatory or vice versa);
2. Damage to a Housing Rental Unit rendering all or a portion of it untenable;
3. Lease termination/expiration;
4. Change in tenant;
5. Change, improvement, or renovation, that may impact a unit's fair market value;
6. Change in use of a unit to a non-residential use; and
7. Any other change that may potentially result in an adjustment to a unit's Rental Rate.

To the extent that DOA approval is needed prior to implementing a Rental Rate change the proposed change shall be deemed approved if DOA does not respond within 30 days. Changes that do not require DOA approval may be implemented at the agency's discretion and in accordance with the circumstances giving rise to the change. Agencies may not implement any change in Rental Rates that are not consistent with this policy.

D. Future Acquisitions

If an agency adds Housing Rental Units to its inventory, either by acquisition or by converting existing facilities to housing, the agency must promptly notify DOA. DOA will hire a qualified appraiser to perform an appraisal of any new Housing Rental Units to determine the Base Rental Rate for the unit. DOA and the agency will then establish the applicable Rental Rate for the unit as set forth in section IV.A.

V. INCOME REPORTING RESPONSIBILITIES

A. Employees of Agencies Other than the University of Wisconsin

The Internal Revenue Service requires employers to report as income the provision of lodging to employees under certain circumstances. This section provides a general summary of IRS guidance. However, agencies are responsible for familiarizing themselves and complying with all applicable IRS rules.

DOA Central Payroll is responsible for withholding taxes on executive branch agency employees' paychecks and reporting income on employees' W-2s. The provision of Mandatory Housing to employees is not reportable as income, but it is the responsibility of the agencies to provide the following documentation to DOA Central Payroll demonstrating that the housing provided qualifies as Mandatory Housing:

1. Documentation that the employee was required to accept such housing as a condition of his/her employment. Such documentation must include an explanation as to why the employee must live in the provided housing in order to be able to properly perform his/her duties.
2. Documentation that the housing is provided to the employee for the convenience of the agency. Such documentation must include an explanation as to what substantial business reason the agency has for providing housing to the employee.

Agencies shall supply such documentation to DOA Central Payroll no later than thirty (30) days from the date of the employee's occupancy of Mandatory Housing.

The provision of housing to employees that is not Mandatory Housing may result in reportable income and tax withholding to the extent that the Fair Market Rental Rate exceeds the Rental Rate paid by the employee. Within thirty (30) days of any of the following triggering events agencies shall work with DOA Central Payroll to provide information necessary for reporting any income and withholding any taxes resulting from the provision of housing:

1. The employee's occupancy of the housing;
2. Any change in the rental rate charged to the employee;
3. The employee's vacancy of the housing.

DOA shall ensure that DOA Central Payroll is provided with information about appraisals of Housing Rental Units and biennial rental rate adjustments based on cost-of-living adjustments in a timely manner so that DOA Central Payroll can accurately determine, for each Housing Rental Unit occupied by an executive branch agency employee, what the unit's fair market rental rate is.

B. Employees of the University of Wisconsin

The provision of housing to University employees is subject to IRS income reporting and tax withholding requirements. However, DOA Central Payroll is not responsible for income reporting for or tax withholding of University employees. It is the University's responsibility to ensure that it complies with applicable IRS rules on incoming reporting and tax withholding related to the provision of housing for its employees.

VI. UNIFORM LEASE POLICY

DOA recognizes that each Housing Rental Unit and employee-tenant presents their own unique set of circumstances, and that agencies will need to tailor each lease agreement to address those circumstances. DOA also recognizes that uniformity and consistency in lease administration ensures

equitable outcomes for both agencies and employee-tenants. To ensure consistent administration of state-owned rental housing agencies should, to the extent practicable, use the Standard State-Owned Housing Rental Unit Lease Template attached hereto as **Attachment B** when drafting lease agreements with employee-tenants.

Agencies may incorporate additional terms into leases provided such terms do not conflict with the policies set forth herein. In rare circumstances agencies may need to tailor a lease agreement by modifying or deleting standard terms and conditions set forth in the lease template. Agencies must first notify DOA prior to modifying or deleting such terms and conditions, provide an explanation for the need for such change, and obtain DOA consent prior to entering into a lease with such changes.

Agencies shall be responsible for ensuring that nothing in their lease agreements is inconsistent with this policy. The provisions in agency lease agreements addressing Rental Rates shall be written in such a way as to ensure that agencies may implement any Rental Rate changes mandated by this policy and/or by statute.

VII. AGENCY USE OF RENTAL REVENUE

Under section 16.40(19) of the Wisconsin Statutes agencies that own Housing Rental Units and have program revenue or segregated revenue appropriations for deposit of housing receipts are required to deposit all revenues received from rents into that appropriation or account and to pay all expenses for maintenance of such housing from that account. If an agency does not have a program revenue or segregated revenue appropriation that is specific to deposit of housing receipts the agency must create a separate subaccount within its program revenue or segregated revenue appropriation account for deposit of all revenues received from rents. Where an agency has discretion in determining Adjusted Rental Rates it should take into consideration the cost of maintenance for its units and the cost of periodic appraisals to ensure that deposits into the applicable account or subaccount are sufficient to cover such costs.

VIII. PROCEDURE FOR REVIEW OF RETAINING STATE-OWNED HOUSING UNITS AND DISPOSITION PROCEDURES

Under section 13.48(14)(d) of the Wisconsin Statutes agencies are required to submit to DOA an inventory of all real property under their jurisdiction every two years. Any agency that owns Housing Rental Units is required to include such units in its biennial inventory. Agencies must also specifically identify any underutilized assets in their inventory. As part of this biennial process agencies that own Housing Rental Units shall review their inventory and determine whether any such unit(s) should be identified as underutilized. For purposes of this policy underutilized may include Housing Rental Units, whether occupied or not, for which an agency has determined that continued ownership is no longer in the state's best interest.

As part of the biennial real property inventory process DOA must obtain appraisals of all properties DOA has identified for potential sale, which would include any Housing Rental Units. DOA must then submit an inventory containing the location, description, and fair market value of each property identified for potential sale to the State Building Commission.

If an agency determines that a Housing Rental Unit should be sold or otherwise disposed of it is not required to wait until it submits its biennial real property inventory to DOA. The agency may inform DOA that it has identified the unit for possible disposition.

Once a Housing Rental Unit has been identified for potential sale the procedures for disposition vary depending on which agency will be responsible for carrying it out. Some agencies have independent statutory authority to dispose of real property under their control. With certain limited exceptions DOA has authority under section 16.848 of the Wisconsin Statutes to dispose of real property owned by the state, regardless of which agency has jurisdiction over it. DOA and the agencies should work cooperatively and should consult with their respective legal counsel to determine the proper procedures for disposing of any housing rental unit.

IX. PROCEDURE FOR PERIODIC REVIEW OF SYSTEM OF POLICIES

DOA is statutorily required to periodically review the state's system of state-owned housing administered by agencies for possible changes. In compliance with this responsibility DOA shall conduct a biennial review of this policy. Not later than June 30 of each even numbered year DOA shall send a written communication to all agencies that own and operate Housing Rental Units requesting such agencies to provide DOA with recommended changes, if any, to this policy. Agencies shall be given thirty days to provide responses. If DOA or any agency proposes a change to this policy DOA shall schedule a meeting, inviting any agency that owns or operates Housing Rental Units to participate. Participation in such meetings shall be at each agency's discretion. Once DOA and the agencies have met to discuss proposed changes DOA shall decide whether to implement them. If DOA chooses to make changes to this policy, it must prepare a report recommending such changes and submit it to the Joint Committee on Finance for passive review pursuant to section 16.004(8)(am) of the Wisconsin Statutes.

X. EXCEPTIONS

This system of rental policies does not apply to the following:

- 1) The Governor's Executive Residence;
- 2) Residences occupied by the President of the UW System, the President-Emeritus of the UW – Madison, or Chancellors within the UW System;
- 3) Graduate student housing where eligibility for residency is not determined by employment status;
- 4) Residences within multi-unit properties open to employees and non-employees alike, where employees are not given preference with respect to occupancy or rental rates, and where the agency can demonstrate that the rental rates are market-based.

REPORT ON STATE-OWNED STAFF HOUSING

Prepared by the Department of Administration
in Response to Section 716(5) of Chapter 39,
Laws of 1975, with the Assistance of the State
Agencies Affected

December 12, 1975

REPORT ON STATE-OWNED STAFF HOUSING

This report is submitted in response to the directive contained in section 716(5) of Chapter 39, Laws of 1975, relating to state-owned staff housing. It addresses each of the points contained in the section, including (1) uniform policies for rental rates, (2) criteria for the designation of housing for mandatory and optional occupancy, (3) procedures for the review and updating of approved rental rates for employe housing, (4) procedures related to the phase-out and disposition of unnecessary state-owned employe housing, (5) recommendations regarding required statutory language, and (6) recommendations for implementing the plan. Included with this report are several attachments: (1) a draft policy statement submitted for the committee's approval under section 716(5), (2) an example of the operation of the formula, (3) an analysis of the impact of the formula and, (4) a draft of recommended legislation.

1. UNIFORM POLICIES FOR RENTAL RATES

After extensive analysis of existing rental rates charged by state agencies and possible alternatives and review of possible rate structures with the agencies affected, the Department of Administration recommends the creation of a formula utilizing the following factors:

- a. A gross rental rate equaling 7% of the standardized value of the housing unit as a fair annual rate of return to the

state, based upon an average return of 6.87% to the Investment Board on investments in mortgages and real estate over the past three years.

- b. A ceiling on rental charges to assure that the monthly rental rate shall not exceed 12% of the monthly salary of the employe, based upon average renter costs as a percentage of total budget for nonmetropolitan areas in figures compiled by the Bureau of Labor Statistics.
- c. Modifications to the rental rates would be allowed to recognize special circumstances:
- (1) A reduction may be made from the gross rental rate where space within the dwelling is used primarily to conduct the agency's business. The reduction would be calculated on a proportional basis consistent with IRS guidelines.
 - (2) A proportional reduction may also be made to the gross rental rate charge to allow for space within the dwelling which is excess to the employe's needs and not being used by the employe or the employe's family.
 - (3) A 50% reduction from the adjusted rental rate to recognize the inconvenience to the employe and/or

the benefits to the state as an employer in those cases in which the employe lives in mandatory housing. In most cases the employe-occupants are required to perform a security function or other services for the state beyond normal work hours.

- d. A minimum rental of \$30 per month for a single-family dwelling is recommended because a (7%) rate of return on lower value houses, coupled with the recommended 50% deduction, would produce very low rental rates in a few cases. The \$30 minimum figure is based on the maximum per room per month charge recommended for apartments, duplexes or dormitory rooms with self-contained kitchen and bathroom facilities. The rationale for the recommended minimum is that an employe living in a single family dwelling should pay a rental figure of at least as much as that paid by a resident of an apartment, duplex or dormitory room with such facilities.
- e. Additional charges are recommended in those cases in which occupants receive benefits which are in addition to housing which are not normally provided to a lessee in the private sector, such as utility costs, convenience maintenance services, and food and domestic services. The policy provides that all occupants shall pay the costs of such services as far as such costs can be ascertained. Utility costs are normally paid by

occupants under current policies for state agencies with the major exception being the Department of Health and Social Services, which includes (utility costs in its rental rates. The rental rates for houses under that department, however, are generally higher than those charged by other agencies. Occupants would be charged for convenience maintenance services (e.g., lawn mowing, snow removal, or gardening) where the living unit is not on or adjacent to the institution or the employe's work station. Food and domestic services would not be provided free of charge in those houses covered by this policy.

- f. Rental rates for apartments, duplexes and dormitory rooms provide for a range from \$21-\$30 per room per month for apartments, duplexes or dormitory rooms having a self-contained living area with bath and kitchen facilities, \$11-\$20 per room per month for those facilities which do not have self-contained bathrooms and kitchens, and not to exceed \$10 per room per month for limited sleeping facilities. Such rates may also be modified consistent with the modifications listed for single family housing.
- g. Recommended exclusions to this policy include the Executive Residence, since that residence is provided by statute and it is customary practice in other states to provide an

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executive residence for the Governor. The house occupied by the president-emeritus of the University of Wisconsin-Madison would also be excluded because of the special circumstances under which that house was provided. It is also recommended that the houses occupied by the President of the University of Wisconsin System and the Chancellors within the system be excluded for the following reasons:

- (1) Many of the houses were donated to the University and thus involved no original investment by the state. Some of the donated houses also have deed restrictions or reversion provisions.
- (2) Contractual agreements or offers of employment included a house to be provided by the state.
- (3) Provision of rent-free housing is a customary practice for university presidents and chancellors.

2. CATEGORIES OF OCCUPANCY

The proposed policy defines two categories of state-owned staff housing, optional and mandatory.

- a. Optional Housing. Most housing categorized as optional would be scheduled for either short-term or long-term disposition and would be rented only as an interim

measure to provide a financial return to the state until the most appropriate disposition can be completed. Only those housing units which could not be moved economically, converted to an alternative use or disposed of in some other manner or those units having historical significance or other restrictions would be retained as optional housing. Examples would include houses located on institution grounds which cannot be moved for physical or economic reasons and are not appropriate for conversion to other uses. Such units would be rented based on the formula to provide some financial return on investment to the state.

- b. Mandatory Housing. Mandatory housing must be located on state premises, furnished as a convenience or benefit to the employer, and is considered a condition of employment. This definition is recommended because it is consistent with IRS guidelines and with the needs of the state agencies involved.

3. PROCEDURES FOR REVIEW AND UPDATING OF RENTAL RATES

We recommend that the rental rates established under this policy be made effective as of July 1, 1976, based on values carried by the Bureau of Facilities Management in January of 1976, and the gross monthly salary paid to the occupant in the same month. The

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rate would then remain constant for a two-year period but would be reviewed in March of each even-numbered year for adjustment of rates the following July. The rates would remain constant for a two-year period unless a rate change would be recommended by the agency due to an unanticipated event such as a change of occupant, act of God, etc. The procedure also provides for review by the Department of Administration and 30-day notice to the affected employe.

