Ms. Kim Day, Manager
Department of Aviation
City and County of Denver

Dear Ms. Day:

Attached is the Auditor’s Office Audit Services Division’s performance audit report examining the Department of Aviation’s (Department) Revenue Management and Business Development Division (RMBD). The audit period was for June 30, 2007 through June 30, 2008. The purpose of the audit was to examine and assess RMBD to identify possible inefficiencies or weaknesses. The audit focused primarily on RMBD’s activities related to their airport contract oversight and space management practices.

Audit work identified some internal control weaknesses and limited oversight practices that hinder the Department’s ability to effectively monitor airport contracts and manage space.

If you have any questions, please call Kip Memmott, Director of Audit Services, at 720-913-5029.

Sincerely,

Dennis J. Gallagher
Auditor

May 21, 2009

cc: Honorable John W. Hickenlooper, Mayor
Honorable Members of City Council
Members of Audit Committee
Kelly Brough, Chief of Staff
Claude Pumilia, Chief Financial Officer
David T. Roberts, Chief Services Officer
David Fine, City Attorney
Lauri Dannemiller, City Council Executive Staff Director
Beth Machann, Controller

To promote open, accountable, efficient and effective government by performing impartial reviews and other audit services that provide objective and useful information to improve decision making by management and the people. We will monitor and report on recommendations and progress towards their implementation.
# TABLE OF CONTENTS

- Transmittal Letter .................................................. 1
- Table of Contents .................................................. 2
- Auditor’s Report ...................................................... 3
- Executive Summary .................................................. 4
- Background, Scope, Objective, and Methodology ............... 5
- Findings and Recommendations .................................... 8
- Exhibit A - Agency Response ...................................... 13
AUDITOR’S REPORT

We have completed an audit of the Department of Aviation’s (Department) Revenue Management and Business Development Division (RMBD) for the period June 30, 2007 through June 30, 2008. The purpose of the audit was to examine and assess the RMBD to identify possible inefficiencies and opportunities for improvement. Audit work focused primarily on RMBD’s activities related to their airport contract oversight and space management practices. This performance audit is authorized pursuant to the City and County of Denver Charter, Article V, Part 2, Section 1, General Powers and Duties of Auditor and was conducted in accordance with generally accepted government auditing standards.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The audit revealed some internal control weaknesses in the RMBD. The weaknesses identified within the accompanying report, hinder the Department’s ability to monitor airport contract oversight and space management practices.

We commend the Department for taking action to review its processes in this area. We also extend our appreciation to the Manager of Aviation and personnel who assisted and cooperated with us during the audit.

Audit Services Division
Kip R. Memmott, MA, CGAP, CICA
Director of Audit Services

Date: May 21, 2009

Staff: John Carlson, CIA, CICA, Deputy Director
Marcus Richardson, CICA, Internal Audit Supervisor
Adeniyi Kelani, Ph.D., CICA, Lead Internal Auditor
Kristin Donald, Senior Internal Auditor

To promote open, accountable, efficient and effective government by performing impartial reviews and other audit services that provide objective and useful information to improve decision making by management and the people. We will monitor and report on recommendations and progress towards their implementation.
Opportunities Exist to Improve DIA Space and Contract Management Practices

Audit work determined that the Revenue Management and Business Development Division (RMBD) does not have an effective control framework in place to address contract oversight and space management. Our audit methods identified two general areas of deficiency. Five audits issued by the Auditor’s Office over the last two years have identified similar internal control weakness related to DIA contract administration. We offer recommendations for resolving these long-standing control deficiencies.

Weaknesses with Space Management Practices - Audit work determined that the RMBD does not have a plan to monitor and utilize space. RMBD was unable to provide listings of all available storage and office spaces located in the airport terminal complex. The audit encountered some contracts with expiration date discrepancies between the RMBD database and the original contract. The Department of Aviation (Department) is in the process of developing written procedures and a strategic plan for space utilization at DIA. The Department can utilize the Merchandise Plan to help identify all tenant shop spaces.

