

Memorandum



CITY OF DALLAS
(Report No. A15-001)

DATE: October 31, 2014

TO: Honorable Mayor and Members of the City Council

SUBJECT: Audit of Controls over Department of Convention and Event Services' Cash Receipts and Collections¹

The Department of Convention and Event Services' (CES) does not have sufficient monitoring controls over the Centerplate Contract (Contract) for food and beverage services (see textbox). Specifically:

- The CES does not have formal documented contract monitoring policies and procedures
- The CES does not have sufficient contract monitoring activities
- Not all Contract payment provisions are followed consistently

Background

Since Fiscal Year (FY) 2003, the City of Dallas (City) has had a Contract with Centerplate to exclusively provide food and beverage services at the Convention Center.

Centerplate collects and remits revenue to the City from the following activities: (1) alcoholic beverage sales; (2) vending machines sales; (3) permanent and mobile food / beverage stand sales; and, (4) catering services. In return, Centerplate is reimbursed for allowable expenses and receives an agreed upon percentage of the net operating profits and management fees.

For FY 2012 and FY 2013, the City received revenue of \$8.8 million and \$12.2 million, respectively, and paid Centerplate \$7.6 million and \$8.7 million, respectively.

Source: Centerplate Contracts and CES

¹ We conducted the *Audit of Controls over Department of Convention and Event Services' Cash Receipts and Collections* under the authority of the City Charter, Chapter IX, Section 3. This audit was part of our Fiscal Year 2013 Audit Plan approved by the City Council. This performance audit was conducted 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. The audit objective was to evaluate the efficiency, effectiveness, or adequacy of internal controls over CES' cash receipts and collections. The scope of the audit included Contract revenue in the form of cash and cash equivalents occurring between FY 2012 and FY 2013; however, certain other matters, procedures and transactions occurring outside that period may have been reviewed to understand and verify information during the audit period. We interviewed CES and Centerplate personnel, judgmentally selected samples, reviewed applicable supporting documentation and policies/procedures provided by CES and Centerplate, and performed various analyses. We also reviewed applicable Administrative Directives, Council Resolutions, and Administrative Actions. Additionally we observed two Centerplate events held at the Kay Bailey Hutchison Convention Center.

- The CES contract administration was not timely and in accordance with City of Dallas (City) Administrative Directives

As a result, CES cannot ensure Centerplate complies with Contract terms, the City receives all revenue due, and Centerplate's requests for expense reimbursement are accurate and in accordance with the Contract terms.

Formal Documented Contract Monitoring Policies and Procedures Are Not In Place

The CES does not have formal documented policies and procedures for Contract monitoring. The CES does, however, have formal policies and procedures for certain financial activities that are relevant to monitoring the Contract, such as processing Accounts Receivable (AR) and Accounts Payable (AP). Without formal documented contract monitoring policies and procedures, CES cannot ensure effective internal controls and that CES personnel are performing their duties consistently to reduce the risk of financial loss and Contract noncompliance.

Policies and Procedures

Policies and procedures:

- Ensure that fundamental organizational processes are performed in a consistent way that meets the organization's needs
- Exist to effect internal controls

Source: COSO and the Office of the City Auditor

The Committee of Sponsoring Organizations² (COSO) identified established policies and procedures as a control activity needed to manage risk.

The CES Does Not Have Sufficient Contract Monitoring Activities

The CES's contract monitoring activities are not sufficient to periodically validate Centerplate's internal control effectiveness and compliance with Contract terms. According to CES, certain monitoring activities are performed, such as: (1) periodic reviews of Centerplate's worksheets, general ledger, and financial statements; (2) expense ratios and fluctuation analyses; and, (3) an annual cash reconciliation of reported cash receipts to amounts recorded in the City's general ledger.

Monitoring Activities

Centerplate is contractually responsible for the internal control activities for food and beverage services at the Convention Center.

The CES is responsible for monitoring the effectiveness of Centerplate's internal controls.

Monitoring activities assess whether internal controls are present and functioning as intended.

Source: COSO and the Office of the City Auditor

² The COSO is recognized as a leading framework for designing, implementing, and assessing the effectiveness of internal control.

While these monitoring activities provide some level of contract oversight, CES's reliance on contractor prepared documents without additional verification would not necessarily disclose contractor's internal control weaknesses or contract noncompliance. In addition, the documentation of monitoring activities observed during the audit did not support that CES monitoring activities were consistently performed or appropriately documented. For example, CES' monitoring activities did not identify that Centerplate's daily cash collections for nine of 30 deposits sampled (30 percent) were not submitted timely. Although the nine events were small, it took three to five business days to deposit the cash collections into the City's bank account.