4. PROCEDURES RELATED TO THE PHASE-OUT OF UNNECESSARY HOUSING

It is recommended that all housing, except housing necessary for mandatory occupancy or optional housing with special restrictions on its disposition, be phased out as soon as possible but no later than the end of the 1979-81 biennium. Mandatory housing, as indicated above, must be on business premises, furnished as a convenience to the employer and must be considered a condition of employment. In addition, those housing units having historical significance and those units whose use and disposition are somehow restricted would be retained by the state. All other houses would be scheduled either for immediate disposition (1975-77 biennium) or for long-term disposition. For these purposes long-term disposition would be a six-year period or the end of the 1979-81 biennium. Each agency would be asked to prepare a written disposition plan similar to that prepared by the Department of Natural Resources, including full written justification for all

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houses classified as mandatory or otherwise scheduled to be retained. The disposition plans would be submitted to the committee for its review, and all requests for disposition or conversion of houses would subsequently be submitted to the Building Commission for its approval in the form of short-term disposition plans.

5. STATUTORY LANGUAGE REQUIRED TO IMPLEMENT THE PLAN

Although the basic plan can be implemented under the language included in Chapter 39, several additional statutory changes would be desirable to fully implement the plan:

- a. A statutory requirement for a biennial review of rental rates and approval by the Joint Committee on Finance.
- b. An amendment to s. 16.086(1)(e) ~~to~~ delete authority of the Director of the Bureau of Personnel over rental rates for housing and create a section to merely place responsibility in the Department of Administration to be assigned at the discretion of the Secretary.
- c. An amendment to section 111.91 to exempt housing from the collective bargaining process for state employees to assure the continuation of a uniform system for rental rates regardless of agency or bargaining unit.

6. RECOMMENDATIONS FOR IMPLEMENTATION

We recommend that the housing plan be implemented as follows:

- a. If the plan meets with the committee's approval, that the Department of Administration be directed to issue the approved policies and procedures to the state agencies involved.
- b. That the committee vote to introduce the recommended legislation (Part 5 above).
- c. That the revised rental rate structure be made effective July 1, 1976, to coincide with wage and salary adjustments effective at that time.
- d. In those cases in which rental rates will be increased, that the Department of Administration be given authority to phase-in the increases over the period from July 1, 1976 to July 1, 1977. This phase-in provision is recommended to cushion the impact of increases in rental rates on individual employees. Reductions in rates would take effect July 1, 1976.
- e. That the Department of Administration be directed to ask affected state agencies to prepare a long-term housing disposition plan to be submitted to the committee within a period of 60 to 90 days.

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f. That, following committee approval of the long-term plan, short-term plans for disposition or conversion of units be submitted to the Building Commission for its review and approval.

Attachment 1

PROPOSED POLICY ON STATE-OWNED STAFF HOUSING

A. Uniform Rental Rate Structure

1. The uniform rental rate structure for state-owned employee-occupied housing for single family units shall be based upon the standardized value of housing units obtained from the operating agency on an annual basis through individual unit assessments, or when that is not possible, through an updating process using an index factor which reflects current market conditions. Such assessments shall be reported to and updated by the Department of Administration, Bureau of Facilities Management, in January of each year.
2. A gross rental rate equaling 7% of the standardized value shall be established as a fair annual rate of return to the state, based upon the experience of the Investment Board on comparable investments.
3. The monthly rental rate charged shall not exceed 12% of the monthly salary of the employee, however, based upon average renter costs as a percent of total budget for non metropolitan areas in figures compiled by the Bureau of Labor Statistics. A minimum rental rate of \$30 per month shall be charged for single family units occupied by state employees.
4. There shall be a uniform rental rate review and adjustment cycle and rates shall be established and revised on a biennial basis in the even-numbered year to recognize changing factors as they affect the rental rate formula.
5. This policy shall not apply to the Executive Residence, the residences occupied by the President of the University System or the president-emeritus of the University of Wisconsin-Madison or to those houses occupied by Chancellors within the University of Wisconsin System.

B. Optional Occupancy

1. The following criteria shall be applied by state agencies for the determination of employe housing designated for optional occupancy:
 - a. Housing units scheduled for disposition shall be classified as optional and shall be rented to an employe or a private party, based on the uniform rental rate structure, until disposed of to provide a financial return to the state.

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- b. Housing units which cannot be moved economically, converted to an alternative use or disposed of in some other manner may be designated as optional housing and rented under the formula to provide a return to the state on its investment.
- c. Housing units which have historical significance or otherwise restricted use and disposition.
- d. Existing housing may be provided on an optional basis if the agency can demonstrate that adequate housing cannot be obtained from the private sector within a reasonable distance from the work site.

C. Mandatory Occupancy

- 1. Mandatory occupancy of state-owned housing may be required if:
 - a. The housing is on the employer's business premises;
 - b. The housing is furnished as a convenience to the employer;
 - c. Housing is considered a condition of employment.
- 2. These criteria are based upon the specific criteria set forth in the Internal Revenue Service Code for the determination of mandatory occupancy for tax purposes to maintain consistency with Federal IRS policies.

D. Modification of Rental Rates

- 1. Where space within the dwelling is being used primarily to conduct the agency's business, an adjustment may be made by the employing agency to the gross rental charge as a result of this condition. Such adjustment shall be calculated based on the number of rooms or square feet used for business purposes as a percentage of the total number of rooms or square feet in the home and applied proportionally as a percentage reduction to the gross rental charge consistent with IRS guidelines. Occasional work in the home such as work done in the den of a home would not qualify for this reduction.
- 2. Where space within the dwelling is excess to the needs of the occupant, an adjustment may be made to the gross rental rate by the employing agency. Such adjustment shall be based on the number of rooms or square feet excess to the occupant's needs in relation to the total number of rooms or square feet in the home and applied proportionally as a percentage reduction to the gross rental charge.

3. Occupants of mandatory housing shall receive a 50% deduction from the adjusted rental rate after any reduction under 1 or 2 above, to recognize the inconvenience to the employe, the services provided by the employe and/or the benefits to the employer.
4. In those instances in which modifications are made under 1, 2 or 3 above, the administering agency shall maintain a record clearly indicating how the modifications were determined, which shall be available for audit purposes.
5. Additional Charges to the Gross Rental Charge

Some occupants (both in mandatory and optional status) receive benefits such as those identified below which are not normally provided to a lessee in the private sector. The actual cost of these benefits shall be assessed the occupant by the agency as far as such costs are ascertainable and include the following:

- a. Utility costs should be paid directly by the occupant whenever possible. However, when direct payment to the provider of utility services is not possible, the agency shall assess additional charges to the occupant which approximate the actual costs to the state as close as is reasonably possible. If a utility expense is attributable to both business use and personal use, such as heat for an entire house, an allocation of costs should be made. Any reasonable method of allocation may be used, although an allocation based on area is usually the most accurate for expenses such as these. Telephone service shall be the responsibility of the occupant except where telephone service is provided primarily for state business.
- b. The cost of convenience maintenance services provided (e.g., lawn mowing, snow removal or gardening) where the living unit is not directly on or adjacent to the institution or the employe's work station.
- c. Food and domestic services provided.

E. Apartments, Duplexes and Dormitories

1. Since the current dollar value for apartments, dormitories and duplexes is indeterminable, a rate scale reflecting the type and physical condition of the living quarters shall be determined and assessed on a per room, per month basis. The agency should determine the "Type" of living unit involved based on the following definitions:

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| <u>Type</u> | <u>Definition</u> | <u>Rate per room per month</u> | |
|-------------|---|--------------------------------|----------------------|
| | | <u>Not less than</u> | <u>Not more than</u> |
| A | Any apartment, dormitory or duplex which has a self-contained living area including bath and kitchen facilities. | \$21 | \$30 |
| B | Those units which do not have a complete self-contained bath and kitchen facility. | \$10 | \$20 |
| C | A limited sleeping facility normally contained within a structure which is primarily used for another purpose (e.g., storage, garage, etc.) | Not to exceed \$10 | |

2. Room as defined for this purpose excludes bathrooms, halls, foyers, galley kitchen, pantry, laundry, storage/utility, alcove, unfinished attic or basement.
3. The agency shall evaluate the condition of the unit for establishment of the specific rental rate for the "Type" of structure considering the following factors:
 - a. General overall condition of the structure.
 - b. Condition of exterior surfaces.
 - c. Condition of interior surfaces.
 - d. Condition of mechanical systems.
 - e. Condition of electrical system.
4. Upon determination of the "Type" and evaluation of the condition of the housing unit the agency shall establish the rental charge within the rate parameters indicated.

F. Uniform Rate Review and Adjustment Procedure

1. Rental rates established under this policy shall be effective July 1, 1976, based on assessed values reported to the Bureau of Facilities Management in January, 1976, and the gross monthly salary paid to the occupant in the same month. Rates shall then remain constant for a two-year period, at which time they shall be reviewed and adjusted based on changes in the factors itemized above unless, upon review, the agency recommends a rate change due to any of the conditions specified in paragraph 2.

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2. Rental rates shall remain constant for this period unless, upon review, the agency determines and recommends to the Department of Administration a rate change due to one or more of the following:
 - a. Change in the status of the occupancy (mandatory to optional or vice versa).
 - b. Where an undesirable and unpreventable alteration of the building's physical condition (normally considered an act of God) has occurred.
 - c. Change in the current assessed dollar value of the house or mobile home based upon a periodic review.
 - d. Change of occupant.
3. In those cases in which a change in rental rate is being proposed, the following procedure shall be followed:
 - a. An agency recommending a change to the established rental rate for a housing unit shall do so at least ~~60~~ 60 days prior to the proposed implementation date, which would normally occur on July 1. This time span is designed to allow the Department of Administration an adequate period to review the proposal.
 - b. All changes to the established rental charge approved by the Department of Administration shall be communicated to the agency recommending the change no later than (40) days prior to the requested implementation date.
 - c. An approved change to the net rental charge shall be communicated by the agency to the occupant affected by the change at least 30 days prior to the implementation date.
 - d. If the recommended change is a result of an abnormal or unanticipated event, the implementation date shall be the first of the month following the date on which the Department of Administration approves the change. Since the event affecting the rental charge was not anticipated, a change in the rental charge shall be handled as soon as possible.

G. Phase-In of Uniform Rental Rates

1. In order to ease the financial impact of the increased rental rates upon individual employees, the following factors shall be included in the phased-in implementation of the rates:

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- a. The revised rates shall be effective as of July 1, 1976 to coincide with wage and salary adjustments effective at that time.
- b. In those cases in which rent is being increased, the Department of Administration may administratively provide for the phase-in of such increases over the period from July 1, 1976 to July 1, 1977.
- c. Assessments for utility costs, convenience maintenance services and food and domestic services shall be effective as of July 1, 1976.

H. Phase-Out of Employee Housing

1. Policy regarding phase-out or conversion of housing:

- a. Recognizing the diminishing need to provide employee housing, it shall be the state's policy that each agency review and justify the retention of each living unit and phase-out all living units which do not meet the guidelines identified above for the continuation of the housing on a mandatory or optional basis.
- b. Housing units not designated to continue as employee housing may be converted, whenever feasible, to other uses which benefit state agency programs (e.g., halfway house, office space, information center, training center, etc.) if such uses are consistent with statutory direction and budgetary authorization and are specifically approved by the Building Commission in the form of short-term disposition plans. If a use other than employee housing is either not needed or not feasible, the subject unit should be, in order of preference:
 - (1) Sold (if no sale restrictions exist);
 - (2) Advertised for rent by the general public; or
 - (3) Demolished.
- c. In the interim, any acquisitions (purchases, gifts, etc.) of property should be studied by each agency for the benefits accompanying such acquisitions. Agencies should not approve purchase of or accept property which cannot be readily or economically converted for mandatory occupancy. Requests for new residential units should also be evaluated by the agency in relation to overall intent of the state to phase-out optional employee housing.

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2. Procedure for phase-out of unnecessary state-owned housing:

- a. Each agency will be asked to carefully evaluate its housing situation and to fully justify those housing units which it plans to retain indefinitely and those which are not necessary and may be phased out on either a short-term or long-term basis.
- b. Those housing units to be retained must meet the criteria for mandatory housing or the special criteria for optional housing to be retained as listed above.
- c. Housing units identified for immediate disposition should be phased out within the current biennium. Sufficient time can be allowed for relocation of the occupant, however, disposition should take place as soon as possible. Each agency should dispose of such units according to its existing practices and within its statutory limitations, except that all requests for disposition or conversion of houses shall be submitted to the Building Commission for its review and approval in the form of comprehensive disposition plans. The following criteria should be used to determine if houses should be scheduled for immediate disposition:
 - (1) House is vacant or will become vacant in the near future.
 - (2) House is in poor condition and repairs are determined to be economically impractical.
 - (3) House is deemed not necessary for program requirements and is considered salable.
- d. Units identified for long-term phase-out may have marginal utility to the state but do not meet the criteria for mandatory housing or optional housing listed above. This categorization allows greater flexibility in the disposition of employe housing to recognize the utility of the house and the possible inconvenience to the employe if he or she would be forced to move within the current biennium. Housing placed in this category should be disposed of when the justification for its continued use no longer exists or when the condition of the house makes it uneconomical to maintain. Phase-out of such housing should be completed by the end of the 1979-81 biennium.

ATTACHMENT 2EXAMPLE OF OPERATION OF FORMULA FOR
SINGLE FAMILY RESIDENCES

- (a) A determination of the current standardized value of an individual unit is made by the Department of Administration, Bureau of Facilities Management.

DNR

22-510

Brule Hatchery

| | |
|--|--------------|
| | <u>Value</u> |
| | \$20,250 |

- (b) Based upon the standardized value, a gross rental rate equaling 7% of the assessed value has been determined to be a fair rate of return to the state. Monthly rental rate at 7% of assessed value:

$$\frac{(.07 \times 20,250)}{12} = \$118.10$$

- (c) A reduction in the rental rate is allowable if the criteria for a mandatory occupancy categorization are met. The rate is reduced by 50% in such cases:

$$\$118.10 \times .50 = \$59.05$$

- (d) The proposed formula includes a "ceiling" on the portion of income to be consumed by housing. 12% has been selected as the ceiling based on figures compiled by the Bureau of Labor Statistics:

$$.12 \times 995 = \$119.40$$

- (e) Since the gross rental rate reduced by 50% for mandatory occupancy is well below the 12% ceiling, the final rental rate equals \$59.05 per month.

