

Denver International Airport Concessions Management Follow-up Report

September 2015

Office of the Auditor
Audit Services Division
City and County of Denver



Timothy M. O'Brien, C.P.A.
Auditor

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City and County of Denver

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Timothy M. O'Brien, C.P.A.
Auditor

September 30, 2015

Ms. Kim Day, Manager of Aviation
Department of Aviation
City and County of Denver
Re: Audit Follow-Up Report

Dear Ms. Day:

In keeping with professional auditing standards and the Audit Services Division's policy, as authorized by D.R.M.C. § 20-276, our Division has a responsibility to monitor and follow-up on audit recommendations to ensure audit findings are being addressed and to aid us in planning future audits.

This report is to inform you that we have completed our follow-up effort for the Denver International Airport (DIA) Concessions Management audit issued February 20, 2014. Our review determined that DIA personnel have implemented seven of the sixteen recommendations made in the audit report. In total, five of the remaining nine recommendations are dependent on DIA finalizing a key document relevant to concessions management—Rule 45. At the time of this report, relevant revisions had been made to the document, but DIA had not yet issued a final version of the document. With regard to the other four outstanding recommendations, two are still in progress, and requested data was not provided to verify the implementation of the other two. Accordingly, auditors determined that the risk associated with the audit team's initial findings has not been fully mitigated. As a result, the Division may revisit these risk areas in future audits to ensure appropriate corrective action is taken.

For your reference, this report includes a Highlights page that provides background and summary information on the original audit and the completed follow-up effort. Following the Highlights page is a detailed implementation status update for each recommendation.

This concludes audit follow-up work related to this audit. I would like to express our sincere appreciation to you and to Department personnel who assisted us throughout the audit and follow-up process. If you have any questions, please feel free to contact me at 720-913-5029 or Sonia Montano, Internal Audit Supervisor, at 720-913-5157.

Sincerely,

A handwritten signature in black ink, appearing to read "K. Memmott".

Kip Memmott, MA, CGAP, CRMA
Director of Audit Services

KRM/sm

*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.*

cc: Honorable Michael Hancock, Mayor
Honorable Members of City Council
Members of Audit Committee
Ms. Cary Kennedy, Deputy Mayor, Chief Financial Officer
Ms. Janice Sinden, Chief of Staff
Mr. David P. Edinger, Chief Performance Officer
Ms. Beth Machann, Controller
Mr. Scott Martinez, City Attorney
Ms. Janna Young, City Council Executive Staff Director
Mr. L. Michael Henry, Executive Director, Board of Ethics
Mr. Bhavesh Patel, Chief Revenue Officer, Aviation
Mr. Neil Maxfield, Senior Vice President – Concessions, Aviation
Ms. Gisela Shanahan, Chief Financial Officer, Aviation

REPORT HIGHLIGHTS



Denver International Airport Concessions Management Follow-up Report: September 2015

Denver International Airport has implemented seven of the sixteen recommendations made in the February 2014 audit report.

Background

In 2012, Denver International Airport (DIA) concessions generated nearly \$250 million in revenue, of which nearly \$50 million was remitted to the airport. Concessions are selected through a competitive Request for Proposal (RFP) process governed by City rules, regulations, and airport policies & procedures. To grow concession revenue and improve performance, DIA management developed the Premium Value Concessions (PVC) Program. Through competition, the PVC Program awards top performers with the opportunity to enter into direct negotiations for new concession contracts in lieu of going through the RFP process.

Purpose

The purpose of our audit was to assess whether the PVC Program is meeting the established goal of encouraging concession revenue growth and if it is sufficiently administered in accordance with the governance of the PVC Program. We also sought to determine if the Request for Proposal process as it relates to the evaluation, scoring, and selection of concessionaire proposals is administered fairly and appropriately.

Highlights from Original Audit

Finding 1: DIA personnel and the third-party administrator tasked with implementing the PVC Program consistently adhere to Rule 45, which governs the PVC Program at DIA. However, based on our analysis, Rule 45 provisions do not ensure that top performing concessions are consistently identified due to ineffective scoring metrics and weaknesses with minor merchandising category provisions. As a result, there are inherent inequities with the program as currently designed.

