City of Long Beach
Office of the City Auditor

Long Beach Airport
Leasing and Concessions Performance Audit

August 1, 2012

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Executive Summary

The Long Beach City Auditor contracted with Sjoberg Evashenk Consulting to conduct a performance audit of the Long Beach Airport's leasing and concession activities. The Long Beach Airport (Airport) is the 72nd largest commercial airport in the U.S. One of the nation's busiest airports in terms of general aviation, the Airport is also served by four major airlines and several commuter carriers on its five runways.

Based on our review of ground leases, concessions and ground transportation services, we believe that although the Airport conducts many quality assurance reviews as required in the terms and conditions of its lease and concession agreements, and has recently implemented some policies and procedures that show promise, more can be done to improve its oversight and management of these revenue producing agreements. Areas where improvements can be made include:

- Periodically validating self-reported revenue amounts to underlying supporting documents, such as sales receipts, financial reports, or gasoline meter readings for leases containing revenue generating fees, and concessions for food, news, gifts, and rental cars.

- Expanding newly created Airport lease and concession management guidance with additional formal policies and procedures requiring well documented and standardized processes. While the Airport conducts various reviews to ensure lessees and concessionaires abide by agreement terms and conditions, these practices are primarily informal in nature with minimal documentation.

- Assuring that lease and concession security deposits and minimum insurance requirements are tracked and appropriately updated.

- Establishing centralized account files and reducing ineffective account management practices. Currently, documents for lease or concession agreements (including correspondence and copies of security deposits) may be filed in the Accounting Department account files, in separate files managed by leasing staff, or in other City of Long Beach Departments.

- Redesigning its approach to ground transportation oversight practices of the nearly 500 authorized shuttle van and limousine operators. Since only about one-half of these operators submit the required monthly passenger pick-up activity reports and pay the self-reported fees to the Airport, oversight and follow-up of non-compliant operators is difficult and other approaches may be more practical.

Background

Based on its 2011 activities, the Long Beach Airport serves 3.1 million enplaned and deplaned passengers who utilize four major airlines and various commuter carriers. Additionally, the Airport handles nearly 25,500 tons of cargo and general aviation traffic from its five runways.

With an adopted 2012 budget of $39.4 million, the Airport also generates revenue from a wide range of leases and concessions, including:

- 104 building and ground leases[1];
- Two concession agreements for food and beverage services as well as gift, news, and retail services, and one agreement for advertising on Airport property;
- Five concession agreements with car rental companies; and
- Approximately 486 permits to shuttle, van, bus and limousine transportation providers.

As prescribed in the City of Long Beach Administrative Regulation No. 8-5, the Department of Community Development (DCD) established a centralized real estate services function for the development and operation of a coordinated acquisition, sale, and leasing program for all departments reporting to the City Manager, with limited exceptions. DCD conducts appraisals on Airport leases, and the City's Asset Management Bureau (AMB) calculates Consumer Price Index (CPI) adjustments on Airport leases periodically. Thus, the Airport works in collaboration with DCD and AMB related to its leasing activities. As of October 2010, the bureaus within the DCD have been consolidated into other City Departments. The AMB is now within the Department of Public Works and the required lease appraisals along with CPI adjustments will now be conducted within this City Department.

Building and Ground Leases

The Airport has 62 large building and ground leases, excluding Commercial Use Permits, within its boundaries generating about $8.2 million annually, as of Fiscal Year 2011. The land and buildings are used for both aviation and non-aviation purposes, including Fixed Base Operators serving the general aviation community; and hotel, office, and retail uses that are typical non-aviation activities.

Food and Beverage, Gift, News, and Retail, and Other Concessions

The Airport has one primary concessionaire for food and beverage services that offers small kiosk/trailer-based food service throughout the airport, as well as operating a restaurant and bar inside the main terminal. SSP America is the Airport's current restaurant concessionaire.

Paradies Shops operates the Gift Shop concession in the Airport terminal in addition to smaller gift, news, and retail kiosks in the passenger terminals. Another Airport concessionaire, Inter-Space Services Inc., operates the Airport display advertising concessions.

[1] Of the 104 building and ground leases, 42 are smaller Commercial Use Permits for use of airport property on a month-to-month basis.

Ground Transportation

The Airport authorizes 26 shuttle van operators, five car rental companies, and approximately 460 luxury sedan/limousine operators who may pick up passengers from the Long Beach Airport. These permits/licenses are secured through the Airport Manager or Director. Rental car operators are not required to obtain a special ground transportation permit from the Airport, but must execute a rental car concession agreement to operate on Airport grounds.

