



Memorandum



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To: Hon. Carlos A. Gimenez, Mayor, Miami-Dade County
Hon. Joe A. Martinez, Chairman, Board of County Commissioners
and Members, Board of County Commissioners

From: Christopher Mazzella, Inspector General

Date: October 31, 2012

Subject: *OIG Audit of the Agreements Between Miami-Dade County and Basketball Properties, Ltd., et.al., to Operate the American Airlines Arena; Audit Close-out, Ref. IG11-34*

The Office of the Inspector General (OIG) issued its final audit report on the Agreements between Miami-Dade County and Basketball Properties, Ltd. (BPL) on May 31, 2012. At that time, we requested that the County administration provide a status report within 90 days pertaining to the 23 recommendations that resulted from our audit. The Internal Services Department (ISD) submitted a 90-day status report to the OIG on August 29, 2012 (Attachment A). Subsequent communication between the OIG and ISD about its responses to outstanding issues followed, culminating in ISD's latest response to the OIG dated October 26, 2012 (Attachment B). In its initial 90-day response, ISD described its commitment to address and implement protocols for 21 of the 23 OIG recommendations. We are pleased with the County implementing procedures that strengthen its administration of its fiscal and operational responsibilities pertaining to the county-owned facility.

There remain, however, two outstanding issues relating to audit recommendation nos. 11 and 23. Recommendation No. 11 proposes that the County seek to recoup, via an adjustment to BPL's annual reported revenues, BPL capital expenditures totaling \$3.3 million (fiscal years 2005 – 2010), that were in excess of its purported capital budget amounts for those years. ISD's position is that these expenditures were "customary in accordance with industry standards" and it will not seek to recoup them. The OIG reaffirms its position that included in these expenditures were those made primarily for the benefit of the team, not the facility.

Recommendation No. 23 proposes that the County seek to recoup \$668,100 of questioned expenses (fiscal years 2005 – 2010), as well as additional monies paid out as executive compensation, bonuses, incentives, and commissions that we contend are

unallowable pursuant to the Agreements.¹ The audit-identified questioned expenses include: \$614,000 paid to lobbyists, \$12,300 for political contributions, \$17,500 for charitable contributions, and \$24,300 for non-arena related memberships and dues. ISD states that it believes that the OIG-identified questioned costs are, in its opinion, legitimate business expenses that are reasonable and customary. For the current fiscal year 2013, ISD has approved BPL's budget for these items totaling \$326,684—\$294,000 for lobbyist fees, \$5,000 for charitable contributions, and \$27,684 for membership fees/dues.

Moreover, ISD states that it will allow BPL to continue to include the salary of a BPL vice president, as an operating cost, notwithstanding the fact that executive compensation is an unallowable Arena operating expense, pursuant to the Agreements. We reaffirm our position that the subject expenses are not appropriate given the nature and the terms of the County's business arrangement with BPL. In addition, ISD states that it met with the County Attorney's Office to discuss what comprises executive compensation and will not be pursuing this issue.

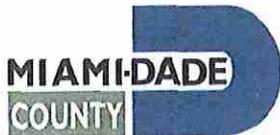
As you recall, this audit was partially predicated on the fact that Arena net operating revenues have never exceeded the threshold triggering profit sharing between BPL and the County. In other words, since its inception, the County has yet to receive any portion of profits from the Arena, despite the fact that profit sharing was a major selling point for the approval of the Arena deal. This condition has been prolonged because of BPL's debt liabilities—i.e., related party loans—which BPL has been paying off for the last several years. These loans were necessitated by operating deficits—expenses exceeding revenues. The audit-identified questioned expenditures directly added to the deficits. Our recommendations for the County to negotiate credit adjustments to the *Schedules of Management Agreement Computations* would bring the County closer to eliminating the deficit gap sooner and, thus, bring the County nearer to realizing profit sharing.

In closing, we are encouraged that our audit has resulted in the implementation of administrative controls that promote fiscal prudence. The OIG considers this audit closed but unresolved, with regards to the two discussed issues.

Attachments

cc: Edward Marquez, Deputy Mayor, Miami-Dade County
Lester Sola, Director, Internal Services Department
Cathy Jackson, Director, Audit and Management Services
Charles Anderson, Commission Auditor

¹ Sums for executive compensation, bonuses, incentives and commissions are not disclosed based on BPL's assertion that this information is a "trade secret." The OIG, nevertheless, has maintained in the audit that collectively these sums are substantial and warrant the County's attention.