ATTACHMENT 3

EXAMPLES OF IMPACT OF FORMULA ON SINGLE-FAMILY RESIDENCES

| | <u>Value</u> | <u>Rental Rate at 7%</u> | <u>12% Ceiling</u> | <u>With Mandatory Deduction</u> | <u>Present Rate</u> | <u>Change</u> |
|-----------------------------|--------------|--------------------------|---------------------|---------------------------------|---------------------|---------------|
| A. Hatchery Residence | \$ 11,100 | \$ 64.75 | --- | \$ 32.38 | \$ 50.94 | - 18.56 |
| B. House at Institution | 18,560 | 108.27 | --- | --- | 143.00 ¹ | - 34.73 |
| C. Hatchery Residence | 20,230 | 118.00 | --- | 59.00 | 60.00 | - 1.00 |
| D. House at Institution | 27,500 | 192.50 | \$151.00 | --- | 143.00 ¹ | + 8.00 |
| E. House at UW Farm | 32,140 | 187.50 | 119.00 | 93.75 | 37.50 | + 56.25 |
| F. House at State Fair Park | 37,920 | 221.20 | --- | 110.60 | 100.00 | + 10.60 |
| G. House at Camp Williams | 44,940 | 262.15 | 247.00 | 131.08 | 75.00 | + 56.08 |
| H. House at DPI Institution | 53,150 | 310.05 | 207.00 | 155.05 | 120.00 | + 35.05 |
| I. House at Institution | 100,295 | 585.05 | 260.00 ² | --- | 156.00 ¹ | +104.00 |

1. Rental rates for Department of Health and Social Services include payment of utilities.

2. Gross rental rates do not reflect possible modifications for business-related space or space excess to needs.

ATTACHMENT 4

PROPOSED LEGISLATION

AN ACT to create 13.101(10), 16.004(8) and 111.91(1)(d) and to amend 16.086(1)(e) of the statutes, relating to policies and procedures for review and approval of rental rates and disposition of state-owned housing.

Section 1. 13.101(10) of the statutes is created to read:

13.101(10) The committee shall receive a report and recommendation from the secretary of administration in March of the even-numbered year relating to rental rates for state-owned housing as required under s. 16.004(8) and, following its review, the committee shall approve a rental rate structure to govern rental rates for state-owned housing for the subsequent two-year period beginning July 1.

Note: This section would establish a procedure for the Joint Committee on Finance to review and approve rental rates for state-owned housing every two years in the even-numbered year.

Section 2. 16.004(8) of the statutes is created to read:

16.004(8) Review of rentals for state-owned housing. The secretary shall establish and maintain a system relating to the rentals charged for state-owned housing and shall review the system for possible changes every two years and shall submit a recommendation to the joint committee on finance in March of each even-numbered year. Such system shall also include a procedure for review of the need to retain state-owned housing

-2-

units and possible disposition of such units. Recommendations regarding the disposition of any housing units shall be submitted to the building commission.

Note: This section would create a requirement for the Secretary of Administration to conduct a biennial review of rates for state-owned housing and to submit a recommendation to the Joint Committee on Finance in March of each even-numbered year. The Secretary would also be directed to review the continuing need for such houses and to submit any recommendations for disposition to the Building Commission. These provisions are intended to assure that rental rates and the need to retain state-owned houses are reviewed periodically.

Section 3. 16.086(1)(e) of the statutes is amended to read:

16.086(1)(e) Maintenance provisions. The compensation plan shall also include the approved schedule of allowable charges for the deductions from the pay of employees who are furnished meals, wholesale provisions, ~~rooms, apartments and houses~~ and other maintenance provisions. Where allowances such as laundry, or meals ~~or lodging~~ are provided any classified employe or an employe and his family, and such allowance in kind is provided as a part of the compensation, the appointing authority or department head in addition shall pay in cash the value of the food during the vacation period or noncumulative leave of absence, if not so utilized, to such an employe.

Note: This amendment deletes the requirement that the compensation plan include allowable charges for rooms, apartments and houses and more generally deletes housing as a responsibility of the Director of Personnel. Together with the proposed section 16.004(8), this amendment would place the responsibility for review of rental rates under the Secretary of Administration to be assigned within the department along with other real estate functions consistent with the recommendations of the Currie Commission.

-3-

Section 4. 111.91(1)(d) of the statutes is created to read:

111.91(1)(d) The employer shall not be required to bargain on matters related to employe occupancy of houses or other lodging provided by the state.

Note: This section would exempt any matters related to employe occupancy of houses or other lodging provided by the state from the collective bargaining process to allow for the implementation of state-wide formulas for lodging regardless of agency or bargaining unit of the employe.

(End)

**Report 19-26
December 2019**

State-Owned Residential Properties

STATE OF WISCONSIN



Legislative Audit Bureau ■

**Report 19-26
December 2019**

State-Owned Residential Properties

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December 2019

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STATE OF WISCONSIN | Legislative Audit Bureau

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Joe Chrisman
State Auditor

December 6, 2019

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles and Representative Kerkman:

In response to a report to our Fraud, Waste, and Mismanagement Hotline, we initiated an audit of certain state-owned residential properties managed by state agencies and leased to state employees. Statutes require the Department of Administration (DOA) to administer those properties by developing policies, conducting appraisals, and determining rental payment amounts to ensure rental payments state agencies charge state employees are based on the fair value of the properties.


As of December 2018, the Department of Natural Resources (DNR) managed 32 state-owned residential properties occupied by 32 employees, and the University of Wisconsin (UW) System managed a total of 114 properties occupied by 171 employees. UW institutions required employees to reside in 15 of the properties in December 2018, whereas other UW employees opted to reside in the properties.

We found DOA has not formally revised policies since 1975 and, although DOA has been statutorily required to conduct appraisals of state-owned residential properties every 10 years since 1991, DOA has not conducted appraisals since 1995. Although DOA calculated rental payment adjustments that averaged 2.3 percent annually between 1998 and 2018, DNR and UW System did not implement all rental payment adjustments. We also found DNR demonstrated compliance with Internal Revenue Service guidelines in only 2 of the 32 lease agreements in effect in December 2018, and UW institutions demonstrated compliance in only 3 of 16 lease agreements.

We recommend DOA comply with statutory requirements, reassess practices surrounding state-owned residential properties, and increase its monitoring and oversight of these properties. We also recommend DNR and UW System comply with DOA policies and improve the management of lease agreements each executes with state employees.

We appreciate the courtesy and cooperation extended to us by DOA, DNR, and UW System. A response from each agency follows the appendices.

Respectfully submitted,


Joe Chrisman
State Auditor

JC/SH/ss

Introduction ■

Some employees may be required to reside in state-owned properties as a condition of employment, while other employees may opt to reside in them.

In response to a report to our Fraud, Waste, and Mismanagement Hotline, we initiated an audit of certain state-owned residential properties currently managed by state agencies and leased to state employees. Certain employees may be required to reside in the properties as a condition of employment and may receive a discount on rental payments. In other instances, employees may opt to reside in them.

Under provisions of ch. 16, Wis. Stats., the Department of Administration (DOA) is required to administer state-owned residential properties that are managed by state agencies. These requirements, which were originally established during the 1975 legislative session, were revised through 1991. Policies DOA developed in 1975 emphasized eliminating or reducing the number of state-owned residential properties in which state employees opt to reside.

According to DOA records, there were 92 state-owned residential properties in 1996 managed by six state agencies, including the:

- Department of Corrections;
- Department of Health Services;
- Department of Military Affairs;
- Department of Natural Resources (DNR);

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- Department of Veterans Affairs; and
- University of Wisconsin (UW) System.

Over time, many state-owned residential properties were either razed, sold, or the agencies found other uses for the facilities. However, we found that only DNR and certain UW System institutions continued to manage the properties that were occupied by state employees. As a result, we limited our audit to DNR and UW System.

DNR Residential Properties

As of December 2018, 32 state-owned residential properties were occupied by DNR employees.

According to available records, DNR managed 55 state-owned residential properties available to lease to state employees as of December 2018. We found that 32 of the 55 properties were occupied by DNR employees as a primary residence and the remaining 23 properties were vacant as of December 2018. As shown in Table 1, the 32 occupied properties were located largely in state parks, fish hatcheries, and state forests.

Table 1

State-Owned Residential Properties Managed by DNR¹ As of December 2018

| Property Type | Number of Properties |
|---------------------------|----------------------|
| State Park | 14 |
| Fish Hatchery | 8 |
| State Forest ² | 5 |
| Other | 5 |
| Total | 32 |

¹ Includes properties occupied by DNR employees as a primary residence.

² Includes properties managed by DNR's Fish, Wildlife, and Parks Division. In December 2018, no occupied properties were within DNR's northern state forests, which are managed by the Forestry Division.

DNR also managed state-owned residential properties that are occupied by employees on a temporary, month-to-month basis but not as primary residences. The majority of these properties are dormitory or family-style residential options for limited-term

employees in positions DNR identified as primarily being active only during the summer season. According to DNR records, 36 employees were in month-to-month lease agreements as of July 2019. Because of the seasonal and temporary nature of these arrangements, these properties were not included in the scope of this audit.

UW System Residential Properties

**As of December 2018,
UW System managed
114 state-owned
residential properties
that were occupied
by UW employees.**

According to available records, UW System managed 114 state-owned residential properties that were occupied by UW employees as of December 2018. As shown in Table 2, the largest number of properties were apartment buildings in which employees may opt to reside. UW-Madison had 96 apartment buildings in which faculty and academic staff resided. UW System Administration, UW-Platteville, UW-River Falls, and UW-Stevens Point also managed properties in which employees resided as a primary residence.

Table 2

State-Owned Residential Properties Managed by UW System¹ As of December 2018

| Property Type | UW-Madison | Other UW Institutions | Total |
|---------------------|------------|-----------------------|------------|
| Apartment Buildings | 96 | 2 | 98 |
| Research Stations | 12 | 4 | 16 |
| Total | 108 | 6 | 114 |

¹ Includes properties occupied by employees in Wisconsin Retirement System-eligible positions as a primary residence. Excludes properties that predominately housed students, state-owned chancellor residences at five UW institutions, and the UW System President's residence.

In addition to these properties, the State owns chancellor residences at five UW institutions, the UW System President's residence, and properties to house students, including undergraduate student residential halls and other housing options for graduate students, some of whom also are employed by UW institutions. These properties were not included in the scope of this audit.

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IRS Guidelines Applicable to Employer-Provided Housing

IRS guidelines specify the criteria that must be met to avoid treating housing provided by the employer or rental payment discounts as taxable income for an employee.

Internal Revenue Service (IRS) guidelines prohibit employers from providing housing or discounts on rental payments as a means to increase employee wages without increasing the employee's taxable income. Therefore, IRS guidelines specify that all of the following criteria must be met to avoid treating housing provided by the employer or rental payment discounts as taxable income for an employee, including:

- the residence is located on the employer's business premises;
- the employee resides in the property for the convenience of the employer; and
- the employee is required to reside in the property as a condition of employment because residing within the employer's property is necessary for the employee to properly conduct job responsibilities, and the terms are agreed to at the beginning of employment.

State employees who reside in state-owned properties and meet these conditions are not taxed on any discounted rental payment amount. Conversely, state employees who opt to reside in the properties are required to report as taxable income any difference between their actual rental payment and the fair value of rent, as determined through an appraisal, when the actual rental payment is lower than the fair value. Although IRS guidelines include some additional exceptions applicable to employees of educational institutions who opt to reside in state-owned properties, these exceptions are permitted when rental payments are based on annual appraisals of the property.

■ ■ ■ ■

Requirements and Policies for Residential Properties ■

Wisconsin Statutes require DOA to administer state-owned residential properties. However, we found DOA did not comply with all statutory requirements. Although DOA is statutorily required to conduct an appraisal of these properties every 10 years, it has not conducted any appraisals since 1995. DOA also has not actively provided monitoring or oversight of state agency compliance with its existing policies for these properties. For example, DOA did not track properties occupied by state employees, retain copies of active lease agreements, or assess whether agencies implemented required rental payment adjustments. We recommend that DOA comply with statutory requirements and take steps to actively monitor and oversee state-owned residential properties.

Statutory Requirements

Under s. 16.004 (8), Wis. Stats., DOA is required to:

- maintain a system of rental policies for state-owned residential properties, periodically review these policies, and submit any proposed changes to these policies to the Joint Committee on Finance;
- conduct appraisals of the fair value of state-owned residential properties following each federal decennial census;

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- establish periodic rental payment adjustments if no appraisal was conducted in the previous 24 months; and
- develop a procedure for reviewing the need to retain state-owned residential properties and submit recommendations for disposing of properties to the State of Wisconsin Building Commission.

DOA has not formally revised its policies for state-owned residential properties since 1975.

We found DOA has not formally revised its policies for state-owned residential properties since 1975. These policies addressed establishing and updating rental payment amounts and specified provisions state agencies should include in executing lease agreements with state employees, such as establishing the responsibility for payment of utility costs and performing maintenance of the properties.

Residential Property Appraisals

DOA did not comply with statutes because it did not conduct appraisals of state-owned residential properties following either the 2000 census or the 2010 census.

Under s. 16.004 (8) (e) 2., Wis. Stats., DOA is required to conduct appraisals of state-owned residential properties following each federal census. After this provision was enacted in 1991, DOA conducted appraisals of the properties in 1995. However, DOA did not conduct appraisals following either the 2000 census or the 2010 census. Because rental payment amounts are determined from appraisals, DOA cannot be assured the rental payment amounts reflect the current fair value of the properties. DOA staff indicated that several reorganizations among its divisions subsequent to 2002 resulted in the responsibilities for administering the properties not being reassigned to any specific division.

Determining Rental Payment Amounts

State employee rental payment amounts are determined using three factors. First, as required by statutes, a base rental amount is determined through an appraisal. Second, statutes require DOA to determine periodic rental payment adjustments between appraisals. Third, under DOA policies, certain discounts may be applied to the rental payment amount.

Between 1998 and 2018, DOA established rental payment adjustments that increased rental payment amounts an average of 2.3 percent annually.

We found that DOA established base rental payment amounts using the 1995 appraised value for each state-owned residential property. Because no appraisals were conducted after 1995, DOA biennially determined rental payment adjustments between 1998 through 2018 that were implemented as incremental, annual increases during each biennium. These rental payment adjustments, which were based on the Consumer Price Index, increased rental payment amounts an average of 2.3 percent annually.

DOA communicated these adjustments to state agencies, including UW System. The state agencies were then responsible for communicating the required rental payment adjustments to their employees as necessary and implementing new rental payment amounts based on these adjustments. However, DOA did not monitor whether state agencies implemented the rental payment adjustments in lease agreements the agencies executed with state employees.