Audit Objectives, Scope, and Methodology

The Long Beach City Auditor contracted with Sjoberg Evashenk Consulting, Inc. (SEC) to conduct a performance audit of the lease and concession activities of the Long Beach Airport. To evaluate the Airport's management of these revenue generating activities, the audit objectives include:

- Identifying and analyzing the full inventory of the Airport's concessions, leases, and other fee generating activities, including:
  - Restaurants and bars
  - Gift shops
  - Terminal advertising
  - Car Rental Agencies
  - FBO and airport services
  - Shuttles, Limousines and Buses
- Reviewing a sample of the agreements, contracts, or leases associated with each of the Airport's revenue generating activities identified above to determine if they are being managed and overseen to the benefit of the Airport and City.
- Conducting an analytical review of each type of concession and lease agreement from Fiscal Year 2008-2009 to present to identify and evaluate instances where anomalies or volatility has occurred.
- Identifying best and leading practices for the management of airport concessions and leases to compare fees, rates, and agreement terms and conditions at the Airport against other airports in the region.
- Assessing whether the Airport is in compliance with FAA, State and City laws, and directives regarding concessions and leases.
- Determining if the Airport is efficiently and effectively establishing, managing, and overseeing selected revenue generating activities.

The City of Long Beach has citywide contracts or license agreements with taxicab services and the Long Beach Airport manages its parking on a month-to-month basis under a contract that needs to be renegotiated. As a result, it was agreed that these areas be excluded from the audit scope. We also reviewed the Airport's oversight of its advertising concessionaire, Inter-Space

Services, Inc., and did not find any issues regarding the Airport's management of this agreement to report.

Additional information on the Audit's Scope and Methodology is provided in Appendix B.

We conducted this 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 limited our review and analyses to those areas described in the "Objectives, Scope, and Methodology" section of the report. A draft report was provided to Long Beach Airport management for comment. Their response is appended to the report as Appendix A.

Results

The Long Beach Airport (Airport) currently has 104 building and ground leases within its boundaries used for both aviation and non-aviation purposes, such as Fixed Base Operators (FBO), fuel services and offices. To address travelers' needs, the Airport also utilizes concessionaires to provide food, beverage, news and sundry products. Finally, to assist travelers departing the Airport, a variety of transportation services are offered, including rental cars, shuttles, and limousines. In all, these leases and concessions generate more than $12 million in revenue annually.

In efforts to better manage its lease and concession revenue generating activities, we noted that Airport management and staff have recently implemented some policies and procedures that will help improve the efficiency and effectiveness of its operations. Although we found that many key features of the lease or concession agreements were being reviewed by staff, we believe there are several areas where additional improvements can be made.

In the following four sections we highlight the opportunities for improvement we identified.

- Validation of Self-Reported Revenues
- Managing Accounts Receivables, Security Deposits and Insurance Coverage,
- Quality Assurance Lease and Concession Monitoring
- Shuttle Van and Limousine Oversight

1. Validation of Self-Reported Revenues

Generally, the Airport does not independently validate or verify the payments it receives from lessees, concessionaires, or transportation providers. For concessions and leases that include the payment of fees based on gross revenues generated or gallons of fuel delivered, the Airport Accounting Department checks the accuracy of the mathematical calculations, but does not validate or otherwise verify the accuracy of the sales amounts submitted. In fact, underlying support for these payments, such as sales receipts or gasoline meter readings is currently not being required. Fees paid based on self-reported revenues represent a significant portion of the revenues collected from lessees, concessionaires, and ground transportation providers. For example, of the $4.2 million of Airport concessionaire revenues collected in 2009, at least $1.3 million was based on self-reported revenues.

For the two major concessions, we observed operations and conducted additional tests of sales revenue data (e.g. financial sales reports, accounting records, etc.) to match against monthly payments made to the Airport. We found that both concessionaires assured that all sales were recorded in their Point of Sale (POS) cash register system and that Airport fees were accurately remitted. Although we did not find instances where lessees or concessionaires underreported revenues, the absence of consistent, periodic validation of underlying support by Airport staff limits the Airport's ability to comply with its responsibilities under lease and concession terms and conditions, and creates a control weakness by removing the deterrent effect such tests would have on its lessees.

a. Building and Ground Leases

Some leases contain revenue-based airport fees in addition to rents based on per-square-foot usage. In these cases, the lease terms and conditions describe the following:

- ***Fuel Sales Revenues*** – Monthly fees are based on a percentage of fuel deliveries. Lease terms specify that the tenant is to provide a year-end statement showing all deliveries (meter tickets) and both monthly and year-end statements on forms supplied by the Airport Manager. Also, the Airport is authorized to examine and review tenant's records to determine compliance with all terms and conditions.
- ***Rental and Other Revenues*** – Monthly fees are based on a percentage of sales. Lease terms specify that the Airport shall be permitted to examine and review records for the purpose of determining compliance with all lease terms and conditions.

We found that some self reporting revenue forms contained attestations by the lessee's Chief Financial Officer (CFO). While attestations do provide an additional level of controlling self reported revenue information, it is not as strong a control as copies of underlying rents, sales receipts, or fuel meter readings. Moreover, we also found instances where the CFO did not consistently sign the self reporting revenue forms to provide this attestation.

b. Food, Beverage, News and Gifts Concessions

Similar to our findings related to building and ground leases, the Airport does not verify or validate the underlying sales revenues (through sales register totals, inventory reductions, etc.) for the self-reported revenues upon which the vendor pays its monthly Airport fees. Each concession agreement requires that the concessionaire pay a monthly fee which equals a specific percentage of its gross receipts for a variety of sales, including food and beverages and in-flight catering. Gross receipts include the revenues from the sale, dispensing and serving of food, food products, beverages, gifts, news, and other related services or products.