Weaknesses with Contract Management Practices - The Department does not adequately monitor and renew contracts on a timely basis. Audit work determined that the RMBD rarely reviews for contract compliance with the monthly concession reports and other financial data provided by airport tenants. Moreover, audit work determined several problems regarding the contract management of an oil and gas well agreement.

Recommendations - In order to fully comply with the Mayor’s Executive Orders and the City Charter regarding contract responsibilities, strengthen operations at the airport, and maximize revenues, we recommend that the Department accurately assess space utilization and create a plan to maximize revenue. In addition, we recommend RMBD create written procedures for contract management processes.
Background

Pursuant to the City Charter, the Department is responsible for managing the development, promotion, and accommodation, of air commerce, air travel and air transportation for Denver International Airport (DIA). This responsibility includes maintaining buildings, structures, terminals, parking and ground transportation facilities, roadways, land, hangers, warehouses, runways, shops, hotels, motels and administrative offices at DIA. The Department is organized in the following manner to execute the aforementioned management functions:

- Engineering Division
- Finance and Administration Division
- Maintenance Division
- Operations/Public Safety/Security Division
- Planning and Development Division
- Public Relations and Marketing Division
- Revenue Management and Business Development Division
- Technologies Division

Audit work focused on RMBD management activities as they relate to contract oversight and space utilization practices.

Revenue Management and Business Development Division

RMBD is responsible for maximizing revenues from airport tenants. The table below illustrates some of the amounts of operating revenues generated for each activity for 2006 and 2007:

<table>
<thead>
<tr>
<th>Activity</th>
<th>2007</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Facility rentals</td>
<td>$205,638,720</td>
<td>$197,353,089</td>
</tr>
<tr>
<td>Concession Fees</td>
<td>$40,598,943</td>
<td>$34,304,468</td>
</tr>
<tr>
<td>Parking Revenues</td>
<td>$116,326,036</td>
<td>$110,534,937</td>
</tr>
<tr>
<td>Car Rental Revenues</td>
<td>$44,998,289</td>
<td>$41,641,365</td>
</tr>
<tr>
<td>Landing Fees</td>
<td>$87,281,898</td>
<td>$91,389,849</td>
</tr>
<tr>
<td>Other Sales and Charges</td>
<td>$11,921,704</td>
<td>$11,871,715</td>
</tr>
</tbody>
</table>

RMBD is comprised of the following three sections:

**Concessions Management** - This section is responsible for contract administration for news and general merchandise, food and beverage, vending machines and news racks, and consumer service operations at DIA. This section of RMBD has two subsections. One subsection is responsible for the Request for Proposal process, business development, and creates new concession revenue opportunities at DIA. The other subsection is responsible for contract administration and it monitors concession operations including pricing, customer service and contract compliance.

**Property Management** - This section is responsible for contract administration for airlines, airline services, air cargo, car rental operations, farming, oil and gas wells, and airport real estate.

**Landside Service** - Landside services has oversight responsibility for airport parking contracts, parking revenue-control maintenance agreements, towing contracts, and employee parking. Another function of this section is the oversight of the ground transportation unit. The ground transportation unit is responsible for the commercial vehicle access to the terminal. Other duties of Landside Service include monitoring and maintenance of change machines.

RMBD performs the aforementioned responsibilities of the Department as well as space management functions at DIA. Contracts typically contain the following types of requirements:

- **Space Provisions** - These provisions identify the area tenants will occupy, space utilization, area maintenance.

- **Compensation Provisions** - These provisions describe payment arrangements, payment due dates, a brief description of gross revenues, and reporting requirements.

- **Liability Provisions** - These provisions describe insurance and performance bonds requirements.

- **Operations Provisions** - These provisions identify the signage, hours of operation, description of operations, and pricing of products.

- **Other Provisions** - Other requirements can include renovations and refurbishments, environmental requirements, and other industry specific requirements.

**City Contract Requirements**

The City Charter requires its tenants to have written agreements to operate at the airport. Specifically, Section 5-13 subsection (a) of the City Charter states:

“It shall be unlawful for … any person to conduct any business or concession upon Denver Municipal Airport System … without first obtaining a written permit from the manager of aviation issued pursuant to rules and regulations of operation, management and control of the airport,
or alternatively receiving a written contract from the manager of aviation.”
The Department also has the authority to adopt its own rules and regulations, which contain the schedule of fees the airport receives for space, usage, fee revenue, and other miscellaneous charges.