DOA policies allow state agencies to provide a 50.0 percent rental payment discount to employees who meet the requirements of IRS guidelines.

DOA policies permit state agencies to provide rental payment discounts in certain circumstances. For example, state agencies may provide an employee a 50.0 percent rental payment discount if the employee meets IRS guidelines for excluding the discount from the employee's taxable income, including that the agency required that the employee reside in a state-owned property as a condition of employment. Each state agency determines whether residing in the property is a requirement of an employee's position. In addition, DOA policies require that monthly rental payment amounts cannot exceed 12.0 percent of the employee's monthly wages. Finally, if an employee opts to reside in the property, agencies may provide a 10.0 percent rental payment discount.

Improving Administration of Residential Properties

DOA did not track all state-owned residential properties for which it is statutorily responsible and did not monitor state agency compliance with its policies.

Although DOA is statutorily required to administer state-owned residential properties, it did not perform overall monitoring to ensure agencies complied with DOA policies. For example, DOA did not track all properties subject to its oversight. If DOA had done so, it may have identified that state agencies were not following its policies.

Although DOA's communications on biennial rental payment adjustments requested that state agencies provide it with the adjusted rental payment amounts, DOA did not attempt to obtain this information when agencies failed to comply with its requests. DOA should ensure that state agencies provide confirmation that the adjustments are implemented. If DOA had done so, it would have been able to identify how many properties were occupied and

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determine instances in which state agencies did not charge an appropriate rental payment.

DOA should work with agencies to reassess whether to retain state-owned residential properties, including recommending to the State of Wisconsin Building Commission whether any of the properties should be sold, razed, or used for other purposes. Although a state agency is typically responsible for determining whether to retain property, these decisions do not appear to have involved DOA in recent years.

Conducting regular appraisals helps to ensure that rental payment amounts reflect fair value of state-owned residential properties.

Statutes require that the cost of appraisals should be funded from the appropriations in which rental payment receipts are deposited. Conducting regular appraisals helps to ensure that rental payment amounts reflect fair value of state-owned residential properties. Although the cost of conducting appraisals may outweigh the potential increased rental payment amounts state agencies receive from employees who reside in the properties, appraisals will assist DOA in identifying whether biennial rental payment adjustments are effective in approximating fair value.

Recommendation

We recommend the Department of Administration take steps to improve its administration of state-owned residential properties, including by:

- *complying with statutes by periodically reviewing and formally revising applicable policies;*
- *tracking state-owned residential properties subject to its oversight and monitoring the rental payment amounts state agencies charge employees;*
- *complying with statutes by conducting appraisals of all state-owned residential properties;*
- *complying with statutes by working with state agencies to assess whether residential properties should be retained and making recommendations to the State of Wisconsin Building Commission; and*
- *reporting to the Joint Legislative Audit Committee by April 10, 2020, on the status of its efforts to implement these recommendations.*

Issue for Legislative Consideration

As noted, DOA must provide to the Joint Committee on Finance any proposed changes to its policies for state-owned residential properties. To further increase its oversight of DOA's administration of state-owned residential properties, the Legislature may wish to consider creating a statutory requirement for DOA to report biennially a list of the properties and the current rental payment amount for each property.

■ ■ ■ ■

Department of Natural Resources Residential Properties ■

The state-owned residential properties managed by DNR were largely obtained as part of land acquisitions and retained for residential use. In executing lease agreements, we found DNR incorrectly calculated rental payment amounts for its properties. We also found that not all of the rental payment discounts DNR provided to state employees in executed lease agreements complied with DOA policies and IRS guidelines. We recommend that DNR comply with DOA policies, better track the properties it manages, and improve communication among DNR staff involved in these processes. We also recommend DNR reassess whether employees should be required to reside in the properties.

Current Uses of Residential Properties

Properties managed by DNR were primarily located within state parks, fish hatcheries, and state forests.

As noted, DNR managed 55 state-owned residential properties available to lease to state employees as of December 2018. We found that 32 of the 55 properties were occupied by DNR employees as a primary residence, and the remaining 23 properties were vacant. These properties were primarily located within state parks, fish hatcheries, and state forests and were largely occupied by DNR park rangers, fishery technicians, property supervisors, and facilities repair workers. A list of the locations of the 32 properties leased to DNR employees as of December 2018 is Appendix 1.

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DNR indicated that the State benefits from employees occupying state-owned residential properties.

According to DNR staff, the state-owned residential properties occupied by state employees benefit the State because they attract potential employees, provide housing in rural areas where alternative housing options may be limited, and allow employees to remain on-site outside of normal working hours. DNR described most of these properties as modest single-family homes that are generally located in rural areas. For example, one residential property located in a state park is a ranch-style, 1,700 square-foot home that had an assessed value of \$106,000 in 2009. Properties are maintained in good condition, but DNR indicated that some of them are up to 100 years old. Although we did not review the complete leasing history for each property, we found 17 of the 32 DNR employees in a lease agreement during December 2018 had lived in a state-owned residential property since at least 2016, including one employee who had resided in a property since 1993.

Employee Lease Agreements

Based on statutory requirements, DOA policies, and practices for effective management of state-owned residential properties, we expected DNR would have:

- implemented policies and procedures sufficient to ensure compliance with DOA policies;
- executed written lease agreements outlining significant terms, including payment of utilities, and retained the agreements for the duration of the period in which the employee resided in the property;
- followed DOA policies in determining rental payment amounts and adjusted rental payment amounts in a timely manner as required by DOA, including communicating rental payment amounts in writing to the employee and administrative staff as necessary;
- collected all rental payment amounts; and
- demonstrated compliance with DOA policies and IRS guidelines when providing rental payment discounts, including by documenting a requirement to reside in a state-owned property as a condition of employment and ensuring this residency was necessary for the employee to properly conduct job responsibilities.

Administrative Policies and Procedures

DNR lacked detailed procedures, including who was responsible for administrative responsibilities or how it communicated its policies to all necessary staff.

We found DNR had a policy for employees residing in state-owned properties that was similar to provisions of DOA policies, including specifying when a 50.0 percent discount may be applied to rental payment amounts. The DNR policy also referenced IRS guidelines, including that the employee be required to reside in the property as a condition of employment. However, DNR lacked detailed procedures about how the policy should be administered, who was responsible for these procedures, how it communicated its policy to all necessary staff, or how it monitored for continual compliance with both its policy and DOA's policies.

Executing Lease Agreements

DNR executed lease agreements in September 2018 for all 32 DNR properties that were occupied in December 2018.

We requested lease agreements between DNR and state employees and found that lease agreements had been signed in September 2018 for each of the 32 DNR properties that were occupied in December 2018. We found one DNR employee signed all lease agreements and the terms of these lease agreements complied with existing DOA policies, including requiring the employee to pay for utilities and conduct routine maintenance of the property.

Determining Rental Payment Amounts

We reviewed DNR's determination of rental payment amounts for its lease agreements in effect with state employees as of December 2018. We considered whether DNR consistently and accurately considered the base rental amount determined through a DOA appraisal, adjusted the rental payment amounts biennially as required by DOA, and correctly applied discounts, if applicable.

In the absence of periodic appraisals by DOA, DNR reassessed the fair value of some properties as they were vacated and established a new base rental payment amount.

For the majority of the state-owned residential properties, it appears DNR continued to use the base rental payment amounts DOA established through its 1995 appraisals. However, in the absence of periodic appraisals by DOA, DNR reassessed the fair value of some properties as they were vacated and before a new lease agreement was executed with another state employee. DNR then established a new base rental payment amount, applied a 50.0 percent discount, and continued to apply biennial rental payment adjustments as determined and communicated by DOA.

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No DOA appraisals were conducted for 13 properties DNR acquired since DOA last conducted appraisals in 1995.

According to DNR records, it managed 13 state-owned residential properties that were not appraised by DOA because DNR acquired them after the 1995 appraisals were conducted. In December 2018, five of the properties were occupied and eight were vacant. According to DNR staff, the properties were largely acquired through land bequests or land acquisitions in which a residential property was located. Because no appraisals had been conducted by DOA since 1995, DNR had taken steps similar to those previously described to assess the fair value of the properties.

DNR will have undercharged an estimated \$38,900 for rental payments during 2019.

Although DOA consistently determined rental payment adjustments, we found DNR did not implement 10 of 21 adjustments established by DOA between 1998 and 2018. We cannot determine from available information what the rental payment amounts would have been had DOA completed an appraisal in recent years. However, DNR was required to accurately implement all rental payment adjustments determined by DOA. We found DNR did not charge employees the full rental payment amounts because it did not accurately implement all adjustments. Based on rental payment amounts charged in December 2018, DNR will have undercharged an estimated \$38,900 for rental payments during 2019.

DNR did not implement 3 of the 11 rental payment adjustments until more than one year after the required effective date.

We also found 6 of the 11 rental payment adjustments implemented by DNR since 1998 were not implemented in a timely manner, including 3 adjustments that were not implemented until more than one year after the required effective date. For example, in May 2016 DOA communicated a 1.74 percent adjustment to rental payment amounts effective in August 2016 and July 2017. However, DNR did not enter into new lease agreements reflecting these adjustments until September 2018. Although DNR eventually made corrections to employee rental payment amounts when it identified the omission, the amounts that employees paid between 2016 and 2018 were less than they should have paid. We also found rental payments for one DNR employee had been unchanged since at least 2010. DNR was unable to explain why this employee's rental payment had not been adjusted.

Collecting Rental Payments

From 2016 through 2018, DNR collected approximately \$110,000 annually in rental payments from state employees.

DNR employees who reside in state-owned properties as primary residences make rental payments through biweekly payroll deductions. In December 2018, payroll rental deductions for the 32 DNR employees totaled \$10,070, with an average monthly rental payment of \$347. From 2016 through 2018, DNR collected approximately \$110,000 annually in rental payments from state employees.

From 2016 through 2018, DNR did not collect approximately \$1,000 in rental payments that we expected should have been collected. We found other instances in which DNR failed to update the payroll system to terminate a rent deduction in a timely manner after an employee vacated a state-owned residential property. In 22 instances, totaling \$6,600, an employee received a refund related to rent. We also found that the majority of these refunds were processed by DNR to adjust for rental deductions that inadvertently continued after the employee no longer resided in the property or to correct for an overpayment by the employee as a result of timing differences between the termination of the employee's lease agreement and the biweekly payroll. We also found that, from September 2018 through June 2019, DNR collected the stated amount of rental payments included in lease agreements it executed in September 2018.

Demonstrating Compliance with IRS Guidelines

DNR demonstrated compliance with IRS guidelines in only 2 of 32 lease agreements in effect in December 2018.

We found all of the 32 lease agreements in effect in December 2018 included a 50.0 percent rental payment discount. In order to not treat the discount amount as taxable income for the employee, DNR was required to comply with IRS guidelines. Therefore, DNR should have documented in appointment letters that the employee was both required to reside in a state-owned property as a condition of employment and that residing in the property was necessary for the employee to properly conduct job responsibilities. However, we found that DNR demonstrated compliance with IRS guidelines in only 2 of the 32 lease agreements. An additional 5 lease agreements met one, but not both, of the requirements, and 25 lease agreements met neither requirement. During our audit, DNR reassessed the 32 lease agreements and confirmed that most employees who occupied its state-owned residential properties had opted to do so.

For three of the five lease agreements that met one but not both requirements, DNR appointment letters stated the employee was required to reside in a state-owned property as a condition of employment, but the employee did not need to reside in the property to properly conduct job responsibilities. For example, a 2013 appointment letter stated that a state park property supervisor was required to reside in the property. However, although the State may have benefited from the employee residing on-site, the employee's job responsibilities did not require residence in close proximity of the state park. Further, DNR staff indicated that if it conducted a recruitment for this employee's position in the future, it would consider candidates that did not agree to reside in the property.

For two of the five lease agreements that met one, but not both requirements, DNR did identify a need for the employee to reside

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in the state-owned property to conduct job responsibilities. However, DNR did not consistently state the requirement in its appointment letters. For example, DNR justified the need for four fish hatchery employees to reside in the properties in order for them to monitor fish propagation operations and to respond quickly to conditions that could adversely affect production. However, only two of the four appointment letters stated that residing in the property was a condition of employment.

If DNR did not meet both requirements, the employee should not have received a 50.0 percent rental payment discount under DOA and DNR policies. Further, IRS guidelines require that the State determine whether the 50.0 percent discount was appropriately considered when preparing annual tax information for employees, such as in instances in which discounts may have been taxable income.

The 50.0 percent rental payment discount was not included as taxable income within 2018 tax information the State prepared for any of the 32 DNR employees.

We found that the 50.0 percent rental payment discount was not included as taxable income within 2018 tax information the state prepared for any of the 32 DNR employees who resided in state-owned properties in December 2018. Because DNR considered all employee lease agreements as having met both requirements of IRS guidelines, it is unlikely that DNR would have considered the 50.0 percent rental payment discount as taxable income.

We did not review DNR's complete leasing history for each property. However, based on our findings, DNR should not have provided a 50.0 percent discount to all employees and, therefore, should consider tax implications for these employees.

Improving Management of Residential Properties

Although DNR had lease agreements readily available for all 32 employees residing in a state-owned property in December 2018, and generally collected the majority of rental payments in a timely manner by using payroll deductions, it did not fully comply with requirements and expectations for management of state-owned residential properties.

DNR lacked timely and accurate communication among those who worked directly with employees residing in state-owned properties and employees who executed lease agreements.

We found DNR's method of tracking state-owned residential properties it managed did not provide sufficient information to ensure that all property information was accurate or that rental payment amounts were accurately determined. There was also insufficient communication or understanding among DNR staff who maintained properties and hired employees to reside in them and those DNR staff who executed lease agreements and determined rental payment amounts. For example, errors in determining rental payment amounts

in some instances resulted from not communicating changes or adjusting payroll rent deductions in a timely manner.

We also found DNR incorrectly executed lease agreements as if all employees were required to reside in the state-owned residential properties as a condition of employment since 1995. However, the need for employees to reside in the properties changed over time. For example, the DNR staff member currently responsible for an employee hired in 2010 and for the property in which this employee resided was not aware that the employee's appointment letter stated the employee was required to reside in the property. This staff member did not consider the employee as one who is required to reside on-site to properly conduct job responsibilities. This staff member indicated to us that if the current employee terminated employment, the residence would be offered to another employee who could opt to reside in the property.