Exhibit 1. Fee Provisions for the Two Major Concessionaires

Vendor	Guaranteed Minimum Annual Concession Fee	Food & Non-Alcoholic Beverage	Alcoholic Beverages	Vending Machine	In-Flight Catering	Category 1	Category 2
SSP	Greater of $450,000 or 85% of prior year fees paid	15%	20%	12%	10%	n/a	n/a
Paradies Shops	Greater of $100,000 or 85% of prior year fees paid	n/a	n/a	n/a	n/a	16%	20%

We reviewed the monthly gross revenue statements submitted by each of the two concessionaires and compared them to the payment amounts remitted for the following periods: October 2011, May 2011, October 2010, May 2010, and October 2009. Our review discovered that concessionaires submitted the appropriate payment amounts on a monthly basis based on the reported month's gross revenues. However, we determined that the revenue amounts were self-reported and were not accompanied with supporting documentation to validate the revenue amounts reported.

The concession agreements include provisions that require the concessionaire to submit a monthly "…accounting of the gross receipts received, derived or billed by concessionaire…" in the operation of the concession business for the preceding calendar month. However, the agreement does not specifically describe what constitutes sufficient evidence of gross receipts although the provisions do give Airport management the authority to prescribe the "manner and detail and…forms" of the support. While the concession agreements appear to allow the self-reporting of gross revenues when remitting monthly fee payments, there are provisions in the agreement that require concessionaires to submit stronger evidentiary support of their gross revenues. Specifically, each concession agreement includes the following provision:

> *"Concessionaire shall also furnish to City a detailed gross receipts or income statement, prepared at the close of concessionaire's taxable year, covering all [applicable] business transacted by concessionaire at the airport…Said income statement shall be certified by concessionaire's Chief Financial Officer."*

We found no evidence that concessionaires consistently submit year-end income statements or detailed statement of gross receipts certified by the concessionaire's Chief Financial Officer.

C. Transportation Services

Similar to revenues generated from leases and concessions, shuttle van, and limousine payments are self-reported without validation by Airport staff. Although Airport accounting and transportation staff review the payments received, the underlying basis for these payments – the number of Airport pickups during the preceding month – is not independently verified. Further, under the current system, there is an opportunity to track airport pickups with logs maintained by the shuttle attendant that are not being utilized. We found that the attendant who guides passengers to shuttle vans also prepares a daily log of this pickup activity. The log includes the shuttle van permit number and the number of passengers served. Since these logs are retained for about one year, the Airport could use the log to reconcile payments by permittees on an occasional basis to identify possible instances of non-compliance.

The five rental car company monthly payments are received by Airport accounting under a prescribed format. However, similar to the other revenue generating agreements, the Airport does not verify or validate the revenue amounts used to calculate the monthly fees.

2. Managing Accounts Receivables, Security Deposits, and Insurance Coverage

Requiring tenants, concessionaires, and ground transportation providers to submit timely monthly payments is an important condition of each agreement we reviewed. Moreover, agreement terms and conditions also require the responsible party to provide the Airport with a security deposit that can be accessed by the Airport in case of default or delinquency, and to maintain insurance coverage to protect Airport assets in case of personal injury or property damage claims. While we identified some efforts by Airport staff to manage accounts receivables and track security deposits and insurance coverage, other changes would improve controls over these key activities.

Demonstrating the importance of overseeing these key activities was the fact that some lease and concession payments are overdue 90-120 days, several lessees are in default, security deposit amounts may not always reflect current agreement requirements, and multiple tenants and providers continued operations under expired insurance coverage. Actively pursuing collection of accounts receivables will identify lessees who may be vulnerable for future default so that early action can be taken. Also, if security deposits do not match the amounts required in the lease, the Airport's ability to absorb losses is diminished. Furthermore, by not consistently tracking and monitoring insurance records, Airport assets may be at risk if a personal injury or property damage claim is levied against a lessee or concessionaire operating under expired insurance policies.

These problems would be mitigated if Airport staff maintained centralized account files that include security deposit data, insurance certificates, lessee/concessionaire communications, payment records and inspection reports, and actively tracking delinquent accounts receivable and documenting steps taken to secure payment.

a. Managing Delinquent Accounts Receivables

We found that several leases are late paying rent by 30 days or more and some are on the verge of default. These overdue accounts receivables total approximately $452,355 in unpaid revenues, as of the February 29, 2012 aging report. Although the Airport has implemented new policies and procedures to address this issue, the Airport lacks having a centralized location to update and track actions taken once an accounts receivable (e.g. lease, concession or fuel payment) is deemed overdue. In late 2011, the Airport created an aging report to track late payments, including late fees, and pursue delinquent account receivables. This aging report was created and is maintained by the Accounting Department, with Airport leasing staff updating changes to account status on a monthly basis. However, Airport leasing staff does not update and track actions taken in the collection escalation process in a centralized location. Although documentation on collection efforts may exist, Airport staff told us they must check multiple locations to determine up-to-date account status.