Executive Order No. 8 states that the responsibilities of the Initiating Authority of a contract include:

- Ensure that the terms of the contract are met.
- Monitor the contract for the life of the contract.
- Ensure that the bonding and insurance requirements continue to be met throughout the life of the contract.
- Report contract performance as required.

**Audit Scope**

The purpose of this audit was to review the efficiency and effectiveness of RMBD’s management activities as they relate to contract oversight and space management practices during the audit period of June 30, 2007 through June 30, 2008.

**Audit Objective**

To determine whether RMBD’s contract and space oversight practices are adequate to detect and deter non-compliance with contract provisions, City Charter, and departmental rules.

**Audit Methodology**

We utilized multiple methodologies to achieve audit objectives. These evidence gathering and analysis techniques included, but were not limited to:

- Interviewing RMBD personnel to understand procedures;
- Interviewing representatives of companies operating at DIA;
- Reviewing reports from the contract management system and accounting system;
- Reviewing contracts and comparing them to the contract management software system for accuracy;
- Surveying PROPworks® users at other airports;
- Testing controls for contract compliance and enforcement; and
- Verifying and recalculating compensation percentages, rentals and fees.
Finding: Opportunities Exist to Improve DIA Space and Contract Management Practices

The City Charter requires written agreements to operate at the airport. RMBD manage these written agreements and the use of airport property with the goal of monitoring and maximizing revenue. Contract and space monitoring is critical to ensuring that contractors fulfill all of their legal obligations to the City and to ensure proper use of City assets. Executive Order No. 8 states:

“Contracts are considered of the highest administrative priorities within the City. While exercising prudent judgment, all Department and Agency Heads are to expedite the processing of contracts. Each Department or Agency must develop a system to track contracts from initiation through execution and ensure contract compliance throughout the life of the contract.”

However, audit work identified significant weaknesses regarding RMBD’s contract and space management and oversight practices and processes as described below. Five audits issued by the Auditor’s Office over the last two years have identified similar internal control weakness related to DIA contract administration.

Weaknesses with Space Management Practices - Audit work identified the following limitations with DIA’s current space management activities.

- **Lack of information available to manage space** - RMBD does not have a plan to utilize space and was unable to provide listings of all available storage and office spaces located in DIA’s terminal complex. Currently, the Department of Aviation (Department) is working on a space utilization plan to catalogue tenant space. The plan should help to ensure proper monitoring of contract expiration dates in order to generate accurate tenant vacancy reports. The Department’s existing Merchandise Plan\(^1\) could be used to help identify all tenant shop spaces.

- **Inadequate process to monitor contract expiration dates** - Audit work determined RMBD does not effectively monitor and update contracts to ensure that all contracts are current and in full compliance with City requirements. For example, audit test work revealed that one of ten randomly selected tenants reviewed were occupying DIA space under an expired contract. RMBD personnel were unaware of this issue. Additionally, we randomly tested twenty contracts contained in PROPworks\(^2\) database and compared that database information with the original contract. Of the twenty contracts selected, we found three contract expiration discrepancies between the PROPworks\(^2\) database and the original contract. Details of the discrepancies are as follows:

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\(^1\) The Merchandise Plans is separate from the Space Utilization Plan. The Merchandise Plan identifies all shop space in the DIA Terminal Complex.

\(^2\) PROPworks\(^2\) is a comprehensive software program DIA uses to manage revenue contracts and airport property (www.Airlt.com).
Table 2: Contract Expiration Date Discrepancies

<table>
<thead>
<tr>
<th>Tenant Name</th>
<th>Original Contract Expiration Date</th>
<th>PROPworks® Expiration Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Concessions Denver, LLC</td>
<td>2010</td>
<td>2014</td>
</tr>
<tr>
<td>F &amp; B Concessions LLC</td>
<td>2003</td>
<td>2015</td>
</tr>
<tr>
<td>Concessions Denver, LLC</td>
<td>2011</td>
<td>2007</td>
</tr>
</tbody>
</table>

Issues with DIA space management practices have been identified by several recent audits performed by our Office as illustrated below:

- CA Concessions of Colorado, Inc. - In 2008, the Office of the Auditor issued an audit of CA Concessions of Colorado, Inc. Audit work determined that CA Concessions occupied space without written agreements for several years. The audit also revealed that RMBD did not have written procedures for governing this area.