Finally, we found DNR did not develop comprehensive written procedures for managing state-owned residential properties. Had DNR done so, it may have more accurately and consistently applied all DOA policies in lease agreements it executed with state employees who resided in state-owned properties. When DOA revises its policies, DNR should be proactive in ensuring changes to DNR's written procedures are implemented accurately and in a timely manner.

DNR should comply with DOA policies in executing lease agreements with state employees. To improve its management of state-owned residential properties, DNR should also implement all required rental payment adjustments in a timely manner; better track its properties; improve communication among DNR staff; collect all rental payment amounts; execute new lease agreements for those in which it incorrectly provided rental payment discounts; consider tax implications for current and prior lease agreements that did not comply with DOA policies; reassess whether it is necessary for employees to reside in properties it manages; and create comprehensive written procedures that align with DOA policies.

Recommendation

We recommend that the Department of Natural Resources take steps to improve its management of state-owned residential properties, including by:

- *complying with Department of Administration policies in executing lease agreements with employees residing in state-owned residential properties;*

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- *accurately implementing all rental payment adjustments required by the Department of Administration in a timely manner;*
- *developing a formal mechanism to track information for its state-owned residential properties;*
- *improving communication among staff when employees terminate employment or discontinue residing in a state-owned property in a timely manner to ensure the rental payment does not continue to be charged;*
- *proactively monitoring uncollected rental payments and following up in a timely manner with employees to receive these payments;*
- *executing new lease agreements to correct rental payment amounts that incorrectly included a 50.0 percent rental payment discount;*
- *considering the tax implications of rental payment discounts it incorrectly provided in current and prior lease agreements;*
- *reassessing its residential properties to determine whether it is necessary for an employee to reside in the property to properly conduct job responsibilities;*
- *formally documenting its procedures for managing state-owned residential properties and communicating them to all appropriate staff; and*
- *reporting by April 10, 2020, to the Joint Legislative Audit Committee on the status of its efforts to implement these recommendations.*

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Current Uses of Residential Properties
Employee Lease Agreements
Improving Management of Residential Properties
Employees Opting to Reside in State-Owned Properties

University of Wisconsin System Residential Properties ■

UW System's state-owned residential properties include apartment buildings and research stations. In executing lease agreements, we found UW institutions did not set rental payment amounts in ways that complied with DOA policies and UW-Madison did not have lease agreements for all employees who resided in a state-owned property. We also found not all rental payment discounts UW institutions provided to employees complied with DOA policies and IRS guidelines. We recommend that UW System Administration establish system-wide policies to improve accuracy and consistency in executing lease agreements with employees, comply with DOA policies in determining rental payment amounts, and improve documentation when requiring employees to reside in such properties. We further recommend that UW System Administration work with DOA to develop policies that specifically address lease agreements for employees who opt to reside in state-owned apartment buildings.

Current Uses of Residential Properties

UW System had 15 state-owned properties in which it required employees to reside as of December 2018.

As shown in Table 3, UW System's residential properties include apartments and research stations, which are largely agricultural in nature. UW institutions required employees to reside in 15 of the 114 state-owned properties as of December 2018. A list of the locations of the 15 properties leased to UW employees as of December 2018 is Appendix 2.

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Table 3

UW System State-Owned Residential Properties¹

As of December 31, 2018

| Property Type | UW Institution | Employee Required to Reside | Employee Opted to Reside |
|----------------------------|----------------|-----------------------------|--------------------------|
| Apartment Buildings | | | |
| | Madison | – | 96 |
| | System | 1 | 1 |
| | Subtotal | 1 | 97 |
| Research Stations | | | |
| | Madison | 12 | – |
| | Platteville | 1 | – |
| | River Falls | – | 2 |
| | Stevens Point | 1 | – |
| | Subtotal | 14 | 2 |
| Total | | 15 | 99 |

¹ Includes those properties occupied by employees in Wisconsin Retirement System-eligible positions and who resided in the properties as a primary residence. Excludes the properties designed for chancellors and the UW System President and those that predominately housed students.

According to UW System Administration, the state-owned residential properties occupied by UW employees benefit the State because they serve to attract potential employees, provide housing close to campuses, or allow employees to remain on-site outside of normal working hours to complete job responsibilities. According to UW-Madison staff, apartments are comparable to others within the surrounding area and the homes located at research stations, though well maintained, are up to 100 years old.

UW-Madison manages most of the apartments, which are largely provided to employees who opt to reside in them. A total of four UW institutions maintain research stations that included 16 state-owned residential properties, including UW-Madison, UW-Platteville, UW-River Falls, and UW-Stevens Point. Although UW-River Falls did not require employees to reside at a research station, UW-Madison, UW-Platteville, and UW-Stevens Point did so to manage the farms and wildlife areas located within the stations. Finally, two residential properties were located on the UW System President's residence grounds, including one in which UW System Administration required an employee to reside and one in which no employee was required to reside.

As of December 2018, 171 UW System employees resided in a state-owned property, of which UW institutions required 16 employees to reside in the properties.

As shown in Table 4, we identified 171 UW System employees who resided in a state-owned property as of December 2018. We found 124 of the 171 employees were academic staff who were not required to reside in the apartment buildings. The number of employees exceeds the number of properties because buildings had multiple apartment units and several employees may reside within an apartment. In total, there were 16 employees required to reside in 15 properties as of December 2018 because two employees resided within one of the properties.

Table 4

UW Employees Residing in State-Owned Properties

As of December 31, 2018

| Employment Category | Employee Required to Reside | Employee Opted to Reside | Total |
|----------------------|-----------------------------|--------------------------|------------|
| Academic Staff | 11 | 124 | 135 |
| Faculty | 1 | 19 | 20 |
| Administrative Staff | 4 | 12 | 16 |
| Total | 16 | 155 | 171 |

Employee Lease Agreements

Based on statutory requirements, DOA policies, and practices for effective management of state-owned residential properties, we expected UW System would have:

- implemented policies and procedures sufficient to comply with DOA policies;
- executed written lease agreements outlining significant terms, including payment of utilities, and retained the agreements for the duration of the period in which the employee resided in the property;
- followed DOA policies in determining rental payment amounts and adjusted rental payment amounts in a timely manner as required by DOA, including communicating rental payment amounts in writing to the employee and administrative staff as necessary;

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- collected all rental payment amounts; and
- demonstrated compliance with DOA policies and IRS guidelines when providing rental payment discounts, including by documenting a requirement to reside in a state-owned property as a condition of employment and ensuring this residency was necessary for the employee to properly conduct job responsibilities.

As of December 2018, 12 of the 15 state-owned residential properties were occupied by UW-Madison employees who were required to do so.

We focused our audit on the 16 employees that UW institutions required to reside in 15 state-owned properties. We found that 12 of these properties were occupied as of December 2018 by UW-Madison employees.

Administrative Policies and Procedures

We found that staff in UW System Administration were aware of DOA's policies and had some central information on state-owned residential properties managed by UW institutions, but all management of lease agreements with employees occurred at the institution level. No system-wide policies existed for managing the properties or executing lease agreements with employees who resided in them.

Executing Lease Agreements

We requested lease agreements for all 16 UW employees required to reside in a state-owned property in December 2018. Based on available documents, we found that some employees had been residing within state-owned residential properties for many years, including one employee who had been residing at a research station since 1998.

For 6 of 12 employees it required to reside in properties located at agriculture research stations, UW-Madison was unable to provide lease agreements in effect in December 2018.

UW-Madison provided signed lease agreements for 6 of 12 employees residing at agriculture research stations. However, it was unable to provide the remaining 6 lease agreements in effect in December 2018, and indicated that each of these leases was signed when the employee was originally hired and could not be located. In response to our request, UW-Madison executed new lease agreements in four instances. Because lease agreements help minimize the legal liability of a lessor by clearly defining the responsibilities of both parties and indicating the process for amending or terminating the agreement, it is important that all UW institutions execute and maintain lease agreements with employees residing in state-owned properties.

UW-Madison should formally communicate a rental payment amount in writing.

For those lease agreements we obtained from UW-Madison, we also found that rental payment amounts were not included in the lease agreements or recorded in any other documents. Instead, it appears rental payment amounts were verbally communicated to the employees. Although new leases are not executed each year, UW-Madison should formally communicate a rental payment amount in writing, including documenting when that amount was revised and communicated to the employee.

Determining Rental Payment Amounts

We reviewed how UW institutions determined rental payment amounts for their lease agreements in effect with state employees as of December 2018. We reviewed whether UW institutions consistently and accurately considered the base rental amount determined through a DOA appraisal, adjusted the rental payment amounts biennially as required by DOA, and correctly applied discounts, if applicable.

We identified that 12 of 15 state-owned residential properties in which employees were required to reside in December 2018 were last appraised by DOA in 1995. Rental payments for the remaining three properties were not assessed because two properties were acquired subsequent to 1995 and one property, although state-owned in 1995, was not appraised.

UW institutions will have undercharged an estimated \$24,000 for rental payments during 2019.

We cannot determine from available information what the rental payment amounts would have been had DOA completed an appraisal in recent years. However, UW institutions were required to accurately implement all rental payment adjustments determined by DOA. We found UW institutions did not charge employees the full rental payment amounts because they did not accurately implement all adjustments. Based on rental payment amounts charged in December 2018, UW institutions will have undercharged an estimated \$24,000 for rental payments during 2019 for the 12 state-owned properties in which UW institutions required employees to reside.

UW Madison did not consistently implement rental payment adjustments determined by DOA between 1998 and 2018.

We found that UW-Madison did not implement all rental payment adjustments determined by DOA between 1998 and 2018 when it executed lease agreements with employees residing at agriculture research stations. According to the UW-Madison employee who managed most of the research stations, rental payment adjustments were determined independently, such as when there was a new occupant or when the employee believed there were inequities in rental payments among employees located at the research stations. As noted, because the rental payment amounts were not included in lease agreements and rental payment adjustments were verbally communicated, we were unable to assess the frequency or

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consistency of the rental payment adjustments for employees that resided at the research stations.

We also found UW System Administration had leased an apartment to two employees who were not required to pay rent in exchange for managing UW events at the UW System President's residence. During our audit, UW System Administration indicated that the two employees no longer resided in the property as of September 2019.

Collecting Rental Payments

In December 2018, UW institutions collected \$4,700 in rental payments from UW employees who were required to reside in a state-owned property.

UW employees who are required to reside in state-owned properties as a primary residence make rental payments either through biweekly payroll deductions or checks. In December 2018, UW institutions collected \$4,700 in rental payments from UW employees who were required to reside in the properties. The average monthly rental payment for these employees required to make rental payments was \$338 as of December 2018. For those lease agreements in effect as of December 2018, we found that all rental payments UW institutions expected had been received through June 2019.

Demonstrating Compliance with IRS Guidelines

UW institutions demonstrated compliance with IRS guidelines in only 3 of 16 lease agreements in effect as of December 2018.

We found all of the 16 lease agreements in effect as of December 2018 related to 15 state-owned residential properties included at least a 50.0 percent rental payment discount. In order to not treat the discount amount as taxable income for the employee, UW institutions were required to comply with DOA policies and with IRS guidelines. Therefore, UW institutions should have documented in appointment letters, or comparable personnel information, that the employee was both required to reside in a state-owned property as a condition of employment and that residing in the property was necessary for the employee to properly conduct job responsibilities. However, we found that UW institutions demonstrated compliance with IRS guidelines in only 3 of the 16 lease agreements. An additional 12 lease agreements met one, but not both, of the requirements, and 1 lease agreement met neither requirement.

For the 12 lease agreements that met one but not both requirements, UW institutions identified a need for the employee to reside in the property to conduct job responsibilities. However, UW institutions did not state the requirement in appointment letters, or other comparable personnel information. For example, UW-Madison staff who managed most of the agricultural research stations indicated that the living arrangement is required for all employees, has been so for the last several decades, and is necessary to meet the demands of a fully operational farm. Several of the agriculture research stations required frequent measurements, monitoring for irrigation,

sampling, and animal feeding, which are conducted by research program managers or other employees in agricultural positions such as animal research technicians. UW institutions should clearly specify in appointment letters, or other personnel information, when they require an employee to reside in a state-owned property as a condition of employment.

UW-Madison should not have provided a 50.0 percent rental payment discount and may need to consider tax implications for one employee.

The lease agreement that met neither requirement was one UW-Madison executed with an employee residing at an agriculture research station who held a position unrelated to agriculture and commuted to work each day to conduct primary job responsibilities elsewhere. As a result, the employee did not conduct primary job responsibilities at the research station and was present only during evenings and weekends. According to UW-Madison staff, because UW-Madison desired that someone reside in the state-owned property, it offered the residence to this employee who opted to reside in it. If the employee was not required to reside in the state-owned property to conduct job responsibilities, UW-Madison should not have provided a 50.0 percent rental payment discount and may need to consider tax implications for this employee.

Improving Management of Residential Properties

Although UW institutions executed some lease agreements for employees required to reside in state-owned properties as of December 2018, collected the rental payments in a timely manner, and identified business requirements for all but one employee required to reside in a state-owned property, UW institutions did not have sufficient documentation for all lease agreements and lacked appointment letters for all employees who were required to reside in the properties. Further, not all UW institutions correctly determined rental payment amounts in compliance with DOA policies.

UW System Administration relied on UW institutions to ensure that rental payment adjustment information was accurately communicated.

UW System Administration did not have a complete listing of all state-owned residential properties at the time of our audit. For example, only 2 of the 15 properties occupied as of December 2018 were included in the listing we initially received from UW System Administration. UW System Administration relied on UW institutions to ensure that rental payment adjustment information was accurately communicated to property managers, and it did not require confirmation that the institutions had implemented the DOA rental payment adjustments. If UW System Administration had done so, the rental payment adjustments on these properties may have been consistently and accurately applied.

The number of state-owned residential properties UW institutions maintain is small in comparison to the number of UW academic

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facilities, yet specific requirements exist for residential properties. As a result, greater monitoring and oversight is needed to ensure that all requirements are consistently and accurately met. UW System Administration should maintain a current listing of properties leased to UW employees, develop policies and procedures for UW institutions to comply with all requirements when executing lease agreements with employees, and periodically take steps to ensure that UW institutions comply with these policies.