Recently, the Airport developed formal policies and procedures detailing the escalation process for delinquent account receivables, which includes timelines for sending delinquent notices to lessees and when to begin process to terminate contracts. These new policies should be combined with centralized tracking so that Airport management can review the status of collection efforts without needing to have staff obtain such information from decentralized files. According to Airport administration, the City's mandated Billing and Collection (B&C) system is the official record for the City, and the Airport, for all accounts receivable; however, the tool is limited in its ability to record and track all necessary updates related to any individual account. As the Airport must continue to use the B&C system as the official financial record, given the system limitations, the Airport should consider using the newly created aging report as the supplementary recording location of collection actions taken with accounts thereby reducing where Airport staff would need to research account status to two locations.

We initially identified six lessees on the verge of default on their leases as of the December 31, 2011 aging report; two of the accounts having delinquent balances dating back to 2009 and 2010. The Airport appears to be taking appropriate action in each of these cases, such as negotiations with a new lessee, establishing payment plans with an existing lessee, or referring delinquent accounts to the City Attorney's Office. We are told that if any negotiations fail, the Airport will proceed with lease default processes. As of the February 29, 2012 aging report, two of the six leases have paid the accounts in full and are no longer in delinquency.

b. Security Deposit Monitoring

Most lease and concession agreements reviewed include terms that require submission of a security deposit with the Long Beach Airport at the time the agreement is initially negotiated. In our 14 sampled lease and concession agreements, the required security deposits ranged from $1,400 to $112,500 in value. The Airport deposits cash payments made for security deposits into a trust account and inputs the data regarding this deposit into a spreadsheet maintained by the Airport Accounting Department. However, security deposit payments made using other means, such as a surety bond, letter of credit, or certificate of deposit, are not recorded on this spreadsheet. We were told that copies of these non-cash security deposits are included in the individual lessee's account file maintained by Airport leasing staff or in files maintained in the Accounting Department, yet they were not always in the files we reviewed. According to Airport staff, non-cash security deposits are managed by the Long Beach City Treasurer's Office. The Treasurer's Office manages this particular contract provision by keeping a copy of each deposit instrument on file at their offices and then providing a list to the Airport of all Airport vendors/contractors who have made non-cash security deposits. Although a City Department may oversee particular contract provisions, it is ultimately the Airport's responsibility to ensure all contract provisions are appropriately adhered to by each lessee and concessionaire.

When we attempted to reconcile security deposit amounts on file against the amounts required in the related lease or concession agreement, we found the following issues. First, our attempt to reconcile cash security deposits held in trust to the required security deposit listed in the agreements revealed that four of the nine deposits requiring a security deposit did not match the required security amounts in the current agreement. The shortfall between the required deposits and those actually on hand ranged from $400 to $34,400, with a total security deposit shortfall of approximately $81,700. Second, although copies of non-cash deposits should be located in account files, when we reviewed the contents of the individual lease account files maintained in the Accounting Department, we found that there were no valid surety bonds, letters of credit or certificates of deposits in the lessee account files we reviewed. Finally, current oversight of non-cash security deposits, which totaled approximately $353,000 for the accounts tested, does not include recording and tracking when security deposit instruments expire.

C. Insurance Coverage

Similar to security deposits, lease and concession agreements include terms requiring maintenance of specific levels of insurance coverage while conducting operations at the Long Beach Airport. The Long Beach City Risk Management Department typically receives original or renewal insurance policy certificates directly from each Airport account holder and maintains a record of pertinent insurance details, including expiration dates and coverage type. Airport staff notifies Risk Management of those certificates processed by the Airport so that insurance records may be updated accordingly.

Although the Airport has incorporated some methods for monitoring insurance requirements, such as receiving periodic reports from Risk Management on expired insurance certificates, records are infrequently monitored, which has led to multiple accounts operating under expired insurance certificates.

Our review of leasing and concession insurance records found that records were not maintained or frequently updated to assure insurance coverage was current or sufficient as required in the agreements. As a result, we were unable to assess whether vendors were currently compliant with lease insurance requirements and whether policy holders maintained sufficient coverage throughout the entire term of the agreement. Although the Airport created a spreadsheet to monitor compliance with insurance requirements for its lease agreements, the spreadsheet was inconsistently updated and was last reviewed on July 22, 2010. Our review of the insurance spreadsheet identified instances where data was missing or inconsistently recorded. Specifically, we found that of the 60 lease agreements with insurance requirements, 39 agreements reflected as least one expired insurance requirement and insurance information was not reported for five additional agreements as of July 22, 2010. Based on the available data, the length of time accounts operated under expired agreements ranged from a few weeks to 2 years.