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August 29, 2012

Mr. Christopher Mazzella, Inspector General
Miami-Dade County Office of the Inspector General
19 W. Flagler Street, Suite 220
Miami, FL 33130

RE: Miami-Dade County's Response to OIG Audit Report IG11-34 - Audit of the Agreements Between Miami-Dade County and Basketball Properties, Ltd., et. al. to Operate the American Airlines Arena - May 31, 2012

Mr. Mazzella:

Please allow this correspondence to serve as a follow-up to Miami-Dade County's (County) earlier response to you dated May 15, 2012.

This correspondence is intended to share with you the policies and procedures which the County and Basketball Properties, Ltd. (BPL) have agreed upon, and voluntarily elected to implement with regard to the ongoing operation and management of the American Airlines Arena (Arena).

The County believes that these new policies and procedures will create a clear and precise approach toward securing and analyzing any and all documents, reports, records, and/or statements necessary to not only evaluate if revenues and costs are within budget, but also the overall operations of the Arena. The newly implemented policies and procedures provide the County with a whole new framework for encouraging timely review of records and statements, and creating a strong conduit for communication between the parties, thereby ensuring prompt notice of legal and operational issues and concerns. This comprehensive approach effectively addresses the concerns raised in the Office of the Inspector General's Audit Report, and equally important, produces an effect that will minimize the County's unwarranted risk and exposure with regard to the long-term condition of the Arena.

Mayor Gimenez has assigned the Internal Services Department (ISD) the function of overseeing the management of the agreements. ISD has been in communications with BPL and is enhancing our ongoing working relationship. It is important to maintain a strong partnership with BPL to guarantee that the remaining years of the agreements are beneficial for both parties. Below you will find your recommendations in blue font and our responses in black font:

ATTACHMENT A

OIG Recommendations for Section 1

1. The County should become familiar with the accounting details and reporting methodology underlying BPL's budgets and its Schedules of Management Agreement Computations and how they relate to the definitions for Arena Revenue and Arena Operating Expenses listed in the Management Agreement.

County staff has familiarized it's self with the various financial documents provided by BPL, and has asked for additional information in order to be in a better position to review and approve the operating and capital budgets for the Arena. County staff has met with BPL staff on numerous occasions to understand the Schedules of Management Agreement Computations which allows us ultimately to determine the Arena Distributable Net Cash Flow numbers for a given year's budget.

2. The County should create written procedures that detail a review process to be followed for each financial report provided by BPL. These procedures should include an explanation as to why the report needs to be reviewed, along with the steps necessary to complete the review.

The County is establishing protocols for the review of the Arena's annual operating and capital budget, as well as, the financial documents associated to those budgets. Documentation will be retained to support the results of those reviews.

3. The County should require BPL to submit its annual operating and capital budgets to the designated County Representative via email or hand delivery. BPL should also obtain a receipt of delivery to maintain for its records.

The County has noticed BPL of the individuals who will be receiving the budgets and requested that the budgets be sent to them via e-mail with the originals hand delivered. The County has received the operating and capital budget submission for fiscal year 2012-2013.

4. The County should require BPL to include its leased equipment expenses in its operating/capital budgets.

The County has asked BPL to include a list of its leased equipment as part of the operating and capital budget submission. The operating and capital budget submission for fiscal year 2012-2013 included a list of leased equipment.

5. The County's process to review BPL's annual budgets should encompass formal steps, such as:

- Comparing the current year's proposed budget detail to prior years' approved budget detail to determine whether there are variances and, if necessary, obtain additional data from BPL to determine the cause of and justification for the variances.
- Requesting, as "additional detail", that BPL to submit a pro forma Schedules of Management Agreement Computations with its annual budget submissions using the amounts taken from the submissions to project whether BPL expects to reach the Net Cash Flow level necessary to share profits with the County.

- Visiting BPL to review its financial records and interview BPL about its budget preparation process and proposed budget amounts.

The County's budget review process for the Arena's 2012-2013 operating and capital budget included a comparison of previous year's budgets, Audited Financial Statements, and the Schedules of Management Agreement Computations and other trend analysis. Additional details were requested of BPL in order to fully understand the budget submittal. The County also met with BPL on numerous occasions, both before and after the submission of the operating and capital budget.