Recommendation

We recommend the University of Wisconsin System Administration improve its management of state-owned residential properties, including by:

- *complying with Department of Administration policies in executing lease agreements with employees who reside in state-owned residential properties;*
- *developing system-wide policies and procedures to promote consistent understanding and implementation of state policies within University of Wisconsin institutions in areas such as formally communicating when an employee is required to reside in a state-owned property as a condition of employment, determining rental payment amounts, and formally communicating expected rental payment amounts to employees;*
- *centrally tracking its state-owned residential properties in which University of Wisconsin institutions require employees to reside as a condition of employment;*
- *periodically monitoring whether University of Wisconsin institutions consistently follow Department of Administration and University of Wisconsin policies to manage state-owned residential properties; and*
- *reporting by April 10, 2020, to the Joint Legislative Audit Committee on the status of its efforts to implement these recommendations.*

Employees Opting to Reside in State-Owned Properties

UW institutions managed 99 state-owned residential properties in which employees opted to reside in December 2018, including two UW-River Falls properties located at a research station and one property at the UW System President's residence.

Lease agreement terms for UW employees opting to reside in 96 optional UW-Madison apartment buildings are treated similar to the terms for students.

The 96 remaining properties are managed by UW-Madison as housing options largely for faculty and academic staff. The apartment buildings in which state employees resided are a subset of the residential housing options administered by UW-Madison's housing division that are located near the campus. Although some of UW-Madison's apartments are rented to students, the lease agreements and management of the agreements appear to be the same between UW employees and students. For example, UW-Madison staff identified that one schedule of rent is used regardless of the occupant. The apartments include one-, two-, and three-bedroom options with monthly rental payment amounts ranging from \$850 to \$1,400.

Current DOA policies do not fully address how rental payment amounts should be determined for UW employees who opt to reside in apartments.

The apartments leased to state employees on an optional basis were not part of the 1995 appraisals conducted by DOA. Because state employees reside in a state-owned property, statutory requirements for these properties apply to UW employees who opt to reside in them. However, we found that current DOA policies do not fully address how the rental payment amounts should be determined.

Instead, we found UW-Madison independently determined rental payment amounts based on periodic comparisons to area rental units. For example, UW-Madison last completed an evaluation of comparable rental payment amounts in 2014. Because UW employees pay the same amounts as others who opt to reside in a state-owned property, the employees are likely receiving no discount, or additional benefit, from UW-Madison.

Recommendation

We recommend University of Wisconsin System Administration work with the Department of Administration to develop policies that specify how to determine rental payment amounts for employees who opt to reside in state-owned properties, including apartment buildings that may house both students and employees, and report by April 10, 2020, to the Joint Legislative Audit Committee on the efforts to implement this recommendation.

Future Considerations ■

DOA's existing policies governing state-owned residential properties leased to state employees were established in 1975. As DOA considers changes, it should ensure that it has clearly defined the responsibilities of DOA and state agencies. For example, DOA should increase its responsibility for monitoring lease agreements with state employees. DOA should also identify potential statutory changes that may be needed to the frequency with which it should conduct appraisals and determine how it will ensure state employees that reside in state-owned properties are consistently charged rental payment amounts that reflect fair value. DOA should also consider establishing policies for determining rental payment amounts for employees who opt to reside in state-owned properties.

DOA Monitoring of State Employee Lease Agreements

DOA should take a more active role in monitoring lease agreements with state employees.

DOA should take a more active role in monitoring lease agreements executed by state agencies to ensure they comply with DOA policies by obtaining and reviewing all lease agreements. As noted, DOA policies identify specific arrangements expected when state agencies execute lease agreements with state employees, including the amount and timing of rental payments; the responsibility for payment of utilities and performance of basic maintenance; the rights of each party to the agreement; and the period covered by the agreement. Involvement by DOA in reviewing lease agreements could help to ensure consistency of lease agreement provisions among state agencies, consider tax implications resulting from the

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lease agreements, and monitor rental payment amounts and discounts. Finally, increased oversight of lease agreements state agencies execute with state employees is consistent with DOA's current statutory responsibilities for actively managing state agency facility lease agreements.

Recommendation

We recommend the Department of Administration:

- *develop policies and procedures to monitor lease agreements state agencies execute with state employees who reside in state-owned properties, and*
- *report by April 10, 2020, to the Joint Legislative Audit Committee on the status of its efforts to implement this recommendation.*

Establishing Fair Values for Residential Properties

In the absence of regular DOA appraisals or policies to address circumstances in which a rental payment amount could be revised between appraisals, we found state agencies had exercised increased discretion by establishing new base rental payment amounts or not implementing rental payment adjustments on the basis that the rental payment amounts did not reflect fair value. Although it will be important for DOA to conduct appraisals, it should reassess the frequency of appraisals to ensure that rental payment amounts consistently reflect fair value.

DOA should exercise its authority and develop a process to adjust the base rental payment amount for factors that significantly affect the fair value of a property.

Although statutes permit DOA to conduct appraisals more frequently for selected properties in certain circumstances, DOA did not exercise this authority when state agencies acquired new properties. DOA should specifically consider how to establish base rental payment amounts for the new properties and how to adjust the amounts for factors that significantly affect the fair value of a property. To do so, DOA could consider seeking statutory changes for conducting a new appraisal or relying on methods other than an appraisal that may be used to periodically revise the base rental payment amount. If DOA identifies that statutory changes are warranted, it should seek them.

DOA should also consider how base rental payment amounts are established for state-owned residential properties relative to appraised amounts. Following the 1995 appraisals, DOA calculated 7.0 percent of the property's appraised value and converted this to a monthly rental payment amount. DOA used 7.0 percent in this calculation based on the real estate investment returns of the State of Wisconsin Investment Board at the time. We note that IRS guidelines generally identify 5.0 percent of an appraised amount as a reasonable rental payment amount.

DOA should work with state agencies to determine what tax implications, if any, result from instances in which the rent charged to employees who opted to reside in state-owned properties was less than fair value.

Finally, under IRS guidelines, if an employee is not required to reside in a state-owned property, the difference between the fair value and rental payment amount may be considered taxable income for the employee. DOA should assess whether rental payment amounts reflect fair value and work with state agencies to determine what tax implications, if any, result from instances in which the rent charged to DNR and UW employees who opted to reside in state-owned properties was less than fair value.

Recommendation

We recommend the Department of Administration:

- *reassess the frequency with which appraisals could be conducted in the future and seek statutory changes if it determines it should do so;*
- *assess whether there should be changes in how rental payment amounts are determined and periodically adjusted to ensure that state employees are charged rental payment amounts that reflect the fair value of the property;*
- *work with state agencies to determine the tax implications, if any, that result from instances in which rental payment amounts charged to employees who opted to reside in state-owned properties were less than fair value; and*
- *report by April 10, 2020, to the Joint Legislative Audit Committee on the status of its efforts to implement these recommendations.*

Leasing to Employees Who Opt to Reside in UW Apartments

DOA policies do not specifically address UW employees who opt to reside in state-owned properties.

Because statutes require that DOA maintain policies that govern leasing state-owned residential properties and these properties are leased to state employees, we considered DOA policies in assessing UW-Madison's practice of leasing apartments to UW employees who opted to reside in them. However, as noted, we found that the policies do not specifically address UW employees who opt to reside in state-owned properties.

The apartment buildings in which UW employees reside were not appraised by DOA in 1995. Further, DOA's 1975 policy established a set rental payment amount for apartments and dormitories, but since there have been no policy revisions since 1975, these amounts are below the amounts UW-Madison currently charges employees. As a result, it is unclear how rental payment amounts should be determined to ensure employees are charged rental payment amounts that reflect a property's fair value as required by IRS guidelines.

It is important to consider how ch. 16, Wis. Stats., requirements apply to UW employees who opt to reside in these state-owned properties. As a result, DOA should develop specific policies for state-owned residential properties UW institutions may lease to UW employees, including how to determine rental payment amounts that reflect fair value.

Recommendation

We recommend the Department of Administration:

- *develop policies that specifically address how University of Wisconsin System Administration should determine rental payment amounts for employees who opt to reside in state-owned properties; and*
- *report by April 10, 2020, to the Joint Legislative Audit Committee on the status of its efforts to implement this recommendation.*

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Appendices ■

Appendix 1

DNR Residential Properties as of December 2018¹

| Property Type | Location | County | Discounted Monthly Rent Amount ² |
|-----------------------|--|-----------|---|
| Education Center | MacKenzie Center | Columbia | \$339 |
| State Fish Hatchery | Kettle Moraine Springs State Fish Hatchery | Sheboygan | 456 |
| State Fish Hatchery | Lake Mills State Fish Hatchery | Jefferson | 368 |
| State Fish Hatchery | Wild Rose State Fish Hatchery | Waushara | 358 |
| State Fish Hatchery | Wild Rose State Fish Hatchery | Waushara | 330 |
| State Fish Hatchery | Bayfield State Fish Hatchery | Bayfield | 239 |
| State Fish Hatchery | Bayfield State Fish Hatchery | Bayfield | 239 |
| State Fish Hatchery | C.D. Besadny Anadromous Fish Facility | Kewaunee | 239 |
| State Fish Hatchery | Brule River State Fish Hatchery | Douglas | 162 |
| State Forest | Kettle Moraine State Forest | Waukesha | 463 |
| State Forest | Kettle Moraine State Forest | Waukesha | 449 |
| State Forest | Kettle Moraine State Forest | Waukesha | 391 |
| State Forest | Kettle Moraine State Forest | Waukesha | 391 |
| State Forest | Kettle Moraine State Forest | Waukesha | 341 |
| State Game Farm | Poynette Game Farm | Columbia | 358 |
| State Park | Lake Kegonsa State Park | Dane | 489 |
| State Park | Devil's Lake State Park | Sauk | 477 |
| State Park | Kohler-Andrae State Park | Sheboygan | 477 |
| State Park | Devil's Lake State Park | Sauk | 463 |
| State Park | Big Foot Beach State Park | Walworth | 430 |
| State Park | Council Grounds State Park | Lincoln | 409 |
| State Park | Mirror Lake State Park | Sauk | 370 |
| State Park | Wyalusing State Park | Grant | 331 |
| State Park | Harrington Beach State Park | Ozaukee | 326 |
| State Park | Peninsula State Park | Door | 316 |
| State Park | Governor Nelson State Park | Dane | 306 |
| State Park | Potawatomi State Park | Door | 301 |
| State Park | Newport State Park | Door | 229 |
| State Park | Pattison State Park | Douglas | 191 |
| State Recreation Area | Richard Bong State Recreation Area | Kenosha | 430 |
| State Recreation Area | Hoffman Hills State Recreation Area | Dunn | 272 |
| State Recreation Area | Chippewa Moraine State Recreation Area | Chippewa | 159 |

¹ Includes those properties occupied by DNR employees as a primary residence.

² These amounts reflect the actual monthly rental payments, which includes a 50.0 percent discount.

Appendix 2

UW System Residential Properties That Required an Employee Reside as of December 2018¹

| Property Type | UW Institution | County | Discounted Monthly Rent Amount ² |
|------------------|----------------|----------|---|
| Research Station | Stevens Point | Waupaca | \$450 |
| Research Station | Platteville | Grant | 389 |
| Research Station | Madison | Columbia | 387 |
| Research Station | Madison | Columbia | 365 |
| Research Station | Madison | Oneida | 359 |
| Research Station | Madison | Columbia | 350 |
| Research Station | Madison | Columbia | 350 |
| Research Station | Madison | Columbia | 345 |
| Research Station | Madison | Wood | 335 |
| Research Station | Madison | Waushara | 330 |
| Research Station | Madison | Columbia | 325 |
| Research Station | Madison | Columbia | 320 |
| Research Station | Madison | Columbia | 316 |
| Research Station | Madison | Oneida | 104 |
| Apartment | System | Dane | — ³ |

¹ Includes those properties occupied by employees in Wisconsin Retirement System-eligible positions as a primary residence.

² These reflect the actual monthly rental payments, which includes a 50.0 percent discount.

³ No monthly rental payment amount was identified as services were provided in lieu of rental payments.

Responses ■



STATE OF WISCONSIN
DEPARTMENT OF ADMINISTRATION

Tony Evers, Governor
Joel Brennan, Secretary

December 3, 2019

Joe Chrisman
State Auditor
State of Wisconsin, Legislative Audit Bureau
22 East Mifflin Street, Suite 500
Madison, WI 53703

Dear Mr. Chrisman:

This correspondence constitutes the Department of Administration's ("DOA") written response to the Legislative Audit Bureau's ("LAB") audit report of DOA's oversight of state-owned residential properties ("Audit Report"). DOA generally concurs with the findings of the Audit Report and has already begun taking steps to address its findings and recommendations. The remainder of this response will enumerate the Audit Report's recommendations and detail DOA's plans for addressing them.

1. Ensure that state agencies provide confirmation that the CPI rent adjustments are implemented

DOA is required by statute to fix rental rates for state-owned housing rental units based on fair market appraisals conducted every ten years, and then adjust those rental rates every two years based on changes in the consumer price index ("CPI"). DOA has been sending letters every two years to state agencies advising them of the applicable CPI adjustments. DOA is also required by statute to establish a system of rental policies and periodically review those policies for possible changes. In order to address this specific recommendation, DOA intends to include in its comprehensive review of its existing system of rental policies potential changes directing agencies to verify implementation of CPI-based rent adjustments.

2. Work with agencies to reassess whether to retain state-owned residential properties, including recommending to SBC whether any properties should be sold, razed, or used for other purposes

DOA is required by statute to include in its system of rental policies a procedure for review of the need to retain state-owned housing units and possible disposition of such units. DOA has existing procedures in place for state agencies to biennially report underutilized real property in accordance with section 13.48(14)(d) of the Wisconsin Statutes, which DOA then uses to evaluate whether such properties should be considered for disposition pursuant to section 16.848 of the Wisconsin Statutes. To the extent that agencies with state-owned residential properties consider such properties to be underutilized, such properties would be included in their biennial reports. In order to address this recommendation, DOA intends to include in its comprehensive review of its existing system of rental policies consideration of whether to include specific reference to the biennial underutilized real property report and/or whether a separate reporting mechanism should apply for state-owned housing units.

3. Improve administration by complying with statutes by periodically reviewing and formally revising applicable policies

DOA is required by statute to periodically review its system of rental policies for state-owned housing for possible changes. DOA's existing policy has not been revised since 1975. In order to address

this recommendation DOA intends to conduct a comprehensive review of its policy and submit proposed changes to the joint committee on finance as required by statute.

