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AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

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DEPUTY AUDITOR GENERAL

August 18, 2016

The Honorable John Allen, Chair
Joint Legislative Audit Committee

The Honorable Judy Burges, Vice Chair
Joint Legislative Audit Committee

Dear Representative Allen and Senator Burges:

Our Office has recently completed an initial followup of the Arizona Sports and Tourism Authority (Authority) regarding the implementation status of the 18 audit recommendations (including sub-parts of the recommendations) presented in the performance audit report released in September 2015 (Auditor General Report No. 15-107). As the attached grid indicates:

- 7 have been implemented;
- 8 are in the process of being implemented;
- 2 are not yet applicable; and
- 1 is no longer applicable.

Our Office will conduct a 24-month followup with the Authority on the status of those recommendations that have not yet been fully implemented.

Sincerely,

Dale Chapman, Director
Performance Audit Division

DC:ka
Attachment

cc: Tom Sadler, President/CEO
Arizona Sports and Tourism Authority

Arizona Sports and Tourism Authority Board of Directors

Arizona Sports and Tourism Authority

Auditor General Report No. 15-107

Initial Follow-Up Report

Recommendation

Status/Additional Explanation

Finding 1: Authority's tourism revenues are insufficient to fund all statutorily designated priorities

1.1 The Board should take an active role in addressing the issue of insufficient tourism revenues for funding monthly distributions by taking the following actions:

a. Working with authority staff to identify and study various options for addressing the issue, including determining the potential financial impact to each statutory priority for each option;

b. Working with stakeholders and the Legislature to identify which options would be feasible; and

c. Clearly communicating to the Legislature and stakeholders the financial impacts to each funding priority for any recommended options.

Implementation in process

The Authority has projected its future monthly distributions from tourism revenues according to the distributions and priorities set in statute for fiscal years 2017 through 2021. The Authority's projections for these fiscal years indicated that, although it will be able to meet its stadium bond debt obligations, all of its other, lower funding priorities will likely be impacted by monthly revenue shortfalls through fiscal year 2021. In addition, the Authority reported that all funding priorities would be impacted even more if the plaintiff in the *Saban Rent-A-Car LLC vs. the Arizona Department of Revenue* lawsuit is successful and the car rental surcharge is eliminated. This could impact the Authority's ability to pay its stadium bond debt obligations with its tourism revenues. The Authority reported that it will begin discussions with its Board of Directors (Board) in October 2016 to develop various options for addressing the shortfalls in its tourism revenues based on the projections.

Not yet applicable

The Authority reported that it will begin identifying options for addressing the potential shortfalls in its tourism revenues in October 2016 (see explanation for Recommendation 1.1a) and, as a result, has not yet approached stakeholders and the Legislature to identify which options would be feasible.

Not yet applicable

See explanation for Recommendation 1.1b.

Recommendation

Status/Additional Explanation

1.2 To help ensure that its distribution of tourism revenues is consistent with current statutory requirements, the Authority should:

- a. Work with its legal counsel to determine if it can legally correct the errors this report has identified in the Authority's prior distributions and then act accordingly; and
- b. Hire an outside contractor to annually review its monthly revenue distributions, including conducting work to determine if the amounts distributed were consistent with its statutory requirements.

Implementation in process

The Authority reported that its legal counsel has determined that it can make corrections for validated errors identified in the audit report. According to the Authority, it is in the process of validating the reported errors by reviewing its fiscal years 2011 through 2014 monthly tourism revenue distributions. The Authority estimated it will complete this process by the end of calendar year 2016.

Implemented at 12 months

Finding 2: Authority may face challenges funding future operations

2.1 In order to ensure that it complies with its FUF agreement with the Cardinals, the Authority should:

- a. Consult with its legal counsel and work with the Cardinals to determine the correct amount of any required payments between the two parties for fiscal years 2011 through 2014;
- b. Continue to conduct the calculations as required by the FUF agreement to determine any future payments between two parties, including any payments from the Authority to the Cardinals; and
- c. Hire an outside contractor to annually review its calculations related to the FUF agreement to identify potential errors.

Implemented at 12 months

Implemented at 12 months

Implementation in process

The Authority's financial auditor reviewed its calculations related to the FUF agreement to identify potential errors during its annual financial audit for fiscal year 2015. Additionally, according to the Authority, its financial auditor will then review its calculations related to the FUF agreement to identify potential errors during its annual financial audit for fiscal year 2016, which should be completed by October 2016.

Finding 3: Authority should consider various options for improving facility management agreement

3.1 The Authority should consider various options for improving its facility management agreement as follows:

a. If the Authority chooses to enter an agreement with a fixed price for any services, whether the agreement is a fixed-price agreement or an agreement with a mixture of a fixed-price and cost-reimbursement components, it should take additional steps to design an effective agreement, including:

- Increasing performance incentives to compensate the facility management contractor for assuming more risk;
- Incorporating incentives and/or disincentives for nonfinancial performance in its agreement; and
- Including its subjective fee evaluations to be completed by the Cardinals and the Fiesta Bowl to help determine a performance-based incentive fee.

b. If the Authority chooses to enter an agreement with cost reimbursement for any services, whether the agreement is a cost-reimbursement agreement or an agreement with a mixture of a fixed-price and cost-reimbursement components, it should take additional steps to appropriately design and oversee an effective agreement, including:

- Enhancing its oversight of the facility management contractor's expenses;
- Including a revenue guarantee that meets the Authority's needs; and
- Better aligning facility revenue and expenses in the facility's annual budget.