More detailed and documented monitoring activities would increase CES's ability to identify internal control weaknesses and contract noncompliance, such as:

- Observing Centerplate's cash collection processes or periodically reconciling and documenting:
 - Daily cash receipts to supporting documentation, such as Centerplate's activity report, cashiers' work sheets, and cash register tapes
 - Monthly credit card sales and catering checks to supporting documentation, such as Centerplate's activity report, Heartland's credit card report, detailed catering check logs, copies of catering checks, banquet event orders, contracts, invoices, and Centerplate's bank statement for Kay Bailey Hutchison Convention Center (Convention Center)
 - Centerplate's reimbursement expenses to supporting documentation, such as invoices
- Monitoring daily cash collections to be deposited into the City's bank account within a reasonable time frame as required by the Contract
- Assessing the accuracy and completeness of food and beverage revenue and allowable expenses, such as requiring Centerplate to periodically submit independent financial or performance audits as provided by the Contract

As a result, CES is not monitoring sufficiently to assess Centerplate's internal control effectiveness and ensure compliance with Contract terms.

The COSO identified monitoring as a key component of the organization's assessment of the effectiveness of internal controls.

Not All Contract Payment Provisions Are Followed Consistently

Centerplate did not consistently follow certain Contract payment provisions. Specifically, Centerplate does not deposit revenue received from credit card sales and checks written to Centerplate for catering services into a City bank account on a weekly basis. Instead, Centerplate deposits this revenue into a corporate bank account and submits a check to the City on a monthly basis.

As a result, the City is at risk for financial losses on Contract revenue deposited into Centerplate's corporate bank account in the event of a Centerplate bankruptcy. Additionally, the City is foregoing potential interest earnings.

Section XXII, *Payments* in the Request for Competitive Sealed Proposal (RFCSP) issued in 2012 state:

"An amount equal to all checks and credit card charges received by contractor will be deposited in a City of Dallas bank account net any sales or alcoholic beverage taxes on a weekly basis. These solicitations are incorporated into the final Contracts by reference."

The CES' Contract Administration Was Not Timely and in Accordance with City's Administrative Directives

The CES' contract administration was not timely and in accordance with City's Administrative Directive 4-5, *Contracting Policy* (AD 4-5). Specifically:

- The CES and Centerplate operated without a formal contract for approximately nine months beginning in December 2012. According to CES management, they began the contract renewal process in January 2012, and the RFCSP was advertised in July 2012.
- The CES did not maintain a complete executed Contract, including the counterparts (a contract that is signed in parts – each deemed to be an original, but taken together constitutes one contract) for the third renewal supplemental agreement.

As a result of operating without a formal contract for approximately nine months, Centerplate and the City did not consistently follow established Contract payment practices. Specifically, from:

- December 2012 to June 2013 – The City withheld \$6.2 million from Centerplate for Centerplate's net operating profit share, management fees, and allowable expenses

- March 2013 to July 2013 – Centerplate withheld \$2.9 million from the City for collections of credit card sales/catering services checks³

In general, operating without a formally executed contract increases the City's risk for Contract noncompliance.

AD 4-5, Section 5, *Administrative Responsibilities* (effective as of 2006, 2011, and 2012) states that it is the department directors' responsibility to:

- *"Ensure that all contracts are properly executed prior to commencement of work or purchase (when applicable), and submit the record copy of the executed contract, including all exhibits, documents incorporated by reference, and necessary supporting documentation to the City Secretary upon execution of the contracts. Vendors and consultants should not be authorized to begin work until the contract, bonding (if bonding is required), and appropriate insurance, including amendments, have been fully executed and delivered."*
- *"Ensure that all contractual activities are adequately documented and that record copies of complete documents are maintained in accordance with requirements established in this Directive, the Public Information Act, the Local Government Records Act, and other applicable laws or policy."*

We recommend the Director of CES:

- I. Develop and implement formal documented policies and procedures for Contract monitoring that provide guidance to CES personnel on their Contract monitoring duties
- II. Improve and document monitoring activities to assess Centerplate's internal control effectiveness and Contract compliance by periodically: (1) observing and reconciling financial transactions performed by Centerplate; (2) validating expenses claimed as allowable; (3) validating compliance with Section XXII, Payments in the RFCSP; and, (4) validating the accuracy and completeness of food and beverage revenue and allowable expenses by requiring Centerplate to periodically submit independent financial or performance audits as authorized by the Contract
- III. Monitor to ensure that Centerplate complies with Contract terms by depositing amounts equal to all checks and credit card charges net of any sales or alcoholic beverage taxes into a City bank account on a weekly basis

³ In accordance with the Contract from:

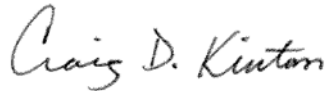
- October 2012 to July 2013 – Centerplate processed \$2.6 million in daily cash collections for food and beverage sales
- December 2012 to February 2013 – Centerplate remitted \$3 million to the City for credit card sales/catering services checks

IV. Implement effective contract administration procedures to ensure contracts are timely renewed, properly executed, and in accordance with AD 4-5

Please see Attachment I for Background information related to the audit and Attachment II for Management's Response to the report recommendations.