4. Improve administration by tracking rental properties and monitoring rental payment amounts state agencies charge employees

In order to address this recommendation, DOA intends to request from the relevant state agencies an up-to-date inventory of state-owned housing and copies of current lease agreements. DOA further intends to include in its comprehensive review of its existing system of rental policies consideration of changes necessary for agencies to report rent payments to DOA and any changes in their inventory of state-owned housing.

5. Improve administration by complying with statutes to conduct appraisals of all state-owned residential properties

DOA is required by statute to conduct appraisals of state-owned housing units every ten years. DOA acknowledges that no such appraisals have been conducted since 1995. By statute DOA is required to conduct its next set of appraisals in 2022. In order to address this specific recommendation, DOA intends to contract with appraisers to conduct the necessary appraisals in 2022. In DOA's exit interview with LAB, we explained the practical and financial difficulties of conducting such appraisals now, given that we are required by statute to conduct them again in three years.

6. Ensure the system of rental policies sets forth clearly defined responsibilities of DOA and state agencies

As discussed above, DOA intends to conduct a comprehensive review of its policy and submit proposed changes to the joint committee on finance as required by statute. As part of that review, DOA intends to consider changes to more clearly define the responsibilities of DOA and state agencies.

7. Increase responsibility for monitoring lease agreements with state employees

As discussed above, DOA intends to conduct a comprehensive review of its policy and submit proposed changes to the joint committee on finance as required by statute. As part of that review, DOA intends to consider changes to address this specific recommendation.

8. Identify potential statutory changes as necessary regarding the frequency of appraisals

DOA is required by statute to conduct appraisals of state-owned housing units every ten years. In order to address this recommendation DOA intends to review whether more frequent appraisals are appropriate. However, based on a preliminary analysis, DOA believes it is unlikely a statutory change is warranted, given the cost and administration required to conduct appraisals of such a large volume of properties. As part of its comprehensive review of the existing system of rental policies DOA will examine whether to recommend any other statutory changes.

9. Consider how to establish base rental payment amounts for new properties and how to adjust amounts for factors that significantly affect the fair value of the property

DOA is required by statute to fix rental rates for state-owned housing rental units based on fair market appraisals conducted every ten years, and then adjust those rental rates every two years based on changes in CPI. DOA is permitted by statute to reappraise the fair market value of a unit if it has been affected by a major renovation. In order to address the first part of this recommendation, DOA intends to include in its comprehensive review of its existing system of rental policies consideration of how to establish the fair market value of new housing units constructed or acquired in between the ten-year appraisals conducted on all housing units. With respect to the second part of this recommendation, DOA observes that section 16.004(8)(e)3. of the Wisconsin Statutes only permits two types of adjustments to rental rates in between the ten-year appraisals: 1) biennial adjustments based on CPI; and 2) adjustments

based on reappraisals when a property has been affected by a major renovation. As part of its comprehensive review of the existing system of rental policies DOA will examine whether to recommend any statutory changes to address this limitation.

10. Work with state agencies to determine the tax implications, if any, that result from instances in which rental payment amounts charged to employees who opted to reside in state-owned properties were less than fair value

IRS guidance establishes that employees who are offered employer-owned housing at below fair market value must report the difference in rent vs. fair market value as income, unless the employee is required to live in such housing as a condition of his/her employment. In order to address this specific recommendation, DOA intends to work with the relevant state agencies to determine which employees may currently be affected by such IRS guidance and the amount of rent they are paying to ensure they are properly reporting any income as part of their tax returns. DOA further intends to work with such agencies in conducting its comprehensive review of its existing system of rental policies to determine: 1) what documentation agencies should provide to establish that an employee is required to live in state-owned housing as a condition of their employment; 2) whether agencies should be permitted to charge employees below market rent to employees who are not required to live in state-owned housing as a condition of their employment; and 3) if so, what the appropriate reporting mechanisms should be to ensure that such employee's W-2s accurately reflect their income.

11. Develop policies that specifically address how University of Wisconsin System Administration should determine rental payment amounts for employees who opt to reside in state-owned properties

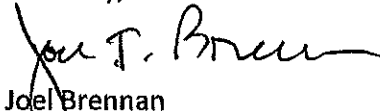
As stated above, as part of a comprehensive review of existing system of rental policies DOA intends to work with relevant agencies to determine whether employees should be permitted to pay below market rates when living in state-owned housing is not mandatory as a condition of their employment. If DOA and the agencies conclude that below market rents are appropriate, DOA will work with them to make proposed changes to its system of rental policies and submit them to the joint committee on finance for approval.

12. Report to the Joint Legislative Audit Committee ("JLAC") by April 10, 2020 on the status of efforts to implement LAB's recommendations

DOA will submit a report to JLAC by April 10, 2020 updating the committee on the implementation actions set forth in this response.

On behalf of DOA, I thank the LAB staff for the professional manner in which they conducted this audit.

Sincerely,


Joel Brennan
Secretary

State of Wisconsin
DEPARTMENT OF NATURAL RESOURCES
101 S. Webster Street
Box 7921
Madison WI 53707-7921

Tony Evers, Governor
Preston D. Cole, Secretary
Telephone 608-266-2621
Toll Free 1-888-936-7463
TTY Access via relay - 711



December 4, 2019

State Auditor Joe Chrisman
Legislative Audit Bureau
22 East Mifflin St. Suite 500
Madison, WI 53703

Subject: State Residential Property Audit

Dear Mr. Chrisman:

Thank you for the opportunity to review the draft Legislative Audit Bureau (LAB) evaluation of the Wisconsin Department of Natural Resources' (DNR) administration of state-owned residential housing. The report provides information and datapoints about state-owned property, appraised values, conditions-of-employment, leases, and rents paid to the DNR by state employees living within state-owned residential housing.

I appreciate the work performed by LAB staff. Please accept my assurance to you and the Joint Legislative Audit Committee that the DNR will work with the Wisconsin Department of Administration to improve management of residential housing, appraisals, lease-terms, rent-calculations, and shared-services human resource protocols regarding employee designations, appointment letters, transfers, and bi-weekly withholdings.

While the issues identified have occurred over the course of multiple decades and administrations, the DNR takes the issues raised within this audit seriously, and I am committed to providing significant improvements in this administrative process. I look forward to providing you with information regarding process improvements on or before April 10, 2020 as outlined in your list of recommendations.

Thank you again for providing the opportunity to review the LAB state-owned residential housing audit report.

Sincerely,

Preston D. Cole
Secretary-Designee
Department of Natural Resources



Office of the President
1700 Van Hise Hall
1220 Linden Drive
Madison, Wisconsin 53706-1559
608-262-2321
rcross@uwsa.edu
www.wisconsin.edu

December 3, 2019

Joe Chrisman, Auditor
Legislative Audit Bureau
22 East Mifflin Street, Suite 500
Madison, WI 53703

Dear Auditor Chrisman,

Thank you for the opportunity to respond to the Legislative Audit Bureau's (LAB) review of state-owned properties leased to state employees that are associated with the University of Wisconsin (UW) System.

LAB's review of state-owned properties was specific to state-owned properties managed by six state agencies and leased to state employees. As the LAB review notes, state statutes require that the Department of Administration (DOA) administer those properties by developing policies, conducting appraisals, and determining rental payment amounts to ensure rental payments state agencies charge state employees are based on the fair value of the properties. The UW System recognizes that there are opportunities for improved processes, procedures and documentation practices and agrees with the five recommendations detailed in the report. However, it is important to acknowledge that the review did not identify any instance of intentional fraud, waste and/or mismanagement, but rather opportunities to improve practices and protocols associated with a relatively low number (43) of the over 1,400 properties managed by the UW System, approximately 3% of the total inventory.

Recommendations from the report specific to the UW System, and the UW System response, are noted below:

- ***LAB Recommendation 1: Comply with Department of Administration policies in executing lease agreements with employees who reside in state-owned residential properties.***
 - UW System Response: The UW System will conduct a review of current Department of Administration policies to ensure compliance.

- ***LAB Recommendation 2: Develop system-wide policies and procedures to promote consistent understanding and implementation of state policies within University of Wisconsin institutions in areas such as formally communicating when an employee is required to reside in a state-owned property as a condition of employment, determining rental amounts, and formally communicating expected rental payment amounts to employees***
 - UW System Response: The UW System will develop an administrative policy and associated procedures that reflect state statutes and Department of Administration policies. Further, the UW System will provide guidance to the UW institutions on both documenting and communicating when an employee is required to assume residency in a state-owned property as a condition of employment.
 - Rental amounts shall be developed in accordance with state statute and Department of Administration guidelines.

- **LAB Recommendation 3: Centrally track its state-owned residential properties in which University of Wisconsin institutions require employees to reside as a condition of employment**
 - UW System Response: The UW System's Office of Capital Planning and Budget, in conjunction with Office of Human Resources, will develop an annual process for UW institutions to report to the UW System regarding those employees that are required to assume residency as a condition of employment.

- **LAB Recommendation 4: Periodically monitor whether University of Wisconsin institutions consistently follow Department of Administration and University of Wisconsin policies to manage state-owned residential properties**
 - UW System Response: The UW System will periodically monitor compliance with state statute and applicable policies.

- **LAB Recommendation 5: UW System work with the Department of Administration to develop policies that specify how to determine rental payment amounts for employees who opt to reside in state-owned properties, including apartment buildings that may house both students and employees.**
 - UW System Response: The UW System will work collaboratively with the Department of Administration on the best means to determine current and future rental payments, including defining a process for conducting a periodic assessment.
 - However, the UW System considers apartment buildings outside of this scope as there is no employment relationship associated with the university housing portfolio.

For all of the above recommendations, the UW System will report to the Joint Legislative Audit Committee on the status of its efforts to implement these recommendations by April 10, 2020.

Thank you for LAB's work on this review of state-owned properties managed by state agencies. We remain committed to working closely with DOA to ensure that the UW System is in compliance with state statutes and applicable DOA policies.

Respectfully submitted,



Ray Cross
President



STATE OF WISCONSIN
DEPARTMENT OF ADMINISTRATION

Tony Evers, Governor
Joel Brennan, Secretary

December 3, 2019

Joe Chrisman
State Auditor
State of Wisconsin, Legislative Audit Bureau
22 East Mifflin Street, Suite 500
Madison, WI 53703

Dear Mr. Chrisman:

This correspondence constitutes the Department of Administration's ("DOA") written response to the Legislative Audit Bureau's ("LAB") audit report of DOA's oversight of state-owned residential properties ("Audit Report"). DOA generally concurs with the findings of the Audit Report and has already begun taking steps to address its findings and recommendations. The remainder of this response will enumerate the Audit Report's recommendations and detail DOA's plans for addressing them.

1. Ensure that state agencies provide confirmation that the CPI rent adjustments are implemented

DOA is required by statute to fix rental rates for state-owned housing rental units based on fair market appraisals conducted every ten years, and then adjust those rental rates every two years based on changes in the consumer price index ("CPI"). DOA has been sending letters every two years to state agencies advising them of the applicable CPI adjustments. DOA is also required by statute to establish a system of rental policies and periodically review those policies for possible changes. In order to address this specific recommendation, DOA intends to include in its comprehensive review of its existing system of rental policies potential changes directing agencies to verify implementation of CPI-based rent adjustments.

2. Work with agencies to reassess whether to retain state-owned residential properties, including recommending to SBC whether any properties should be sold, razed, or used for other purposes

DOA is required by statute to include in its system of rental policies a procedure for review of the need to retain state-owned housing units and possible disposition of such units. DOA has existing procedures in place for state agencies to biennially report underutilized real property in accordance with section 13.48(14)(d) of the Wisconsin Statutes, which DOA then uses to evaluate whether such properties should be considered for disposition pursuant to section 16.848 of the Wisconsin Statutes. To the extent that agencies with state-owned residential properties consider such properties to be underutilized, such properties would be included in their biennial reports. In order to address this recommendation, DOA intends to include in its comprehensive review of its existing system of rental policies consideration of whether to include specific reference to the biennial underutilized real property report and/or whether a separate reporting mechanism should apply for state-owned housing units.

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this recommendation DOA intends to conduct a comprehensive review of its policy and submit proposed changes to the joint committee on finance as required by statute.

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based on reappraisals when a property has been affected by a major renovation. As part of its comprehensive review of the existing system of rental policies DOA will examine whether to recommend any statutory changes to address this limitation.

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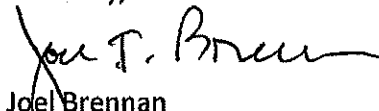
As stated above, as part of a comprehensive review of existing system of rental policies DOA intends to work with relevant agencies to determine whether employees should be permitted to pay below market rates when living in state-owned housing is not mandatory as a condition of their employment. If DOA and the agencies conclude that below market rents are appropriate, DOA will work with them to make proposed changes to its system of rental policies and submit them to the joint committee on finance for approval.

12. Report to the Joint Legislative Audit Committee ("JLAC") by April 10, 2020 on the status of efforts to implement LAB's recommendations

DOA will submit a report to JLAC by April 10, 2020 updating the committee on the implementation actions set forth in this response.

On behalf of DOA, I thank the LAB staff for the professional manner in which they conducted this audit.

Sincerely,


Joel Brennan
Secretary

[NAME OF STATE AGENCY]

RESIDENTIAL LEASE

This Lease is made and entered into by and between [STATE AGENCY], hereafter called the Landlord, and the Tenant as named below:

1. TENANT(S): _____

Number of occupants: _____

Names and email addresses (if any). Indicate if occupant is a minor instead of email address:

Name: _____ Email: _____

Name: _____ Email: _____

Name: _____ Email: _____

Name: _____ Email: _____

- Tenant shall notify Landlord of any additional occupants following the execution the lease. Total number of occupants is limited to local residential occupancy and zoning code limits.

2. LANDLORD: [STATE AGENCY]

Agent for payment of rent and service of process: _____

Mailing address: _____

Email address: _____

Agent for maintenance and management: _____

Mailing address: _____

Email address: _____

3. PREMISES: Building Address

4. RENT: Rent for the premises shall be \$_____ per month, payable by check and received from the Tenant before the first of each month. ***[Include the following, if applicable: The parties acknowledge that the monthly Rent specified herein includes a __% rent reduction for Tenant's performance of specific duties in connection with Tenant's occupancy of the Premises as set forth in in Attachment A to this Lease. In the event that Tenant fails to perform such duties without Landlord's written consent the __% rent reduction for the month in which such failure to perform such duties will not apply.]***

5. RENT ADJUSTMENTS: Rent as set forth in Paragraph 4 is subject to adjustments set forth in this Paragraph 5 as applicable. Tenant shall receive notice of any Rent adjustment at least 60 days prior to such adjustment.

