

APPENDIX 1

Parks, Forestry and Recreation Division

Concession Agreements Review

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Auditor General's Office

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EXECUTIVE SUMMARY

Part of an ongoing series of revenue audits

The Auditor General's 2009 Audit Work Plan included ongoing reviews of the City's revenue billing, collection and related processes. The intent of including the audit of revenue sources in the work plan was to systematically address various City revenue streams over a period of time. The review of concession agreements is part of this series of revenue audits.

Other revenue streams recently audited include:

- Land Transfer Tax
- Property Tax Appeals and Refunds
- Parking Tags
- Ferry Services
- Pay and Display Parking Operations, Toronto Parking Authority
- Children's Services - Subsidies

Similar issues identified in a 2006 Auditor General report on the Facilities and Real Estate Division

The issues identified in this current report are similar to those contained in a report entitled "Review of the Administration of Leases on City Owned Property" dated July 8, 2006. While the July 2006 report focuses on the administration of property leases managed by the Facilities and Real Estate Division, certain components of that report have relevance to concession agreements which is the subject of the current report.

Certain of the issues in the 2006 report centered around the following:

- The need to independently verify that the City is receiving the revenue to which it is entitled
- The need to ensure that adequate financial information is provided to the City by third parties
- The need to follow-up on old outstanding arrears
- The need to review as to whether or not interest should be charged on old outstanding receivable amounts

Recommendations from 2006 audit report have not been fully addressed

While the revenue amounts relating to concession revenue are considerably less than the revenue earned from property leases, the issues addressed in the 2006 report continue to have relevance four years later.

One of the benefits of any audit process is the ability to leverage issues identified and recommendations made pertaining to one division with other divisions throughout the City. In fact, one of the standard recommendations in most of our audit reports is a requirement that divisions review audit recommendations to determine their relevance in their divisions. In the case of the 2006 report, it appears that the recommendations made at that time have not been fully addressed as we have identified similar issues in our review of concession agreements.

City-wide concession revenue for 2009 was \$3 million. The Parks, Forestry and Recreation Division share of 2009 concession revenue was approximately \$1 million.

Concessions are businesses operating on City property under contract or license

Concessions are businesses operating on City property under a contract or license within a certain geographical area. These agreements encompass a wide spectrum of businesses from small operations such as bicycle rentals to larger operations including theme parks and restaurants. Payment to the City is based on a percentage of gross revenue, a flat rate or combination of both.

\$3.5 million outstanding, \$1.8 million outstanding over 12 months

The City also bills concessionaires for property taxes, rent, hydro, and other costs such as advertising and maintenance. As of June 30, 2010, \$3.5 million was outstanding in property taxes, rent, hydro and other services provided by the City to concessionaires. Approximately, \$1.8 million has been outstanding for over 12 months with some accounts outstanding for over five years and include amounts currently being contested by concessionaires. Due to the length of time certain receivables have been outstanding, their collectability becomes more difficult.

Summary of issues and recommendations

Our review identified the following:

- Policies and procedures for follow-up on past due accounts need to be formalized. Property tax and expense collection procedures should be revised to ensure timely recovery of these amounts.

- Procedures should be implemented to validate sales reported by concessionaires. Currently, City revenue amounts are based on sales reported by concessionaires with no verification by City staff. Consequently, staff is not in a position to ascertain whether or not the City is receiving all the revenue to which it is entitled.
- Collection methods should be expanded to include pre-authorized payment, electronic fund transfers and on-line banking payments.
- Certain concession agreements require payment once at year end. A more frequent payment schedule would improve cash management, increase City interest revenue and reduce the potential for bad debts
- Concession agreements need to be standardized and should as a minimum include "right to audit" clauses.

Our report contains seven recommendations. The implementation of these recommendations will contribute to improvements in the management of concession revenue and receivables.

BACKGROUND

City contracts with various concessionaires

City concession agreements vary from business to business. Agreements include contracts with a variety of concessionaires from bicycle rentals and food service to theme park operators.

Contract terms vary

Contract periods vary according to the nature of the business. Payments to the City are based on a percentage of total concession revenue, a flat rate or some combination of both. The amount or percentage of rent is established through a competitive bidding process.