We would like to acknowledge CES's and Centerplate's cooperation during this audit. If you have any questions or need additional information, please contact me at 214-670-3222 or Carol Smith, First Assistant City Auditor, at 214-670-4517.

Sincerely,



Craig D. Kinton
City Auditor

Attachments

C: A. C. Gonzalez, City Manager
Ryan S. Evans, First Assistant City Manager
Jeanne Chipperfield, Chief Financial Officer
Forest E. Turner, Assistant City Manager
Ron King, Director – Department of Convention and Event Services

Attachment I

Background

According to the Department of Convention and Event Services (CES), the Kay Bailey Hutchison Convention Center (Convention Center) is one of the largest, most versatile convention complexes in the nation. The Convention Center provides approximately one million square feet of space which includes 200,000 square-foot column-free exhibit hall, three ballrooms, 88 total meeting rooms, and a 1,750 person theater. The Convention Center is managed by CES.

Centerplate Contract

Since Fiscal Year (FY) 2003, the City of Dallas (City) has contracted with Service America Corporation, a Delaware Corporation doing business as Centerplate, to exclusively provide food and beverage services at the Convention Center. Centerplate collects and remits revenue to the City from the following activities: (1) alcoholic beverage sales; (2) vending machines sales; (3) permanent and mobile food/beverage stand sales; and, (4) catering services. In return, Centerplate is reimbursed for allowable expenses and receives an agreed upon percentage of the net operating profits and management fees. The following are significant Centerplate Contract (Contract) payment terms:

Initial Contract (2002): The profit sharing between Centerplate and the City was as follows:

- Ninety percent of the net operating profits on food and beverage and all vended products are paid to the City and ten percent to Centerplate when annual gross sales are up to \$8.5 million
- Eighty percent of the net operating profits on food and beverage and all vended products are paid to the City and twenty percent to Centerplate when annual gross sales are greater than \$8.5 million

The annual Centerplate management fee was \$275,000 for the first seven years with a provision for a five percent increase for each renewal year.

Current Contract (2012): The profit sharing between the City and Centerplate is now a fixed 95 percent of net operating profits on food and beverage and all vended products to the City and five percent to Centerplate.

The annual Centerplate management fee is \$450,000 for the first five years and \$500,000 for the remaining five years.

Both Contracts include the following provisions:

- Centerplate pays the City a concession equal to 38 percent of gross sales on all alcoholic beverage sales
- The City pays Centerplate the same allowable expenses except for personnel expenses for three permanent staff positions (General Manager, Catering Manager, and Executive Chef) which are reimbursed according to the 2012 Contract

Convention and Event Services

The CES is responsible for monitoring the Contract, including reviewing and approving all revenue deposits received from Centerplate and reimbursement payments made by the City to Centerplate for Centerplate's share of net operating profits, management fees, and allowable expenses.

Related City Council Resolutions and Administrative Actions

City Council Resolution No. 02-2277 (August 14, 2002) – The City Council authorized an initial seven year Contract with Centerplate, including three one-year renewal options. The Contract term was from October 1, 2002 to September 30, 2009.

City Council Resolution No. 09-1895 (August 12, 2009) – The City Council authorized the first Contract renewal option. The initial Contract term was extended for an additional year from October 1, 2009 to September 30, 2010.

Administrative Action No. 11-0353 (January 10, 2011) – The City processed the second Contract renewal option. The Contract term was extended for an additional year from October 1, 2010 to September 30, 2011.

Administrative Action No. 11-2636 (September 26, 2011) – The City processed the third Contract renewal option. The Contract term was extended for an additional year from October 1, 2011 to September 30, 2012.

Administrative Action No. 12-2855 (October 25, 2012) – The City processed a two-month extension of the Contract from October 1, 2012 to November 30, 2012.

City Council Resolution No. 12-2726 (November 14, 2012) – The City Council authorized an initial ten year Contract with Centerplate, including one five-year renewal option. The term of the initial Contract is for December 1, 2012 to November 30, 2022.