6. As providing a written response within the five-business day deadline seems unreasonable, the County should negotiate a longer period. In addition, the County should obtain BPL's agreement on what constitutes the start date, (i.e. budget submission date) for measuring the duration of the County's review period.

The County requested 20 days from BPL in order to allow for a thorough review of the operating and capital budget submission for fiscal year 2012-2013. BPL agreed to the County's request which became effective from the time the budget was received by the County.

7. The County needs to periodically review BPL trial balances, vendor payment reports, and source documentation (such as invoices, receipts, and contracts) to gain an understanding of specific expenses being incurred for Arena operations.

We will address the issue of specific expenses incurred through our contract management oversight responsibilities, recurring meetings with BPL staff, County audits and the independent external auditors financial reports provided by PricewaterhouseCoopers, LLC. This topic will be *discussed further at the quarterly meetings held between the County and BPL.*

8. The County should request that BPL provide interim period (unaudited) financial statements showing its actual revenues and costs through a stated date (e.g., through the first 3 quarters of the fiscal year) and the projected revenues and costs for the remainder of the year, along with the coming year's budgets.

BPL's response to the OIG states that this request is not practical given their business model. Regardless, the County will work with BPL to be able to understand the current year's revenues and expenses and be in a better position to review the upcoming year's operating and capital budget submission.

OIG Recommendations for Section 2

9. BPL should take whatever steps are necessary to produce its Annual Operating Budget and submit it to the County within the timeframe required by the Management Agreement.

BPL has requested an alternate submission date than what is called for in the Maritime Park Arena Management Agreement (Management Agreement). The County is reviewing this request and will come to an agreement with BPL for the submission of the operating and capital budget for fiscal year 20-13-2014 which will be inclusive of equipment leases. The County's goal is to receive from BPL the most accurate budget possible and to have adequate time to conduct a thorough review.

10. The County should ensure that prospectively, it receives from BPL its Annual Capital Budget, inclusive of equipment leases, within the timeframe required by the Management Agreement.

Please see response to OIG Recommendations for Section 2 - Recommendation # 9 above.

11. The County should seek to claim these amounts (Capital Expenses) from BPL, via an adjustment to a future Schedules of Management Agreement Computations, BPL capital expenditures in excess of its capital budget, totaling \$3.3 million over fiscal years 2005-2010.

The Management Agreement requires County approval of the annual capital budgets and the OIG recommends that the County require BPL to adjust for the amounts that exceeded the budgets from future Schedules of Management Agreement Computations reports. In order to do so, the County must follow the terms of the Management Agreement with respect to Section 5.11 "Records and Audits". This process includes a presumption of reasonableness, as described in Section 5.11.3.3, for expenses that meet certain standards inclusive of those expenses that exceed the annual capital budget. The County has reviewed the expenses, and the detailed back-up associated for a number of these during this period and determined that the expenses are reasonable because they are customary in accordance with industry standards in connection with maintaining, managing and operating the Arena in a first class manner. Accordingly, we have decided that these expenses will not be submitted to mediation/arbitration. For the 2012-2013 operating and capital budget, BPL is funding the Arena Capital Replacement Reserve Payment as required in Section 5.1.3 of the Management Agreement.

12. The County should review BPL's fiscal year 2011 results to determine if BPL's actual capital expenditures exceeded its capital budget and, if a similar over expenditure is found to have occurred, the County should seek recoupment.

Please see response to OIG Recommendations for Section 2 - Recommendation # 11 above.

13. The County and BPL should agree to a protocol that would ensure that the County receives timely notice of BPL capital expenditures in excess of its approved capital budget amount.

The County will work with BPL to establish protocols to ensure timely notice of BPL capital expenditures in excess of its approved capital budget amount. This topic will be discussed during our quarterly meetings.

14. The County should request from BPL that it provide a personal property and equipment inventory listing as of the end of the most recent fiscal year, and require that every year hereafter that BPL automatically provide such a listing to the County, as part of its required fiscal year end reporting.

The County has received an equipment inventory list from BPL as part of the 2012-2013 operating and capital budget submission and will request that the list be updated yearly and submitted as part of the budget process.