Review focused on Parks, Forestry and Recreation

The City Parks, Forestry and Recreation, and Facilities and Real Estate Divisions manage the majority of City-owned properties. This review focussed on policies and procedures administered by the Parks, Forestry and Recreation Division for collecting and monitoring concession revenue.

This audit did not include a review of concession agreements related to properties managed by the Facilities and Real Estate Division. Several concession agreements in the Facilities and Real Estate Division were being revised in early 2010, and the Division is in the process of implementing contract changes. A future audit will include a review of concession agreement contracts administered by the Facilities and Real Estate Division. In any event, the recommendations in this report will have applicability to the management of concession revenues in other Divisions.

Divisional improvement initiatives are underway

The Business Services Unit of the Management Services Branch, in the Parks, Forestry and Recreation Division administers divisional concession agreements. The Parks, Forestry and Recreation Division has undertaken a number of initiatives to improve controls in the management of concession agreements. These initiatives include implementation of a credit check protocol to reduce potential collection issues and development of an electronic lease database in the City's SAP Financial System.

AUDIT OBJECTIVES, SCOPE AND METHODOLOGY

Why we conducted this review

The Auditor General's 2009 Audit Work Plan included a review of the City's revenue billing, collection and related processes. The intent in including the audit of revenue sources in the work plan was to systematically address various City revenue streams over a period of time. This review is part of a series of revenue stream audits.

Objectives of the review

The objective of our review was to determine the adequacy of controls over the administration and collection of concession agreements and revenues.

The review focused on the administration of concession agreements, revenue collection and follow-up on outstanding accounts by the Parks, Forestry and Recreation Division.

Steps in the review

Our audit methodology included:

- Review of concession policies and procedures
- Review of Council reports
- Review of documents, verification of concessionaire compliance with agreement terms and conditions
- Interviews with Parks, Forestry and Recreation Division staff and various other related City Divisions
- Review of information technology systems, processes and related data maintained by Parks, Forestry and Recreation
- Review of reports and best practices at other North American cities including Hamilton, Seattle, Los Angeles and New York.

We conducted this audit in accordance with generally accepted government auditing standards

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 believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

AUDIT RESULTS

A. REVENUE COLLECTION PROCESSES REQUIRE IMPROVEMENT

The Parks, Forestry and Recreation Division administers 21 concession agreements. These agreements include a combination of fixed and variable concession payments. Variable concession payments are based on a percentage of sales.

In 2009, City-wide concession revenue totalled \$3 million

In 2009, City-wide total concession revenue totalled \$3 million. Parks, Forestry and Recreation concessions comprise \$1 million of this total.

A.1 Billing and Collection of Property Taxes and Concession Costs Requires Improvement

In a number of concession agreements the Parks, Forestry and Recreation Division pays for certain costs, such as property taxes, utilities and maintenance and later requests reimbursement from concessionaires.

Approximately \$1.8 million outstanding for over 12 months

As of June 30, 2010, \$3.5 million was outstanding in property taxes, rent, hydro and other services provided by the City to concessionaires. Approximately \$1.8 million has been outstanding for over 12 months with some accounts outstanding for over five years. These outstanding accounts include amounts currently being contested by concessionaires. Out of the total of \$1.8 million outstanding, \$1.75 million is comprised of four accounts that are being addressed by either Legal Services or negotiated Corporately.

A formal documented procedure for follow-up on outstanding past due accounts needs to be developed. The issues identified below relate to divisional practices for collecting outstanding accounts.

a) Recovery of City Concession Costs

Billing and collection of concession costs are not timely

Billing and collection of concession costs are not performed on a timely basis. Concession costs include utilities and maintenance costs incurred by the concessionaire. In some instances, these costs are billed and collected annually.

\$1.4 million outstanding for expenses already paid by the City

Timely collection of concession costs minimizes the potential for bad debt and related collection expenses, improves cash management and increases interest revenue. As of June 30, 2010, approximately \$1.4 million was outstanding for expenses the City had already paid or incurred, and awaiting reimbursement. This amount includes \$670,000 disputed by lessees and concessionaires currently being negotiated.

Property taxes paid in advance by the Division then billed to concessionaires

b) Recovery of Property Taxes

Similar issues exist in the billing and collection of property taxes. Property taxes are first paid through an inter-departmental charge by the Division then billed to concessionaires. Some agreements contain provisions for late payment charges, however management does not consistently exercise its right to collect late payment charges.