Methodology

- Reviewed the following:
 - Initial and current Contracts as well as available supplemental agreements
 - City Council Resolutions No. 02-2277, No. 09-1895, and No. 12-2726
 - Administrative Actions No. 11-0353, No. 11-2636 and No. 12-2855
 - Administrative Directive (AD) 4-5, *Contracting Policy*, effective as of 2006, 2011, and 2012
 - AD 4-13, *Cash and Debt Management Policies and Procedures*
 - The CES' Accounts Payable and Accounts Receivable Policies and Procedures
 - Centerplate's Cash Handling Policies and Procedures Manual
 - The CES' FY 2013 annual revenue reconciliation
- Interviewed CES and Centerplate personnel
- Observed Centerplate's cash handling procedures at two events
- Judgmentally selected 30 days and reviewed daily cash collections
- Judgmentally selected and reviewed six months of:
 - Revenue deposits made by Centerplate to the City
 - Payments made by the City to Centerplate for allowable expenses

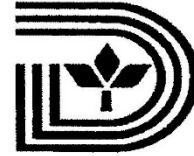
Management's Response

Memorandum

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OCT 15 2014

City Auditor's Office



CITY OF DALLAS

DATE: October 15, 2014
TO: Craig D. Kinton, City Auditor
SUBJECT: Response to Audit Report:
Audit of Controls over Department of Convention and Event Services'
Cash Receipts and Collections

Our responses to the audit report recommendations are as follows:

The Convention and Event Services Department (CES) appreciates the time and professionalism demonstrated by the City Auditors office in developing their report. Management considers the audit to be a useful tool in assessing vulnerabilities and mitigating potential risk.

Recommendation I

We recommend the Director of CES develop and implement formal documented policies and procedures for Contract monitoring that provide guidance to CES personnel on their Contract monitoring duties.

Management Response / Corrective Action Plan

Agree Disagree

As noted in the auditor's report, CES has contract monitoring procedures in place. CES will develop and implement formal documented policies and procedures for contract monitoring that will provide guidance to CES personnel.

Implementation Date

March 31, 2015

Responsible Manager

CES Assistant Director

Recommendation II

We recommend the Director of CES II improve and document monitoring activities to assess Centerplate's internal control effectiveness and Contract compliance by periodically: (1) observing and reconciling financial transactions performed by Centerplate; (2) validating expenses claimed as allowable; (3) validating compliance with Section XXII, Payments in the RFCSP; and, (4) validating the accuracy and completeness of food and beverage revenue and allowable expenses by requiring

Audit of Controls over Department of Convention and Event Services' Cash Receipts and Collections

Centerplate to periodically submit independent financial or performance audits as authorized by the Contract

Management Response / Corrective Action Plan

Agree Disagree

CES will improve and document monitoring activities to assess Centerplate's internal control effectiveness and contract compliance. CES will require an independent periodic audit in the future of Centerplate financials which shall include the following elements:

- Review of selected monthly settlement statements for the selected period
- Review of independent auditor selected events which shall typically be one event per month for the selected period
- Review of independent auditor selected cash, credit card, check, and wire transfers for the selected period
- Review of independent auditor selected reimbursable expenses for the selected period

Implementation Date

March 31, 2015

Responsible Manager

CES Assistant Director

Recommendation III

We recommend the Director of CES monitor to ensure that Centerplate complies with Contract terms by depositing amounts equal to all checks and credit card charges net of any sales or alcoholic beverage taxes into a City bank account on a weekly basis.

Management Response / Corrective Action Plan

Agree Disagree

CES will monitor to ensure that Centerplate complies with the Contract terms by depositing amounts equal to all checks and credit card charges net of any sales tax or alcoholic beverage tax into a City bank account on weekly basis.

Implementation Date

March 31, 2015

Responsible Manager

CES Assistant Director

Recommendation IV

We recommend the Director of CES implement effective contract administration procedures to ensure contracts are timely renewed, properly executed, and in accordance with AD 4-5.

Management Response / Corrective Action Plan

Agree Disagree

On November 14, 2012, Dallas City Council approved an agenda item to award a contract to Centerplate to provide food and beverage services for the Convention Center. Due to on-going contract negotiations between the City Attorney's Office, CES, and Centerplate and in order to fulfill our contractual obligations with our mutual clients, CES and Centerplate operated under the terms and conditions of the previous contract. CES personnel continued to monitor the contract; however, without an executed contract in place the City had no legal authority to pay for services rendered. Upon the execution of the contract CES and Centerplate reconciled all financial transactions.

CES will implement effective contract administration procedures to ensure contracts are timely renewed, properly executed, and in accordance with AD 4-5.


Implementation Date

March 31, 2015

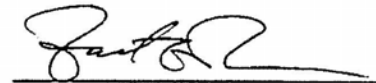
Responsible Manager

CES Assistant Director

Sincerely,



Ron King, Director
Department of Convention and Event Services



Forest Turner
Assistant City Manager