- a. No later than July 1 of the 2nd year following the federal decennial census Landlord is required by law to obtain an appraisal of the fair market value of the Premises and to determine and fix rent based on such appraisal ("Decennial Appraisal-based Rent"), with the new rate taking effect on the following August 15 ("Decennial Appraisal-based Rent Adjustment Date"). In the event that the Decennial Appraisal-based Rent Adjustment Date occurs during the term of the Lease the parties hereby agree that the Decennial Appraisal-based Rent, ***[Include the following, if applicable: as adjusted by the ___% rent reduction for Tenant's performance of specific duties in connection with Tenant's occupancy of the Premises as set forth in in Attachment A to this Lease,]*** shall replace the Rent set forth in paragraph 4 beginning on the Decennial Appraisal-based Rent Adjustment Date.
 - b. In the event that the Premises has been affected by a major renovation, as determined by the State of Wisconsin, Department of Administration ("DOA"), DOA may obtain an appraisal of the fair market value of the Premises for the purpose of determining and fixing a new rental rate based on such appraisal ("Renovation Appraisal-based Rent"). In the event that such an appraisal occurs during the term of the Lease the parties hereby agree that the Renovation Appraisal-based Rent, ***[Include the following, if applicable: as adjusted by the ___% rent reduction for Tenant's performance of specific duties in connection with Tenant's occupancy of the Premises as set forth in in Attachment A to this Lease,]*** shall replace the Rent set forth in paragraph 4 effective August 15 of the year in which such appraisal occurs, unless such appraisal occurs on or after July 1, in which case the rent adjustment shall take effect on August 15 of the following year.
 - c. The parties acknowledge that in the event that no appraisal-based rental rate adjustments have been made during the 24-month period ending on July 1 of any even-numbered year the Rent shall be subject to a cost-of-living adjustment, determined by multiplying the Rent by the percentage change in the consumer price index for all items, U.S. city average over a 12-month period ending on December of the preceding year, then adding the product to the current rental rate and rounding to the nearest whole dollar ("COLA-Adjusted Rent"). The COLA Adjusted Rent shall replace the Rent set forth in paragraph 4 beginning August 15 of such even-numbered year.
6. LEASE TERM: Lease term is for one year, commencing _____ and continuing until _____ unless terminated earlier according to the terms of this Lease. This Lease agreement is only for the stated term and is not automatically renewable. Landlord and Tenant must agree in writing if tenancy is to continue beyond the last day of the rental Term. The Tenant shall surrender the Premises on the last day of the Term provided in this Lease Agreement, or if Tenant separates from [STATE AGENCY] employment, at the end of the month in which separation occurs. Upon surrender, Tenant and all occupants shall vacate the Premises and return or account for any of Landlord's property held by Tenant, such as keys, garage door opener, etc. and provide Tenant's forwarding address to Landlord. This lease may be terminated by either party with 30-days' notice.

7. UTILITIES: Tenant agrees to pay all utilities for the Premises including gas, heat, electricity, water, sewer, and internet and cable television. The tenant is responsible for trash collection and disposal. If the Premises is located on [STATE AGENCY]-owned property where trash collection is provided, Tenant may use such trash collection.
8. RENTERS INSURANCE: Tenant agrees at Tenant's sole expense, to procure and maintain in full force and effect a renter's policy, with a Personal Liability limit of not less than \$500,000 per each occurrence, for bodily injury and property damage liability, and sufficient limits to protect the value of Tenant's personal property. Tenant shall provide Landlord at least 30 days written notice of any changes to this policy, such as cancellation of coverage or changes in insurance limits. Tenants shall furnish Landlord with evidence of insurance on or before effective date of lease. The policy declaration page and/evidence of insurance letter shall name Landlord as an additional interest.
9. LANDLORD INSURANCE: Landlord maintains liability coverage for its officers, employees, and agents pursuant to the State of Wisconsin Self-Funded Liability Program. Landlord also provides property coverage for contents owned by the Landlord that are considered part of the real property. Tenant personal effects are not included in this coverage.
10. INSPECTION: Tenant shall be given a check-in sheet by Landlord upon commencing occupancy that Tenant may use to make comments, if any, about the condition of the Premises, and the Tenant shall have seven (7) days from the date of first occupancy to complete the checklist and return to Landlord.
11. CODE VIOLATIONS: Landlord has no actual knowledge of any building code or housing code violation that affects the Premises or common areas associated with the Premises, presents a significant threat to Tenant's health or safety, and has not been corrected, unless disclosed in an Attachment to this Lease per Wis. Stat. s. 704.07(2)(bm). The Premises do not contain any of the following conditions adversely affecting habitability unless listed in an Attachment: no hot or cold running water, plumbing or sewage disposal facilities not in good operating order, unsafe or inadequate heating facilities (incapable of maintaining at least 67°F in living areas), no electricity, electrical wiring components not in safe operating condition, or structural or other conditions that are substantially hazardous to health or safety.
12. MAINTENANCE: Attach Exhibit A outlining specific duties.
 - a. All requests by Tenant for non-emergency maintenance services by Landlord must be in writing, provide authorization for Landlord to enter, and identify reasonable time periods in which entry for maintenance is authorized. Tenant shall notify Landlord as soon as practicable for any repair or maintenance that may occur that is the responsibility of the Landlord.
 - b. Tenant shall maintain the Premises under Tenant's control in a clean and as good a condition as they were at the beginning of the Term or as subsequently improved by Landlord, ordinary wear and tear excepted. Tenant is responsible for minor repairs

including but not limited to replacement of smoke detector batteries, light bulbs, fuses, and washers.

- c. Tenant is responsible for all snow removal and ensuring walks and driveways are clear and free from ice and snow. Tenant is also responsible for mowing grass and other exterior landscape maintenance. Tenant is allowed to make modifications to the landscaping, such as a vegetable garden or planting flowers, that do not materially impact the function of the Premises. ***[This is standard language for when the agency intends to make these various items the tenant's responsibility. Replace with "Intentionally Omitted" if the agency will not be making the tenant responsible for these items.]***
 - d. Tenant is responsible for all damage and repairs that are beyond normal wear and tear, due to their own causation. This includes, but is not limited to clogged drains, foreign objects in the toilet or garbage disposal, frozen pipes, fires, damage to the air conditioner (if provided), stove/oven, refrigerator, and washer/dryer.
 - e. Tenant agrees not to make or permit to be made any alterations, improvements, or additions in, or to the Premises, without the permission of Landlord.
 - f. Tenant shall not store any trash, merchandise, appliances, crates, pallets, or materials of any kind outside the leased premises without the Landlord's prior approval. Tenant shall not park or keep any unlicensed and/or unregistered vehicles or equipment on the paved and landscaped areas immediately adjacent to the premises without prior approval of the Landlord.
 - g. Smoking in the Premises or common areas appurtenant thereto is not allowed.
 - h. Tenant shall not permit guests or invitees to reside in the Premises for more than three consecutive days without prior written consent of the Landlord.
13. SMOKE AND CARBON MONOXIDE DETECTORS: Tenant is responsible for maintaining smoke and carbon monoxide detectors within the Premises, including replacing batteries, or giving Landlord written notice whenever a detector on the Premises is not functional. If the detectors are connected directly to the household electrical service, maintenance of the detectors shall be the responsibility of the Landlord. Landlord is responsible for maintaining smoke and carbon monoxide detectors within the common areas appurtenant to the Premises.
14. ENTRY BY LANDLORD: Landlord may enter the premises at reasonable times upon advance notice to inspect the Premises, make repairs, show the Premises to prospective tenants or purchasers, or comply with applicable laws and regulations. Landlord may enter without advance notice upon consent of Tenant, or when a health or safety emergency exists, or if Tenant is absent and Landlord believes that entry is necessary to protect the Premises from damage.
15. DAMAGE OR DESTRUCTION OF PREMISES: If the Premises are wholly destroyed by fire or other casualty, this lease shall terminate. If the Premises become untenable due to fire, water or other casualty or because of any condition hazardous to health, either party by terminate the Lease by giving written notice to the other within fifteen (15) days of such destruction or damage.

16. EARLY TERMINATION: If Tenant vacates the Premises before the end of the Tenancy, or If the lease terminates due to separation of employment, Tenant shall be responsible for all rent due through the end of the month in which separation occurs, or until Tenant vacates the Premises, whichever is later. If Tenant leaves personal property behind, Landlord shall have the right to dispose of the property as provided by law or per any written property agreement. This does not apply if Tenant has terminated employment with the State. If tenancy is terminated for Tenant's breach of this Agreement, Tenant shall be liable for all rent due under this Agreement through the last day of the month, plus any cost to repair damages incurred by Landlord.

17. DEFAULT; REMEDIES.

- a. If Tenant fails to pay any installment of rent when due, or is in default of the Lease by committing waste or a material violation of s. 704.07 (3) or by breaching any covenant or condition of the Lease, the Tenant's tenancy is terminated if the Landlord gives the Tenant notice requiring the Tenant to pay rent or remedy the default, or vacate, on or before a date at least 5 days after the giving of the notice and if the Tenant fails to pay accordingly or remedy such default. In the case of notice of instances of default, Tenant is deemed to be complying with the notice if promptly upon receipt of such notice the Tenant takes reasonable steps to remedy the default and proceeds with reasonable diligence, or if damages are adequate protection for the Landlord and Tenant makes a bona fide and reasonable offer to pay the landlord all damages for the Tenant's breach. If Tenant has been given such a notice of failure to pay rent or default and has paid the rent or cured the default on or before the specified date, or been permitted by Landlord to remain in possession contrary to such notice, and if within one year of any prior failure to pay rent or act of default for which notice was given Tenant fails to pay a subsequent installment of rent on time or again commits waste or breaches the same or any other covenant or condition of the Lease, the Tenant's tenancy is terminated if the Landlord, while the Tenant is in default of the obligations to pay rent or other covenant or condition of the lease, gives the Tenant notice to vacate on or before a date at least 14 days after the giving of the notice.
- b. Following vacation of the Premises on account of non-payment of rent or other default, Tenant remains responsible to the Landlord for any unpaid rent and damages for which Tenant is responsible under the Lease, in addition to any other rights or remedies available to the Landlord by law.
- c. If Tenant leaves personal property behind, Landlord shall have the right to dispose of the property as provided by law or per any written property agreement

18. PETS: Dogs and cats may be kept on the Premises upon written approval of Landlord, which may be rescinded at any time. All such animals must be restrained on a leash under the physical control of the person responsible for the animal when in the common areas appurtenant to the Premises, unless written approval is obtained from Landlord for working dogs and cats used for rodent control. A copy of the Policy on Dogs and Cats on Agricultural Stations, Farms and Animal Facilities is attached as Attachment B.

19. HOLD HARMLESS: Tenant shall hold Landlord harmless from any liability or expenses for loss, injury, death, or damage to any person or property from any causes whatsoever which may at any time be suffered or sustained by Tenant, or invitees or any persons who may at any time be using, occupying, or visiting the demised premises.
20. RULES. Landlord may make additional reasonable rules governing the use and occupancy of the Premises and the building in which they are located, and Tenant hereby agrees to comply with such rules, provided that Landlord provides Tenant with a copy of such rules. Failure to comply with such rules shall constitute a default under this Lease.
21. FIREARMS: ***[Agency to insert their own specific rules regarding firearms, if any, here. If none, insert "Intentionally Omitted."]***
22. ASSIGNMENT: Tenant shall not assign this Agreement or sublet the Premises without the written consent of Landlord.
23. ELECTRONIC COMMUNICATIONS: Tenant agrees that Landlord may provide or deliver through electronic means:
 - a. A copy of the Lease Agreement and documents related to the Lease Agreement.
 - b. Advance notice of entry for purposes of sections 10 and 14 of this Lease Agreement.
24. ATTACHMENTS:
 - a. Attachment A, Required Duties
 - b. Attachment B, Tenant Rules
 - c. Attachment C, Disclosure of Information on Lead-Based Paint and/or Lead-Based Paint Hazards.
25. NOTICE OF DOMESTIC ABUSE PROTECTIONS:
 - a. As provided in section 106.50 (5m) (dm) of the Wisconsin statutes, a tenant has a defense to an eviction action if the tenant can prove that the landlord knew, or should have known, the tenant is a victim of domestic abuse, sexual assault, or stalking and that the eviction action is based on conduct related to domestic abuse, sexual assault, or stalking committed by either of the following:
 - i. A person who was not the tenant's invited guest.
 - ii. A person who was the tenant's invited guest, but the tenant has done either of the following:
 1. A person who was not the tenant's invited guest.
 2. A person who was the tenant's invited guest, but the tenant has done either of the following:
 - a. Sought an injunction barring the person from the premises.
 - b. Provided a written statement to the landlord stating that the person will no longer be an invited guest of the tenant and the

tenant has not subsequently invited the person to be the tenant's guest.

- b. A tenant who is a victim of domestic abuse, sexual assault, or stalking may have the right to terminate the rental agreement in certain limited situations, as provided in section 704.16 of the Wisconsin statutes. If the tenant has safety concerns, the tenant should contact a local victim service provider or law enforcement agency.
- c. A tenant is advised that this notice is only a summary of the tenant's rights and the specific language of the statutes governs in all instances.

Landlord shall provide Tenant with a copy of this Lease Agreement and all Attachments. Landlord shall give Tenant a check-in sheet on or before commencement of the tenancy. NOTE: SIGNING THIS LEASE AGREEMENT CREATES LEGALLY ENFORCEABLE RIGHTS. TENANT SHOULD CONSULT LEGAL COUNSEL REGARDING QUESTIONS AS TO THEIR LEGAL RIGHTS UNDER THIS LEASE AGREEMENT. THIS LEASE AGREEMENT INCLUDES THE ATTACHMENTS NOTED ABOVE, WHICH ARE HEREBY INCORPORATED BY REFERENCE.

In witness hereof, the parties have executed this Lease Agreement.

LANDLORD: _____

Date: _____

TENANT: _____

Date: _____