Finding 2: The DIA Concession Policy is outdated and can be revised to better meet the goals of the concessions program. Based on our review of the Policy, the sections related to revenue reporting and the RFP Evaluation Committee membership need to be updated and enhanced to reflect actual practices and close identified gaps. Additionally, the section of the Policy regarding concentration of concession ownership was increased when a concessionaire exceeded the concentration percentage allowed by the policy.

Finding 3: DIA management and personnel are effectively communicating upcoming concession opportunities and requirements of operating a concession. However, we could not determine if the actual evaluation and scoring of proposals submitted under an RFP advertisement are fair and appropriate because DIA management and personnel do not maintain, document, or store individual evaluation committee member comments and scores for each proposal. City rules and regulations, in addition to DIA policies and procedures, should make it explicitly clear that all documents related to the evaluation and scoring of proposals under an RFP advertisement are maintained for future review.

Findings at Follow-up

While DIA has made key revisions to Rule 45, the document has not been finalized. Five of the outstanding recommendations are dependent on this document being approved and implemented. With regard to the other four outstanding recommendations, two are still in progress, and requested data was not provided to verify the implementation of the other two.

Recommendations: Status of Implementation

Recommendation	Auditee Action	Status
Finding 1: The Premium Value Concessions Program Should Be Modified to Fairly, Accurately, and Consistently Identify and Reward Top-Performing Concessions		
<p>1.1 Rule 45 Scoring Metrics – The Manager of Aviation should revise the financial scoring metrics outlined in Rule 45 to better align with the goals of the PVC Program.</p>	<p>Airport Concessions management worked with a group of concessionaire leaders to revise Rule 45 and the program’s financial scoring metrics. The agreed-upon revised metrics include a revised sales/sq. ft/allocated enplaning passenger metric, a revised sales/allocated enplaning passenger metric, and a single growth metric. The growth metric would be awarded to only the top 1/3 within a merchandise category. Rule 45 has not yet been finalized; when it is finalized, these new metrics will go into effect.</p>	<p>Agree/Not Implemented</p>
<p>1.2 Rule 45 Scoring Weight – The Manager of Aviation should revise the scoring weights as outlined in Rule 45 so that financial performance is at least equitable to customer service performance to better align with the goals of the PVC Program.</p>	<p>The agreed-upon Rule 45 revision included changing the scoring weights of the financial performance and the customer service performance metrics. The agreed-upon revised weights place a higher weight on financial performance than customer service performance. Rule 45 has not yet been finalized; when it is finalized, these new scoring weights will go into effect.</p>	<p>Agree/Not Implemented</p>
<p>1.3 Premium Value Concessions Program Data – The Manager of Aviation should ensure that the PVC Program Administrator and the third-party administrator use accurate data in administering and scoring concessions participating in the PVC Program.</p>	<p>As of the writing of the Audit, only a partial dataset existed of aircraft departures. Since then a full dataset has become available. Additionally, a quality control process is being developed and documented to ensure the use of accurate data. However, this process is not yet complete.</p>	<p>Agree/Not Implemented</p>