- Airport Management Services, LLC - In 2008, the Office of the Auditor also issued an audit of Airport Management Services, LLC (AMS). Audit work determined that AMS operated at DIA under expired contracts for several years. DIA failed to detect this inaccurate contract data in PROPworks® resulting in weaknesses with contract monitoring process.

**Weaknesses with Contract Management Practices** - Based on our audit work we determined a lack of review and contract enforcement regarding gross revenue reporting.

- **Concessions** - Concessionaires that operate at the airport pay rent based on a percentage of their gross revenue. They must submit monthly concession reports and other financial data. The reports and data are rarely reviewed for compliance by RMBD. For example, annual statements are not required to be certified by an independent CPA if they participate in the daily revenue program that includes 137 of the 180 concession contracts. In addition, as noted in the Datascape audit issued by the Auditor’s Office in 2008, 19 of the 137 concessionaires submitted their annual statement late and the Department did not charge the required $100 a day late fee, totaling $15,400. In the Airport Concessions audit issued in 2008, the contract requirement for a CPA certification for the late submission of their annual statement was not enforced. The audit found that the company had several computation errors in their annual statements. The company also submitted their statements late. In addition, an independent CPA as required by the contract did not prepare the statements.

- **Airline Services** - Audit work found a lack of contract enforcement for gross revenue reporting for an airline service operator. The company’s annual statement was not certified by an independent CPA and was submitted 178 days late, totaling $17,800. The operator was not assessed any late fees. With this lack of enforcement, RMBD cannot confirm whether an operator is properly reporting gross revenue.
- **Car Rentals** - Audit work also determined that RMBD could not produce the annual statement for 2007 for two of the three car rental companies selected for testing. The 2007 Thrifty Rent-A-Car System and the 2006 Budget Rent-A-Car System audits both noted that the annual statement was not submitted by the contractual due date.

- **Lack of Internal Controls Over Cash Receipts and Contract Enforcement for Oil and Gas Wells** - Audit work found several problems regarding the contract management of the Petro-Canada oil and gas well agreement. An audit issued by the Auditor’s Office in 2004 revealed similar contract administration weaknesses with a different DIA oil and gas agreement.

  - **The contract lacks a specific due date for royalty payments** - The due dates for monthly royalty payments are not clearly determinable in the Petro-Canada contract. The contract states 15% of gross wellhead value of lease substances are payable monthly. It is difficult to determine late payment penalties or support any interest charges without a specific due date.

  - **Petro-Canada payments were submitted to an inappropriate division** - Petro-Canada payments were being submitted to the RMBD contract administrator. As a result of our audit observation, RMBD has stopped this process. Currently, payments are being submitted directly to the cashier’s office.

  - **Billings are not prepared for payments** - The Department does not bill Petro-Canada and therefore payments are recorded on a cash basis. This is contrary to Governmental Generally Accepted Accounting Principles (GAAP). GAAP requires revenue be recorded when it is earned.

  - **Miscalculation regarding the minimum annual royalty amount** - During the course of our audit, RMBD miscalculated the minimum annual royalty amount for the year 2007. RMBD informed us that the annual minimum royalty was $22,400. However, according to the contract, the annual minimum royalty should have been $133,392.

  - **Annual statements could not be located** - According to the contract, Petro-Canada is required to submit its annual statement no later than February 28 of every year. RMBD could not provide us with the 2007 annual statement.

Similar findings and recommendations identified in 2004 involving an audit of Prima Oil & Gas operations still require implementation.

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3 Car rental operations are exempt from having one of their annual statements certified by an independent CPA and there are no contract penalties for late submission.

4 Audit of Prima Oil and Gas Agreement (June 2004).
Several Factors Contribute to Space and Contract Management Weaknesses

- RMBD has not assessed the space available at DIA.

