

Internal Audit Services for Real Estate

In the present economic environment, there are a number of indicators showing that internal control should receive an increased focus; first a slow-down in business in the real estate sector, with a stabilisation of investment portfolios and development projects put on hold resulting in a greater focus on asset management and property management activities. Then, there is an incentive to trim costs and to ensure that activities are well under control in order to mitigate brand and reputation risk, as well as increased financial risks for landlords following tenant defaults and/or large incentives granted to tenants to extend their leases and finally we observe a need to strengthen investor confidence and trust.



Your challenges in the property sector

As a property company, there are some specific challenges you need to address:

- An investment portfolio in real estate properties located in different jurisdictions;
- Outsourcing of services to a number of different third party service providers;
- Different types of real estate properties including office buildings, shopping malls, hospitality industry and development projects;
- A need to manage risks such as compliance, health & safety regulations, business conduct, physical security and information security across different locations;
- A need to assess risks in diverse and remote geographical locations requiring the necessary local language skills and understanding of local culture;
- The forthcoming AIFM directive which will require to have in place documented internal systems of management and control complying with EU standards.

Our added value

We have listed below some of the benefits we provided to property companies, when those companies relied on PricewaterhouseCoopers to perform internal audits:

- An experienced central team combining internal audit experience with a broad knowledge of the different types of real estate properties;
- A top down analysis by a core team of experts, encompassing risk assessments related to a specific property and location, and with multilingual capabilities;
- A benchmarking of third party service providers used in different locations;
- A proven and consistent internal audit methodology and approach;
- Authority to deploy resources anywhere in the world;
- Access to local compliance rules and culture.

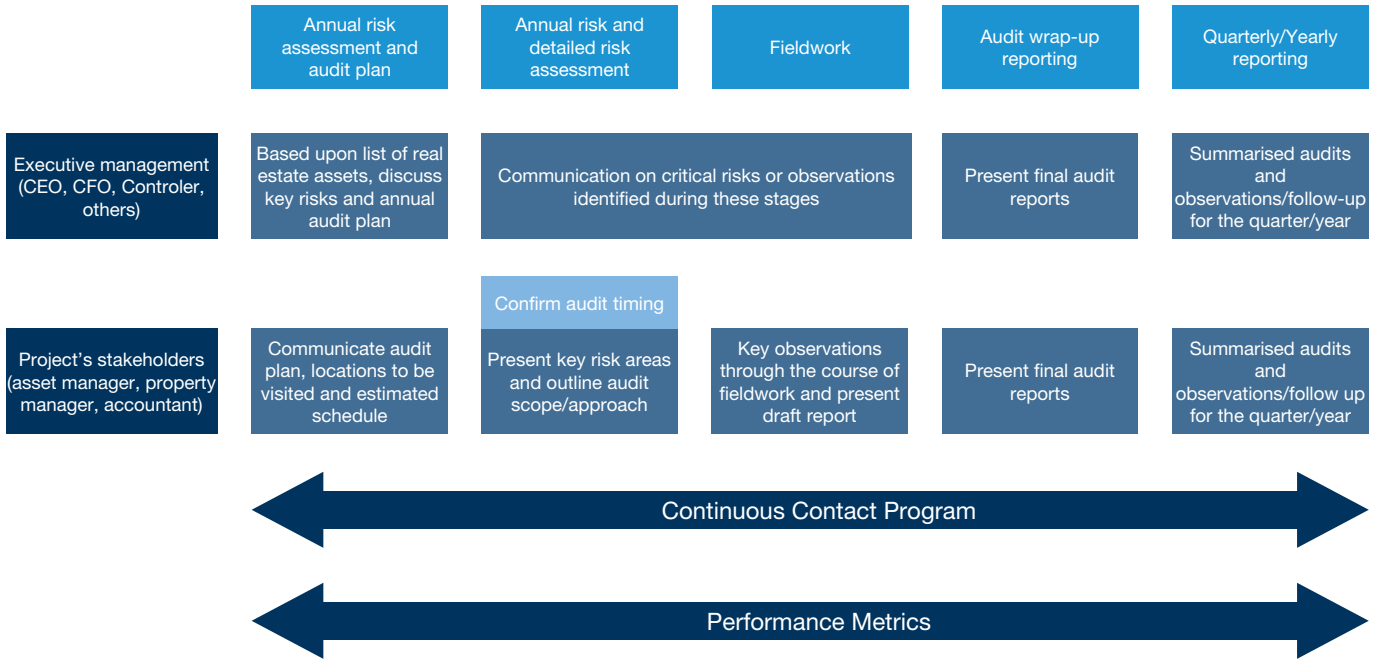
Typical risks and potential impacts

Below you will find a list of typical risk factors for real estate structures which outsource functions to third parties, and which we identified in asset management companies (“AM”) and property management companies (“PM”). The relevance of those risk factors is to be tailored to the operating environment of the property companies.