Recommendations: Status of Implementation

	Recommendation	Auditee Action	Status
1.4	Rule 45 Minor Merchandising Categories – The Manager of Aviation should revise Rule 45 to ensure that there is consistent competition in each minor merchandising category and concourse.	The agreed-upon Rule 45 revision includes revising the financial performance metrics such that there is more consistent competition in each minor merchandising category and concourse. Situations will no longer exist where a concession will not have competitors for financial performance monthly points. Rule 45 has not yet been finalized; when it is finalized, these new metrics will go into effect.	Agree/Not Implemented
1.5	Rule 45 Program Benefit – The Manager of Aviation should revise Rule 45 to ensure that no more than the top-performing one-third of concessions are eligible for future Program Benefit.	The discussed Rule 45 revision includes a tightening of program benefit award recipients: Rounding up of monthly point recipients and program benefit recipients have been eliminated, concessions' scoring pool inclusion have been reduced after a concession's closure, and the program's Subjective Appeal will be replaced by an Extenuating Circumstances appeal.	Agree/Not Implemented
1.6	Rule 45 Evaluation – The Manager of Aviation should formally assess the effectiveness of Rule 45 and the PVC Program on a regular basis using statistical analysis to determine if the PVC Program is generating more revenue for DIA. In addition the analysis should determine if the PVC Program is fairly, accurately, and effectively identifying top-performing concessions as defined as having statistically higher monthly revenue, statistically higher monthly revenue growth year over year, and statistically higher customer service scores than all other concessions in their minor merchandising categories.	As part of the Rule 45 revision process, DIA utilized BBC Research and Consulting to develop an alternative statistical analysis to predict top performers. However, DIA did not provide auditors with the summary report from BBC Research and Consulting, as requested. Without this additional evidence of the work done in conjunction with BBC Research and Consulting, we were unable to verify the steps taken by DIA to implement the recommendation.	Agree/Not Implemented

Recommendations: Status of Implementation

	Recommendation	Auditee Action	Status
Finding 2: Denver International Airport’s Concession Policy Is Outdated and Can Be Revised to Better Meet the Goals of the Concessions Program			
2.1	<p>Concentration of Ownership Standard Study – The Manager of Aviation should initiate a study regarding the concentration-of-ownership standard to determine whether it is more appropriate to limit the number of leases a concessionaire can operate or limit the square footage a concessionaire can control to achieve Denver International Airport’s goal of encouraging competition and maximizing opportunities for small, local businesses.</p>	<p>The DIA Concession Policy has been updated to include a revised Concentration of Ownership policy and calculation methodology. The revised policy became effective December 17, 2014. DIA indicated that they would provide a copy of a redline report received from concessionaires indicating their agreement to the revised Concentration of Ownership policy and calculation methodology. However, DIA did not provide auditors with a copy of this report, as requested and therefore we cannot consider this recommendation implemented.</p>	Agree/Not Implemented
2.2	<p>Concentration of Ownership Standard Revision – Once a study on concentration of ownership is complete, the Manager of Aviation should revise the concentration-of-ownership standard to reflect the study’s findings.</p>	<p>The DIA Concession Policy has been updated to include a revised Concentration of Ownership policy and calculation methodology. The revised policy became effective December 17, 2014.</p>	Implemented
2.3	<p>Concentration of Ownership Standard – The Manager of Aviation should revise applicable policy to outline a specific standard for concentration of ownership for concourses and the terminal. The policy should clearly define the ownership standard and how it applies to concourses and the terminal.</p>	<p>The DIA Concession Policy has been updated to include a revised Concentration of Ownership policy and calculation methodology. The revised policy became effective December 17, 2014.</p>	Implemented

Recommendations: Status of Implementation

	Recommendation	Auditee Action	Status
2.4	Concentration of Ownership Data – The Manager of Aviation should ensure that data and formulas used to calculate concentration of ownership is used consistently by all personnel.	The DIA Concession Policy has been updated to include a direct reference to the source of the data used in calculating concentration of ownership. The revised policy became effective December 17, 2014.	Implemented
2.5	Revenue Reporting Policy – The Manager of Aviation should revise the DIA Concession Policy to reflect the most up-to-date revenue reporting requirements, including removing the outdated and inaccurate section regarding the daily reporting system. The policy should further be revised to ensure that revenue reporting contract language takes precedence over the DIA Concession Policy.	DIA is currently revising the base concession agreement for use by all DIA concessions when new contracts are required. This is an iterative process and will require some time to complete and communicate. DIA expects to have the new contract in place in the next few months and will adjust the timing of new contract issuances to help move to the new template, once approved.	Agree/Not Implemented
2.6	Evaluation Committee Policy – The Manager of Aviation should expand the DIA Concession Policy, with regard to the Evaluation Committee, Evaluation Committee scoring, and oral interviews, to outline procedures that should be followed when a Committee member or members are unable to attend the oral interviews.	DIA has implemented a new Contract Evaluation Guideline. The guideline has been communicated and training will be provided.	Implemented