- RMBD lacks written policy and procedures for space and contract management.

- Contracts are not specifically assigned to a contract administrator that enforces all requirements.
  - The assignment of a contract administrator for car rentals companies occurred during our audit work.
  - The contract administrator for the oil and gas wells monitors only payments and no other contract requirements.
  - RMBD staff collects annual statements instead of the in-charge contract administrator.

- Contract administrators do not consistently maintain documentation of their contract monitoring activities, or interactions with contractors.

- Some contract administrators use paper files for documentation; others use PROPworks®.

- There are issues with PROPworks® security
  - Lack of robust password requirements
  - Inadequate maintenance of user accounts and user account permissions

Inability to Effectively Manage Space and Contracts has Several Negative Impacts

- RMBD cannot utilize space for the greatest return.

- Inability to identify expiring and expired contracts leads to legal liability exposure for the City.

- RMBD is not currently maximizing revenue when contracts expire with a holdover clause.

- Poor contract enforcement can lead to a loss of revenue and missed fees and fines.

- Inadequate access controls over PROPworks® diminish the reliability of computerized data and increase the risk of destruction or inappropriate disclosure of data.
Recommendations

In order to fully comply with the Mayor’s Executive Order and the City Charter regarding contract responsibilities, strengthen operations at the airport, and maximize revenues, we offer the following recommendations. These recommendations are similar to those contained in five different audits issued over the last two years involving DIA space and contract management practices.⁵

1. Develop a plan and procedures for space utilization, including the following:
   - Accurately catalogue all tenant space.
   - Monitor contract expiration dates.
   - Reconcile PROPworks® information to original contracts.
   - Generate timely and accurate tenant vacancy reports.

2. Develop written procedures and train staff on those procedures for contract administration for all industry types operating at the airport including the following:
   - Processes for documentation requirements from the initiation of a contract until contract expiration
   - Assignment of a contract administrator for all contracts
   - Rigorous enforcement of contract compliance with monitoring by the Airport Manager when necessary
   - Processes for reviewing and enforcing compensation calculation, monthly gross revenue reporting and submitting annual statements
   - Enhance PROPworks® controls

3. Amend the oil and gas contract to provide specific payment due dates.

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⁵ These audits include: CA Concessions (July 2008), Airport Management Services (October 2008), Airport Concessions (October 2008), Thrifty Rent A Car System (October 2008), and Budget Rent A Car (December 2007).
Audit Response Letter Template

May 14, 2009

Mr. Kip R. Memmott, MA, CGAP, CICA
Director of Audit Services
Office of the Auditor
City and County of Denver
201 West Colfax Avenue, Dept. 705
Denver, Colorado 80202

Dear Mr. Memmott:

The Office of the Auditor has conducted a performance audit of the Revenue Management Business Development Division Performance Audit for the audit period June 30, 2007 through June 30, 2008.

This memorandum provides a written response for each reportable condition noted in the Auditor’s Report final draft dated April 23, 2009. This response complies with Section 20-276 (b) of the Denver Revised Municipal Code (D.R.M.C.).

Before addressing the specific findings of the audit, there is a statement in the audit report that needs to be expanded: “RMBD is responsible for maximizing revenues from airport tenants” (page 4 of the report). While it is true that RMBD does work to maximize revenues, there are other objectives that we must take into consideration in making decisions regarding tenants, two examples of which are the customer experience and building strong partnerships with the tenants. The development and enforcement of leases considers many other aspects of the business in addition to revenue maximization.