The Airport advised us that as they transition account management responsibilities from the City to the Airport, they are requesting that Risk Management send all insurance certificates to the Airport as they expire. The Airport plans to manage a number of contract requirements, including insurance requirements, through its new automated contract management system, CityLaw. According to Airport staff, the CityLaw system will include enhanced contract management functionality such as automated tracking of insurance certificate expiration. However, at the time of this audit the Airport had not fully transitioned to the CityLaw system and as a result this audit did not rely on data generated from the CityLaw system nor were CityLaw system controls reviewed and tested. Regardless of the method used, similar to security deposits, the Airport needs to ensure it improves the consistency of its oversight over insurance requirement to ensure lessees and concessionaires remain in compliance.

3. *Quality Assurance Lease and Concession Monitoring*

Although Airport staff actively review and monitor a number of contract provisions to ensure appropriate concession and lessee compliance, there are several areas where additional monitoring and oversight would provide the Airport with greater assurance regarding compliance with contract terms and conditions. These include such areas as standardizing and documenting periodic on-site lease inspections and quality assurance walk-throughs of concession areas.

a. Periodic On-Site Reviews of Ground Leases

Ground lease provisions allow the Airport the right to conduct site inspections (to enter and inspect leased premises) to "determine the condition of and protect landlord's interests in the [leased] premises for the purpose of keeping the premises in a decent, safe, healthy, clean, and functional condition." Current Airport practices include having Airport Operations Department staff drive the perimeter of each leased space to conduct visual inspections of exterior areas and those internal areas that are visible.

If any issues are identified, responsible Airport staff contact the lessee to resolve these problems. Although Airport leasing and Operations staff also periodically "stop by" the lessee's location in an effort to keep a strong relationship with the lessee, these visits do not include an inspection inside of the leased premises to evaluate premise conditions, such as through a compliance checklist. Furthermore, ground lease provisions also permit the Airport to audit tenant records "…for the purpose of determining compliance with all terms, covenants and conditions of this lease…" such as ensuring lessee activities fall within the authorized use provisions of the agreements. Moreover, the Airport has not conducted formal audits, as allowed under lease provisions, to examine and review tenant records for compliance to lease provisions.

Lessee observations and visits conducted by the Airport staff are not formally documented and tracked. This information could also be used when negotiating lease extensions or renewals, or possibly to determine whether on-going problems warrant lease termination. Presently, the Airport does not have a formal inspection or auditing program incorporating the unique authorized use parameters of each lease agreement that captures in detail (such as a check list) lessee responsibility for appropriately maintaining the conditions of leased areas. In addition to inspections and audits, the Airport should continue the informal, periodic review of exterior leased spaces and visits to lessees as an effective supplement to less frequent formal inspections and to foster improved Airport and lessee relations.

b. Concession Quality Assurance Inspections

We also found that similar to building and ground leases, Airport staff to do not have formal policies and procedures in place for conducting inspections or evaluations of the concessions as required in the lease terms and conditions. Although Airport staff typically conducts a weekly "walk-through" of the concession areas to assure that the facilities are clean and well maintained, the inspections are not recorded and monitored. Incorporating a more formalized quality assurance (QA) process will provide the Airport the ability to evaluate performance trends and identify repeat issues related to the quality of concession services. A QA review process should include formally documenting which concessionaire was reviewed, time, and date of review, review categories (this may be in the form of a checklist), the concession areas reviewed, issues discovered during review, date concessionaire notified of issues found during QA review, date by which concessionaire should resolve issues, and a method of recording, tracking, and resolving issues discovered.

Although Airport staff were confident that each concessionaire used an appropriate Point of Sale (POS) cash register system, based on their visual inspections conducted during the weekly quality assurance reviews, they could not demonstrate it had a description of concessionaire cash handling and sales recording systems and the Airport could not describe the functionality of said systems or describe concessionaire cash handling or inventory internal controls.

To assess whether the two major concessionaires used the appropriate POS systems and incorporated sufficient internal controls over its inventory and cash handling, we conducted site visits and interviewed management with each company. Overall, it appears that the two concessionaires use acceptable POS systems and have sufficient cash handling and inventory controls in place to provide the Airport adequate assurances that POS system generated accurate revenue reports reflect all concession sales, unique usernames and passwords, and frequently audited sales reports back to inventory levels. In addition to these measures, the concession management described unique controls such as conducting daily quality assurance checks of cashiers and using secret shoppers.

Notwithstanding our observations, we believe that the Airport should conduct similar unannounced inspections along with more detailed audits of sales records as part of its on-going concessionaire management and oversight responsibilities.

4. Shuttle Van and Limousine Improvement Opportunities

The Airport has 26 authorized shuttle van operators (vans and buses), and approximately 460 authorized limousine operators (limousines and luxury sedans) who may pick up passengers from the Long Beach Airport[2]. Other transportation services offered by the Airport include rental car concessions with five rental car companies.

To comply with Long Beach Municipal Code, the Airport developed a ground transportation license agreement application that describes the minimum requirements to obtain an Airport ground transportation permit. Applicants must pay a one-time non-refundable $50 application fee with each application submitted (multiple vehicles may be listed under one application). Airport staff reviews the application for completeness and verify the CPUC information. We were told by Airport leasing staff that the primary purpose of the licensure process is to assure that the transportation providers have appropriate commercial licenses and insurance to protect the traveling public.