The Facilities and Real Estate Division bills property taxes in advance on a monthly basis. The amount is estimated based on previous year taxes and adjusted accordingly at the end of the year. A similar practice should be considered by the Parks, Forestry and Recreation Division.

c) Management Explore Options to Accept Concession Payments on a More Frequent Basis

Our review of payment terms for concession agreements indicated varying payment schedules ranging from monthly to once a year.

From a cash management perspective, a more frequent payment schedule is preferred

From a financial and operational perspective, a more frequent payment schedule is desirable. Receiving payments in installments rather than one lump sum at the end of the period minimizes the risk of bad debts. We appreciate there may be circumstances where a less frequent payment schedule is appropriate. An example might be a small seasonal business. These need to be evaluated on a case-by-case basis.

Recommendations:

- 1. The General Manager, Parks, Forestry and Recreation, develop written procedures for follow-up on past due accounts.**
- 2. The General Manager, Parks, Forestry and Recreation, revise concession cost and property tax billing and collection practices to include more timely collection.**
- 3. The General Manager, Parks, Forestry and Recreation, develop a process to evaluate concession payment terms for new or existing agreements at the time of renewal to include, where appropriate, terms requiring more frequent payments.**

A.2 Management Explore Options to Validate Sales Reported by Concessionaires

The Division relies on concessionaire reported sales

Concessionaires forward payment and sales information to the Parks, Forestry and Recreation Division. The Division relies on concessionaire reported sales information to collect concession revenue. The Division does not have a process to verify the information submitted. Validation of concessionaire records by the Division is a significant control as payments due the City are based on a percentage of concessionaire reported sales. The City cannot detect concessionaire reporting inaccuracies without a review by City staff.

The City Facilities and Real Estate Division has initiated a process for validating concession payment information. The Parks, Forestry and Recreation Division should consider a similar initiative for concession revenue.

Recommendation:

- 4. The General Manager, Parks, Forestry and Recreation, implement a process, where applicable, to validate concessionaire reported sales by City staff on a periodic basis.**

A.3 Expanding Payment Options to Include Pre-Authorized Payment, Electronic Funds Transfer, On-Line Banking and Post Dated Cheques

Collection methods should be expanded

The Parks, Forestry and Recreation Division does not have a formal documented procedure for collecting concession payments. Payments are received through mailed cheques or picked up by City staff in person.

Payment methods should be reviewed and expanded to include other options for concessionaires including pre-authorized payment, electronic fund transfer, on-line banking and post-dated cheques.

Recommendations:

5. **The General Manager, Parks, Forestry and Recreation, develop written procedures for collecting concession payments.**
6. **The General Manager, Parks, Forestry and Recreation, explore other collection methods including pre-authorized payment, electronic fund transfer, on-line banking and the use of post-dated cheques.**

B. STANDARDIZATION OF CONCESSION AGREEMENT TERMS AND CONDITIONS

The City inherited a wide range of concession agreements at the time of amalgamation. Some of these pre-amalgamation agreements are still in place. There is a need to standardize agreement terms and conditions and include management controls not incorporated into agreements. Certain inconsistencies and missing management control provisions include the following:

Agreement terms, conditions and controls should be standardized to the extent possible

- Not all agreements provide for audit of concessionaire records and sales by City staff
- Agreements do not require concessionaires to maintain adequate financial records
- Agreements do not provide remedies for situations where concessionaires do not comply with agreed-upon terms.

Certain concession agreements may need to vary to some extent, depending on the nature and size of the business. However, the use of a standard agreement template which includes common management control provisions will improve concession agreements.

Recommendation:

7. **The General Manager, Parks, Forestry and Recreation, in consultation with the City Solicitor, review new and existing concession agreements at the time of renewal, for opportunities to standardize management control clauses.**

CONCLUSION

This report contains seven recommendations related to improvements in concession revenue collection and administration processes. Our recommendations relate to the need to:

- Follow-up on past due accounts
- Revise and formalize billing and collection processes
- Validate concession sales
- Revise concession agreements

Implementing the recommendations contained in this report will strengthen controls, improve revenue collection and result in operational efficiencies.