AUDIT FINDING:
Opportunities Exist to Improve DIA Space and Contract Management Practices

RECOMMENDATION 1:

Develop a plan and procedures for space utilization, including the following:

- Accurately catalogue all tenant space
- Monitor contract expiration dates
- Reconcile PROPworks® information to original contracts
Generate timely and accurate tenant vacancy reports

RESPONSE/ACTION PLAN:

| State your agreement or reason for disagreement with Recommendation | Target date to complete implementation activities (Generally expected within 60 to 90 days) | Name and phone number of primary individual responsible for implementation |
|---------------------------------------------------------------|------------------------------------------------------------------------------------------------|%--------------------------------------------------------------------------|
| RMBD is in agreement with this finding                        | December 31, 2009                                                                               | Patrick Heck (303) 342-2207                                               |

An accurate catalogue is possible through PROPworks®. We will check data and functionality of the system to generate these reports in the future, including vacancy reports for space that was formerly under lease. RMBD will use PROPworks® to monitor expiration dates and will reconcile PROPworks® to information in the leases. Due to the large number of contracts and other projects currently underway, RMBD needs until the end of the year to complete this task.

RECOMMENDATION 2:

Develop written procedures and train staff on those procedures for contract administration for all industry types operating at the airport including the following:

- Processes for documentation requirements from the initiation of a contract until contract expiration
- Assignment of a contract administrator for all contracts
- Rigorous enforcement of contract compliance with monitoring by the Airport Manager when necessary
- Processes for reviewing and enforcing compensation calculation, monthly gross revenue reporting and submitting annual statements
- Enhance PROPworks® controls

RESPONSE/ACTION PLAN:
EXHIBIT A – DEPARTMENT OF AVIATION RESPONSE

<table>
<thead>
<tr>
<th>RMBD is in agreement with this finding with one exception (see below)</th>
<th>(Generally expected within 60 to 90 days)</th>
<th>Concessions: Bryan Touchstone (303) 342-2501</th>
<th>Properties: John Ackerman (303) 342-2568</th>
</tr>
</thead>
<tbody>
<tr>
<td>December 31, 2009 for policies and procedures. Others are already complete or will be completed as noted below.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Jefferson Wells has been hired to complete the task of documenting policies and procedures. Concessions is approximately 80% complete with this task and Properties has started initial planning for this. (Landside Services was done over a year ago.) We have now assigned all Properties and Concessions contracts to a specific administrator, who is responsible for all contract compliance, including all material terms in the contract. These assignments may need to change from time to time, but we will ensure appropriate training for all individuals responsible for this. (Note that there are revenue contracts administered by other divisions at DIA, and other divisions are responsible for the actual collection of revenues from the tenants.) Assignment of a contract administrator will allow for enforcement of material contract provisions, which includes responsibilities from other divisions for portions of this enforcement such as collections. We disagree with the concept of monitoring by the Airport Manager as that implies involvement in a level of detail that is the responsibility of RMBD. We agree that controls need to be strong on PROPworks® and will do an initial review of access levels to determine if they are appropriate and will do this review on a periodic basis. We will also implement an access approval process in conjunction with IT.

RECOMMENDATION 3:

Amend the oil and gas contract to provide specific payment due dates.

RESPONSE/ACTION PLAN:

<table>
<thead>
<tr>
<th>State your agreement or reason for disagreement with Recommendation</th>
<th>Target date to complete implementation activities (Generally expected within 60 to 90 days)</th>
<th>Name and phone number of primary individual responsible for implementation</th>
</tr>
</thead>
<tbody>
<tr>
<td>RMBD is in disagreement with this finding</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

We cannot unilaterally make this change to the contract. The contract payment provisions are standard for oil/gas in this area, and are also influenced by existing state regulations governing timely submittal of
production reports. Payment has been timely in the past, and we do not believe there is a pressing need to amend the contract. If an opportunity presents itself to amend the agreement as part of a broader negotiation RMBD will consider this item when evaluating the entire contract.

Please contact Patrick Heck at (303) 342-2207 with any questions. We sincerely appreciate the efforts of the Auditor’s staff and thank them for their time and professionalism.

Sincerely,

[Signature]

Patrick Heck
Deputy Manager of Aviation
Revenue and Business Development

cc: Kim Day, Manager of Aviation
Les Berry, Acting Deputy Manager of Aviation, Technologies
Stan Koniz, Deputy Manager of Aviation, Finance and Administration
John Ackerman, Assistant Deputy Manager of Aviation, Properties
Bryan Touchstone, Assistant Deputy Manager of Aviation, Concessions
Mary Buckley, Director of Government Affairs
Brian Elms, Assistant Director of Government Affairs