No matter the number of riders, the shuttle van and limousine operators are responsible to pay the airport $1.75 for each airport pickup. Payments are to be made monthly and are self-reported by the operator. For the period March 2011 through July 2011, self-reported revenues from all van, bus, and limousine operators averaged $1,426 per month, representing about 815

[2] As stated in the Scope and Methodology of the report, Taxi operators at the Airport are managed under a non-exclusive license agreement managed on a citywide basis by the City of Long Beach, and as such, they were not included in the audit.

pick-ups per month. Our review of transportation tracking sheets indicated that a significant number of authorized ground transportation providers do not appropriately adhere to the Airport permit/licensing provisions requiring monthly fee payment and/or submission of monthly Airport pick-up activity reports.

Although required to file the monthly pick-up activity reports whether operators picked-up passengers from the Airport or not; overall, we found that only 246 of the 446 shuttle and limousine operators with Airport licenses filed at least one activity report during Fiscal Year 2011. Of the 246 operators that filed activity reports only a fraction filed the requisite form for all 12 months. Since pick-up activity is self-reported, there is a potential loss in Airport pick-up fee revenues from those shuttle operators either not reporting or under-reporting passenger pick-up activity.

As previously discussed, under the current system, there is an opportunity to track airport pickups with logs maintained by the Shuttle Attendant that are not being utilized. We reviewed the shuttle pick-up activity logs for July 2011 and compared the information in the logs to the self-reported pick-up activity reports submitted by shuttle operators. Of the 18 operators listed in the log, one accurately reported the number of passenger pick-ups. The remaining 17 operators either under reported pick-up activity or did not submit a report. This resulted in approximately $1,460 in lost revenues.

a. Opportunities to Improve Shuttle Van and Limousine Compliance and Increase Revenue

Our benchmarking with other airport methods of managing shuttles and limousines suggests that the Airport could consider various approaches to increasing revenue and assuring compliance with reporting requirements. Although these transportation services do not generate significant revenues for the Airport, it does currently consume staff time to review reports and monitor usage. We gathered comparable shuttle and limousine information from three airports, Boise, Idaho, Tucson, Arizona and Louisville, Kentucky, and two nationwide surveys. One national survey revealed the following:

Exhibit 2. Results from A National Survey

Benchmarks of Ground Transportation Fees[3]			
Vehicle Type	**Per Trip**	**Annual Per Vehicle**	**Per Permit Issued**
Shuttles/Vans			
Range	$0.20-$8.50	$100-$1,971	$25-$750
Average	$2.39	$539.00	$172.86
Limos			
Range	$0.20-$10	$15-$15,000	$1.25-$400
Average	$2.94	$1,284.59	$96.04
Buses			
Range	$0.10-$30	$50-$900	$25-$400
Average	$10.91	$273.50	$140.71

[3] Source: Airport Ground Transportation Association survey

Although the approaches to manage these services varied on both the national level as well as our three benchmarked airports – such as using an electronic tracking device at the airport entry point or curbside – the lowest cost and efficient methods we identified that could be applied to the Airport include:

- Evaluating the fee structure and permit authorization process to increase revenues and reduce Airport staff time to manage shuttle and limousine activities in keeping with benchmarked airports.
- Utilizing the daily trip logs maintained by the Shuttle Attendant at the pickup site to conduct periodic audits of the self reported trip counts used by the shuttle and limousine operators to pay the Airport.
- Rethinking the policy that both shuttle vans and limousines pay a single pickup rate since shuttles carry more passengers than limousines. Charging higher rates for shuttle van operators who can carry many more passengers than limousines or setting two levels for an annual fee would be fairer. If the annual fee approach is chosen, the Airport could issue color-coded stickers each year to assure only authorized providers serve its deplaning passengers.

Creating an annual or monthly fee and issuing annual stickers identifying authorized providers may reduce the number of infrequent operators who may decline to pay the fee, but it will also assure that operators are properly licensed. Such a system would also increase revenues since the sticker will provide security with a ready means of identifying users and abusers. Although the flat fee payment frequency selected is ultimately the Airport's decision, implementing an annual flat fee would provide the most efficient method to reduce the necessity of tracking per trip fee payments. Finally, it would also increase the effectiveness of Airport staff oversight of shuttle van and limousine operators.

Recommendations

To address the issues we have identified for improving the Airport's leasing and concession activities, we recommend that Airport management should:

- ✓ Require lessees and concessionaires that have revenue or fuel flowage reporting requirements provide evidence (register receipts, fuel delivery meter receipt, independent auditor statement, etc) of revenue or fuel flowage reported to the Airport.
- ✓ Evaluate all current building and ground lease, concession and ground transportation agreements to determine the minimum security deposit and insurance requirements of each account and ensure all required security deposit amounts are on deposit with the Airport and appropriate levels of insurance coverage remains in place throughout the term of each agreement.
- ✓ Review all current funds held in trust with the Airport to determine if any security deposits currently held by the Airport should be refunded or may be applied to building and ground lease, concession or ground transportation accounts with delinquent account balances.