15. The County should request that BPL provide a separate budget for its annual leases of systems, equipment, and furnishings, as part of its required budget submission process or include it in either its annual operating or capital budgets.

Please see response to OIG Recommendations for Section 1 - Recommendation # 4 above.

16. The County should require BPL to disclose the main terms of all of its equipment lease, including the relationship of the lessor to BPL and its affiliated parties.

The County asked BPL to include a list of its leased systems, equipment and furnishings as part of their 2012-2013 operating and capital budget submittal. The County confirmed with BPL that a relationship does not exist between the Heat Group, or any of its affiliates, and the entities providing the leased equipment.

17. The County and BPL should meet to discuss how they will go about implementing the consulting engineer option and to formally agree, in future years, that they will periodically call upon an independent engineer to inspect the Arena and site.

The County has discussed this matter with BPL and we will work to identify a third party engineer to periodically provide an independent assessment of the physical condition of the Arena.

18. The County should meet with BPL to develop procedures detailing how BPL will provide the County with written notice of future legal actions. In addition, BPL should disclose to the County how it handles legal actions, including whether it uses in-house or outside counsel and how it selects outside counsel. The County and BPL should establish regularly scheduled meetings as one means of ensuring that the County is properly noticed of new and ongoing BPL legal actions related to Arena operations.

Staff from ISD and CAO have are in the process of finalizing a process for formal notification of legal issues related to the Arena. This topic will also be discussed at our quarterly meetings.

OIG Recommendations for Section 3

19. The County should be more informed about the Arena Revenue that is included in the Schedules of Management Agreement Computations used to derive the "Arena Distributable Net Cash Flow" upon which the County's share of Arena profits is calculated. Steps that the County should consider include:

- Perform variance analyses between current year's actual revenues with prior year's actual revenues, and written requests to BPL asking for explanations and supporting detail, as necessary.

The County has compared actual revenues numbers for the latest year available with actual revenues from a number of prior years. The County has also met with BPL on numerous occasions to discuss this topic.

- Develop an understanding of BPL revenue details, such as: main contract terms of the sales agreements; Premium Inventory sold versus unsold; pricing comparisons for the sold inventory and remaining contract periods for this inventory; and competition with other local venues for booking events.

The budgetary review process and the establishment of recurring meetings with BPL will assist the County in developing a deeper understanding of revenue details.

- Request that a County representative attend the annual committee meetings held by BPL and the Miami Heat personnel to set pricing, budgeting, and contract terms pertaining to the Arena. Implement reviews of BPL's actual contracts for sales of Premium Inventory.

In BPL's draft response to the OIG they stated that this recommendation falls outside of the County's purview as outlined in the Management Agreement. Regardless, the County will take the opportunity to will meet with BPL throughout the year in order to discuss these topics.

- Periodic audits of event basis sales that would include a review of the sales terms and conditions of this Premium Inventory.

The County will perform periodic audits of event basis sales that will include a review of the sales terms and conditions of Premium Inventory.

- Meet with BPL regarding its handling of complimentary tickets and to ascertain the financial impact of dispensing these tickets, i.e., impact on Use Fee.

The County has had an initial meeting with BPL on the issue of complimentary tickets and its impact on Use Fees. Additional meetings to address this topic have been scheduled.

OIG Recommendations for Section 4

20. The County and BPL should meet to discuss the methodologies utilized to allocate costs between BPL and the Miami Heat, so that the County can approve the allocation percentages directly attributing to the Arena's annual operating costs as part of the budget process. Once allocation percentages have been established and approved, periodically, as part of future audits or other in-depth reviews, the County should examine BPL's accounting records to ensure that the cost allocations are still reasonable and based on actual costs.

The County and BPL have met and reviewed cost allocation methodologies proposed for the 2012-2013 operating and capital budget. The County and BPL have agreed that a number of these calculations will be revisited at the end of the fiscal year and adjusted accordingly on the actual expenses incurred.

21. The County needs to periodically review BPL trial balances; vendor payment reports; and source documentation (such as invoices, receipts, and contracts) to gain an understanding of specific operating and capital expenses being incurred for Arena operations.

Please see response to OIG Recommendations for Section 1 - Recommendation # 7 above.

22. For legal fees relating to the architect lawsuit, the County and BPL should determine whether or not expended funds should be reclassified, i.e., reclassified into something other than Arena operating expense, and how potential future recoveries will be classified.