Risk	AM	PM	Impact of failure
Control environment			
Policies and procedures specific to each property do not exist	X	X	<ul style="list-style-type: none"> • Roles and responsibilities not clearly defined • Management decisions made on inaccurate/incomplete data • Exposure to fraud or error • Loss of reputation and customers • Decrease in property value due to inadequate maintenance
Reporting deliverables are not clearly defined and/or inconsistent	X	X	
Inadequate procedures in terms of segregation of duties, delegations of authority and approval limits	X	X	
Outstanding litigation and/or customer complaints are not communicated or properly evaluated	X	X	
No maintenance plan is in place/monitored		X	
Financial reporting			
Significant variations between budget and actual are not sufficiently explained	X	X	<ul style="list-style-type: none"> • Lack of transparency • Exposure to accounting errors • Regulation/brand risk
Key reconciliations are not prepared and/or reviewed	X	X	
Manual adjustments are not reviewed/authorised	X	X	
Income			
Pricing strategy is not clearly defined and/or applied	X		<ul style="list-style-type: none"> • Reduced margins • Exposure to tenant damages • Litigation costs incurred • Cash flow leakage
Non-standard terms for leases are not pre-approved	X		
Properties are inadequately insured	X	X	
Contract terminations result in claims and disputes	X	X	
Credit checks for new tenants prove to be inadequate	X	X	
There are significant overdue balances with tenants	X	X	
Expenditures			
No adherence to capital expenditure procedures for acquisitions and/or disposals	X	X	<ul style="list-style-type: none"> • Expenses exceed budgets without adequate explanations • No cost optimisation • Unauthorised expenses • No optimal use of suppliers
Development projects are not supported by adequate budgets/cost monitoring	X		
Supplier invoices for operating expenses are not authorised and/or matched to service orders	X	X	
Formal tendering procedures are not adhered to	X	X	
Vendor pricing and performance is not monitored	X	X	
Compliance			
AM & PM agreements are not regularly reviewed	X	X	<ul style="list-style-type: none"> • Loss of reputation • Exposure to litigation
Bonus and incentive schemes to sales staff are not genuine	X		
Cash management			
Cash flow is not adequately budgeted/monitored	X	X	<ul style="list-style-type: none"> • Cash flow is not optimised • Unauthorised payments
There are no regular reconciliations for key bank accounts	X	X	
Authorised signatures are not up-to-date	X	X	
Health & Safety			
H&S policies and procedures are not well defined		X	<ul style="list-style-type: none"> • Loss of reputation • Exposure to fines
H&S objectives are not set and measured		X	
IT Controls			
Users’ access rights are not adequate and/or regularly reviewed	X	X	<ul style="list-style-type: none"> • Inaccurate reporting • Manipulation of data • Loss of data
The DRP/BCP is not updated and/or tested at regular intervals	X	X	
There is no full back-up on a daily basis	X	X	

Our service process overview

You will find below an example of a service process overview. This can be tailored to specific client needs.



Example from the field

An investment fund has a broad range of property investments located in over 20 different countries in various parts of the world, and which include a wide range of investments such as retail shopping centres, commercial properties, hotels and residential apartments.

We have built a team consisting of a global coordination team in Luxembourg, overseeing regional teams to cover the investment properties located in the different countries. We perform internal audits of the properties on a rotational basis, using a multi-year audit plan. We refer to a common framework of audit programs, which is subsequently tailored to the nature of the property and the local environment. Our team combines internal audit and real estate experts.

How can PricewaterhouseCoopers help?

An independent internal audit will provide you with a fresh, independent assessment of your properties. Our reviews may indicate weaknesses but will also provide suggestions on ways to improve and change.

PricewaterhouseCoopers allows you to benefit from:

- A team of experts that is well grounded in both internal audit services and the real estate sector and abreast of any related challenges;
- Industry experience and specialist skills. With our leading industry practice in real estate, your internal audit team has ready access to relevant resources within the real estate industry.

Why PricewaterhouseCoopers Luxembourg?

PricewaterhouseCoopers Luxembourg (www.pwc.com/lu) has nearly 2,000 professionals from 53 different countries. PricewaterhouseCoopers (www.pwc.com) provides industry-focused assurance, tax and advisory services to build public trust and enhance value for our clients and stakeholders. More than 163,000 people in 151 countries across our network share their thinking, experience and solutions to develop fresh perspectives and practical advice.

Your contacts:

Kees Hage	Partner, Real Estate	+352 49 48 48 2059	kees.hage@lu.pwc.com
Vincent Villers	Partner, Internal Audit Services Leader	+352 49 48 48 2367	vincent.villers@lu.pwc.com
Robert Castelein	Director, Internal Audit/Real Estate	+352 49 48 48 2159	robert.castelein@lu.pwc.com

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