- ✓ Continue efforts to identify and pursue collection of delinquent accounts.
- ✓ Develop formal policies and procedures (standardized, documented and tracked) for conducting audits and inspections, documenting delinquent account activity, etc. of lessees, concessionaires, and ground transportation operators.
- ✓ Conduct unannounced audits of reported monthly revenues by requiring evidentiary support accompany the reported revenue for a particular selected month.
- ✓ Incorporate an annual or monthly flat fee for the authority to pick up at the Long Beach Airport and annually issue a color-coded window sticker to shuttle van and limousine operators for identification purposes.

Appendix A – Airport Response to the Audit

LONG BEACH AIRPORT
Building a Better Way to Fly

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July 19, 2012

Laura Doud, City Auditor
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Subject: Management Responses to Airport Leasing and Concessions Audit

Dear Ms. Doud:

We are in receipt of your performance audit report on Leasing and Concessions at the Long Beach Airport. We would like to recognize the auditor from Sjoberg and Evashenk for her professional demeanor and focus on helping the Airport improve its operations. Below is a brief discussion of the Airport and specific comments in regards to the audit report.

OVERVIEW

The Long Beach Airport is home to a commercial air-carrier terminal, general aviation support services, two business parks, and other aviation support tenants. Much of the airfield improvements (runways, lights and signs) are funded with Federal Aviation Administration (FAA) grants, which prohibit any revenues being used outside of the Airport. This funding results in significant oversight by the FAA, including routine audits for operational safety, financial stability, compliance with Federal Regulations, and fair treatment of both general and commercial aviation partners.

Please note that for the past three years, Airport Administration has implemented stronger business practices and revenue enhancement strategies. This is evident by a $5,000,000 per year increase in revenue during this period.

The following are management's responses to the audit recommendations:

1. *Validation of Self-Reported Revenues*

In general, we agree that controls over revenue accuracy may be improved, if self-reported revenue were periodically validated. For the most part, Airports have historically relied on the internal controls of its airlines and concessionaires, which are very large corporations (e.g., Delta Air Lines, U.S. Airways, JetBlue Airway, Hertz, Avis, SSP America and The Paradies Shops). Of these partners, the smallest reports over $500 million in annual revenue. It is obvious that these corporations have very strong and well-established revenue controls. In addition, for some time, the Airport has developed and used several "dashboards" that track industry revenue matrices from concessionaires and others. These dashboards are very useful tools for identifying both opportunities and anomalies in terms of revenues per enplaned passenger.

Although the current agreement allows the self-reporting of gross revenue when remitting monthly fees, the Airport will contact the concessionaires in an attempt to document their established internal controls for revenue reporting, in order to determine how much reliance can be given to their processes. In addition, the Airport will study the benefit of engaging a consultant to conduct periodic sampling of the reported revenue with the source documents, including fuel sales and other percentage revenues.

For Transportation Services reporting, the Airport is developing a long-term business approach to correct this very common problem. One option we contemplated is working with LAX and John Wayne airports to implement a program where all three airports use a single electronic transponder system to record each visit by a transportation provider to the Airport and allow for electronic reconciliation and, possibly, billing. Although conversations have been promising and management fully anticipates that this approach would be a very effective method for ongoing validations, the costs far exceed the benefits. In other words it does not make any business sense.

The preferred option in this circumstance is to opt for a yearly permit fee, in lieu of a per pick-up fee. This will reduce administrative overhead and thus increase net revenues. Currently, the Airport spends about $80,000 to collect almost $45,000. The annual fee option management will implement will lower costs to near-revenue levels and free up staff time to address other leasing duties.

2. *Managing Accounts Receivable, Security Deposits and Insurance Coverage*

Management agrees that monitoring delinquent receivables is important and has been monitoring receivables all along. Moreover, we recognize that delinquent accounts are a reality of every business. To this end, the Airport last year purchased an electronic leasing system to centralize the tracking of correspondence, insurance renewals, security deposits, annual concession revenue certifications, and other important events for each lease. Moreover, as acknowledged by the Auditor, the Airport has a new policy for handling and managing delinquent receivables. Management believes that these new measures will make a significant improvement in managing delinquent accounts. Further, most of the larger receivable amounts are associated with airlines or leases that are backed by bank mortgages. These mortgage-backed leases provide a strong financial contingency, due to the collateral position each bank has in the properties. Thus, the Airport has been willing to work with tenants during these difficult financial times.

It should be noted that several of the Airport's lease properties went through bankruptcy filing last year, and each time the underlying bank brought the rents current. Management is and has been in conversation with the other large delinquent accounts, of which each also has a bank mortgage.

It should be further noted that, although management is in the process of centralizing tracking information, staff is nonetheless tracking these actions.

Of the $452,355 in accounts receivable, $324,376 is considered fully collectable.

The table below provides a breakdown of the aging report. The AR Balance column is an assortment of small to modest balances, with 67 percent in the 30 day category. Staff is continuing to work these accounts for collection.