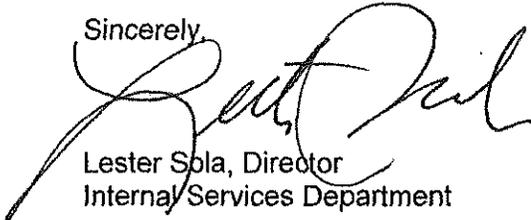
The County has confirmed with BPL that future recoveries related to the architect lawsuit will impact the Arena Distributable Net Cash Flow listed in the Schedules of Management Agreement Computations.

23. The County should seek to review the OIG's work papers (both in the OIG's possession and at BPL's offices) regarding the questioned expense amounts identified by the OIG. The County should seek to claim these amounts (executive compensation, lobbyist fees, and political and charitable contributions) via an adjustment to a future Schedules of Management Agreement Computations.

The County visited the OIG, both at the Arena and at their offices, to review their work papers related to this audit. The County is analyzing these documents and will act accordingly with respect to any adjustments that may be requested of BPL and applied to future Schedules of Management Agreement Computations once this review has been completed.

Your careful review of the following document is appreciated and I thank you for the opportunity to review your report and provide a response. Should you have any questions, please feel free to contact me.

Sincerely,

A handwritten signature in black ink, appearing to read "Lester Sola", written over the word "Sincerely,".

Lester Sola, Director
Internal Services Department

c: R. A. Cuevas, Jr., County Attorney
Gerri Bonzon- Keenan, Assistant County Attorney
Edward Marquez, Deputy Mayor
Leland Salomon, Acting Assistant Director, ISD
Jose A. Galan, Acting Director, ISD, REDD



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October 26, 2012

Mr. Christopher Mazzella, Inspector General
Miami-Dade County Office of the Inspector General
19 W. Flagler Street, Suite 220
Miami, FL 33130

RE: Miami-Dade County's Response to OIG Item #23 Letter - OIG Audit Report IG11-34
Audit of the Agreements Between Miami-Dade County and Basketball Properties, Ltd., et.
al. to Operate the American Airlines Arena

Mr. Mazzella:

I am in receipt of your letter dated September 27, 2012 regarding the County's position on issues found in item #23 of our response to the OIG's final report.

We have met with Basketball Properties Limited (BPL) representatives on several occasions to discuss a number of issues including those outlined in your letter. The County has reviewed the expenses associated with lobbyist's fees, political contributions, charitable contributions and memberships/dues and have concluded that they are legitimate business expenses allowed under the current agreement. Therefore, we will not be challenging these past charges.

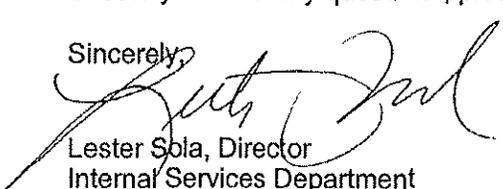
For the Arena's 2012-2013 fiscal year, the County has approved operating expenses for lobbyist fees (\$294,000) and requested appropriate back-up to justify actual expenses, charitable contributions (\$5,000) and memberships/dues (\$27,684). We feel these expenses are reasonable and customary for an operation such as the Arena.

Additionally, we discussed the role of the Vice-President that serves as the events coordinator for the Arena. This individual was hired shortly after the Arena opened in order to be competitive with the other venues in the area, namely the Bank Atlantic Center which opened prior to our Arena. His primary role is to attract top tier entertainment for the Arena and the title to Vice-President serves to bolster his credibility when trying to accomplish this mission. After reviewing the job duties of this individual, we feel this role serves to enhance the functions of the Arena and again contributes to maximizing Arena Net Cash Flow.

Finally, we met with the County Attorneys' Office to discuss the issue of bonuses, incentive payments and commissions as they relate to the agreements. Based on these discussions and our review, we will not be pursuing this matter at this time.

Should you have any questions, please contact me at 305-375-2363.

Sincerely,


Lester Sola, Director
Internal Services Department

c: R. A. Cuevas, Jr., County Attorney
Gerri Bonzon- Keenan, Assistant County Attorney
Edward Marquez, Deputy Mayor
Leland Salomon, Assistant Director, ISD
Jose A. Galan, Acting Director, ISD, REDD

ATTACHMENT B