Recommendations: Status of Implementation

	Recommendation	Auditee Action	Status
2.7	Rule 45 & Premium Value Concessions Program – The Manager of Aviation should update the DIA Concession Policy to include Rule 45 and the Premium Value Concessions Program. The Manager of Aviation should also ensure that Rule 45 and the DIA Concession Policy clearly and thoroughly outline the Subjective Appeals process.	The DIA Concession Policy has been updated to include the Premium Value Concessions program. Subjective Appeals have been removed from the forthcoming revised Rule 45 and are replaced by Extenuating Circumstances appeals. In the draft of the revised Rule 45, the Extenuating Circumstances appeal is clearly and thoroughly described. The Extenuating Circumstances appeal has been a recent Rule 45 development. The next version of the Concession Policy will reflect this appeal process.	Agree/Not Implemented
Finding 3: The Evaluation and Scoring of Proposals under the RFP Process Lack Transparency			
3.1	Evaluation Committee Training – The Manager of Aviation should develop a training course or materials for review by Evaluation Committee members to ensure that all members have the knowledge and skills to fairly and appropriately evaluate all proposals submitted under concession RFPs.	DIA has implemented a new Contract Evaluation Guideline. The guideline has been communicated and training will be provided. In addition, DIA has an evaluation panel presentation that they provide to the panel members.	Implemented
3.2	Standardized Oral Interview Protocol – The Manager of Revenue Procurement should work with other DIA personnel involved with the evaluation and scoring of concession proposals to ensure that all oral interviews of proposers are conducted in accordance with a standardized protocol and that all proposers are asked the same set of questions.	DIA has implemented a new Contract Evaluation Guideline. The guideline has been communicated and training will be provided.	Implemented

Recommendations: Status of Implementation

	Recommendation	Auditee Action	Status
3.3	<p>Evaluation Committee Scoring and Comments – The Manager of Aviation should revise policies and procedures that govern the concession RFP process to make the evaluation and scoring process more transparent. Such revisions should specify that proposals reviewed, Evaluation Committee individual scores from both before and after oral interviews, and Evaluation Committee individual comments from oral interviews are required to be documented, maintained, and made available for review by all interested parties. In addition, to protect the identity of Evaluation Committee members, the Manager of Aviation should ensure that all Committee member names are redacted before they are released to individuals not employed by DIA or the City.</p>	<p>DIA has implemented a new Contract Evaluation Guideline. The guideline has been communicated and training will be provided.</p>	<p>Implemented</p>

Conclusion

While DIA personnel have implemented seven of the sixteen recommendations made in the DIA Concessions Management audit report, the remaining nine recommendations have yet to be acted upon or fully implemented. Specifically, while DIA has made key revisions to Rule 45 in response to our recommendations, the document has not been finalized. In total, five of the remaining nine recommendations are dependent on this document being approved and implemented. According to DIA personnel, recommendations 1.3 and 2.5 are still in progress. Although DIA personnel noted that recommendation 1.6 has been implemented, they did not provide auditors with the summary report from BBC Research and Consulting, as requested. Without this additional evidence of the work done, we were unable to verify that the proper steps were taken to implement the recommendation. In addition, DIA personnel indicated that they would provide a copy of a redline report received from concessionaires indicating their agreement to the revised Concentration of Ownership policy and calculation methodology to support the implementation of recommendation 2.1. However, DIA did not provide auditors with a copy of this report, as requested, and therefore we cannot consider this recommendation implemented. Accordingly, auditors determined that the risk associated with the audit team's initial findings has not been fully mitigated. As a result, the Audit Services Division may revisit these risk areas in future audits to ensure appropriate corrective action is taken.

On behalf of the citizens of the City and County of Denver, we thank staff and leadership from DIA for their cooperation during our follow-up effort and their dedicated public service.