No longer applicable

The Authority did not enter an agreement with a fixed price for any services.

Implementation in process

In July 2016, the Authority entered a cost-reimbursement agreement with a new facility management contractor to manage and operate the facility. According to the new agreement, the Authority pays for all of the facility management contractor's expenses for managing and operating the facility. The new agreement does not include a revenue guarantee. Additionally, the Authority has not yet taken steps to enhance its oversight of the facility management contractor's expenses. However, the new agreement includes compensation provisions for incentivizing the facility management contractor to maximize facility revenues while also minimizing facility expenses. Auditors will follow up at 24 months to assess the impact of the new agreement on the Authority's revenues, expenses, and budget, and its enhanced oversight of the facility management contractor's expenses.

3.2 The Authority should work with its consultant to procure and negotiate the most beneficial agreement possible by:

a. Designing the agreement to help ensure that the Authority's facility-related revenues can pay for its administrative and operational expenses;

Implemented at 12 months

Recommendation	Status/Additional Explanation
<ul style="list-style-type: none"> b. Incorporating into the agreement and/or establishing sufficient mechanisms to adequately oversee its facility management contractor and ensure that the Authority is receiving the highest quality service for the lowest possible costs; and 	<p>Implemented at 12 months</p>
<ul style="list-style-type: none"> c. Ensuring the agreement is consistent with any of the Authority's other agreements. 	<p>Implemented at 12 months</p>
<p>3.3 The Authority should work with its legal counsel to ensure that the new agreement complies with IRS regulations for tax-exempt facilities.</p>	<p>Implemented at 12 months</p>

Finding 4: Authority should improve its facility capital improvement practices

4.1 To help ensure the sustainability and viability of the facility, the Authority and its Board should develop and implement capital planning policies and procedures that include:

- a. A clear definition of what constitutes a capital improvement project, including but not limited to significant capital maintenance projects;
- b. Provisions for the Board's monitoring and oversight of capital improvements planning and budgeting to help ensure a clear decision-making process, including a description of how the Board will prioritize and approve projects, and a description of the roles and responsibilities in the process for authority staff, the facility management contractor, and facility tenants;

Implementation in process

The Authority has developed a revised draft of its procurement policy that includes a definition of what constitutes a capital improvement. It estimated that it would complete the development of the revised policy and receive board approval by the end of calendar year 2016.

Implementation in process

In June 2015, the Authority's Board of Directors (Board) approved a revision to its procurement policy which added a new procurement procedure for capital improvements. The new procedure includes a requirement that any acquisitions of capital improvements must be set forth in a capital improvement plan approved by the Board. In addition, the revised policy states that capital improvement acquisitions must follow a request for proposal (RFP) process, and the Board must approve the capital improvements following the RFP process before they can be acquired. However, the revised policy does not include provisions for the Board's monitoring and oversight of other aspects of capital improvements planning and budgeting, such as its role in overseeing the development of a capital improvement plan or a description of how the Board will prioritize and approve projects before the procurement process begins. In addition, it does not include a description of the roles and responsibilities in the capital improvements planning and budgeting process for authority staff, the facility management contractor, and facility tenants. The Authority reported that it was working with its facility management contractor and other stakeholders to develop written policies and procedures for all aspects of the capital improvements planning and budgeting process, and estimated that it would complete this process by the end of calendar year 2016.

Recommendation

Status/Additional Explanation

- c. Provisions for developing a multiyear capital improvement plan (capital plan) covering a period of at least 3 to 5 years that clearly identifies capital and major equipment needs, maintenance requirements, funding options, and operating budget impacts; and

- d. Provisions for developing a capital improvement budget as part of its annual budget process using the information in the capital plan to help separately budget and track capital projects. The budget should include a schedule for completing each project, including specific project phases, estimated funding requirements for the upcoming years(s), and planned timing for acquisition, design, and construction activities.

Implementation in process

Although the Authority has developed a multiyear capital improvement plan, it had not yet developed policies and procedures requiring the development of a multiyear capital improvement plan. The Authority reported that it was working with its facility management contractor and other stakeholders to develop written policies and procedures for all aspects of the capital improvements planning and budgeting process, and estimated that it would complete this process by the end of calendar year 2016.

Implementation in process

The Authority included proposed capital improvement projects in its fiscal year 2016 budget, which its Board approved. However, the list of proposed projects in the budget did not include a schedule for completing each project, including specific project phases, estimated funding requirements for the upcoming year(s), and planned timing for acquisition, design, and construction activities. In addition, the Authority has not yet developed written policies and procedures that include provisions for the development of a capital improvement budget. The Authority reported that it was working with its facility management contractor and other stakeholders to develop written policies and procedures for all aspects of the capital improvements planning and budgeting process, and estimated that it would complete this process by the end of calendar year 2016.