	AR Report	AR is Collectable	Remaining AR Balance	% Remaining AR Balance
30 Days	$ 252,225	$ 166,265	$ 85,960	67%
60 Days	34,147	23,252	10,895	8%
90 Days	11,509	6,901	4,608	4%
120 Days	7,982	6,901	1,081	1%
Over 120 Days	146,492	121,057	25,435	20%
Total	$ 452,355	$ 324,376	$ 127,979	100%

For security deposits and insurance, staff will work with the City's Financial Management Department and Risk Management Division to reaffirm roles and responsibilities and to utilize the new leasing software to track renewals and compliance.

3. *Quality Assurance Lease and Concession Monitoring*

Management agrees that more can be done to formally document leasing visits and tenant responses. As the Auditor indicated, last year staff began implementing a practice of making periodic site visits to each of their lease accounts, including weekly visits with concessionaires and quarterly meetings with rental car companies. These meetings have been beneficial for staff and have helped improve professional relationships with the lessees. Staff has been instructed to record all tenant visits in the new leasing software to better document their visits, along with the resulting actions requested and taken.

Please note that on-site lease inspections become impractical with many clients, since the Airport does not own the actual facilities and because of security concerns with facilities such as The Boeing Company and Gulfstream Aerospace Corporation.

The new practice of enhanced account management is being formalized in the new concourse concessions contract, with the inclusion of a detailed quality control checklist for use at the weekly walk-through. Please note that although this checklist is not required, the Airport is currently negotiating inclusion of one with the new concessionaire.

It should also be noted that the Airport's concessions are selected based in part upon their quality assurance process. The Airport's current implementation of this process exceeds that of most comparable facilities.

As for the Auditor's discussion of cash POS controls and Airport staff surprise inspections, management believes this is an audit skill set and, therefore, will not ask staff to conduct such inspections. Management will study the benefit of contracting with an audit service to periodically conduct concessionaire audits.

4. Shuttle Van and Limousine Improvement Opportunities

As the auditor correctly recognized, tracking ground transportation is an extremely time consuming undertaking, when compared to the revenue it produces. As indicated previously, the Airport will implement a fixed annual fee program to simplify the administration of ground transportation, both for staff and drivers. With the change to an annual fee approach, this problem will be eliminated. This will reduce administrative overhead and thus increase net revenues. Currently, the Airport spends about $80,000 to collect almost $45,000. The annual fee option management will implement will lower costs to near-revenue levels and free up staff time to address other leasing duties.

Again, we wish to thank the Auditor for assisting the Airport in improving internal controls and operations.

Sincerely,

MARIO RODRIGUEZ
Director, Long Beach Airport

MR:JC:km

cc: Patrick H. West, City Manager
Suzanne Frick, Assistant City Manager

Appendix B – Additional Information on the Audit's Scope and Methodology

Following is additional information on the Audit Scope and Methodology used in the audit.

To understand the background context of the issues and develop audit criteria, we reviewed the language and intent of nine lease agreements, five concession agreements, and the permitting and oversight process for ground transportation providers

Additionally, as part of assessing the level of management and oversight of the lease and concession agreements as well as ground transportation service providers, we interviewed key Long Beach Airport management and staff to determine their roles and responsibilities regarding the contract and what monitoring efforts are undertaken. Further, we conducted on-site visits of selected lease holders and all concession areas to determine whether lessee activities appeared in compliance with lease terms of use and whether the Airport conducted appropriate quality assurance oversight with its food and beverage as well as gift, news, and retail concessionaires. Furthermore, we also interviewed these same lessees and concessionaires to obtain confirmation of the Airport's oversight efforts.

To determine whether the Long Beach Airport effectively manages its lease and concession agreements, we performed the following tasks:

- Reviewed the following key Airport documents:
  - City municipal code, and policies and procedures related to airport operations and city services
  - Long Beach Airport's related policies and procedures
  - FAA assurances and regulations regarding the Airport
  - Airport schedules of landing fees
  - Fourteen land leases and subleases
  - Restaurant and bar concession agreements
  - Overview of Commercial Use Permits
  - Selected rental car agreements
  - Limousine, shuttle, and van agreement spreadsheet with revenues
  - RFP for new terminal concession contracts
  - Background information on the Gift, News, and Retail concessionaire
- Evaluated the revenue statements and accompanying concession fee payments submitted by the lessees and concessionaires.
- Gathered operating and financial data from three airports of similar size and operations to the Long Beach Airport.
- Verified whether monthly percentage fee payments were in line with lease and/or concession agreement provisions.

- Verified whether monthly fuel flowage reporting requirements were in line with lease agreement provisions.
- Compared the security deposit requirements described in each applicable lease and/or concession agreement against the Airports fiscal records.
- Compared the insurance requirements (General, Liability, Worker's Compensation, etc.) described in each applicable lease and/or concession agreement against Airport records.
- Evaluated the Airports process for managing delinquent account collections.
- Evaluated underling supporting documents for the revenues reported by lessees and/or concessionaires.
- Evaluated the Airport's process and management of concessionaire quality assurance reviews.