

Metropolitan Nashville Airport Authority

MEMORANDUM

TO: Raul Regalado, President and CEO

CC: Monty Burgess, Senior Vice President and COO
Stan Van Ostran, Vice President and CFO
John Howard, Asst. Vice President of Properties and Business Development
Amber Gooding, Director of Business Diversity Development
Tom Bibb, Director of Properties
Rebecca Ramsey, Manager of Properties

FROM: Julie Zwicknagel, Internal Auditor

DATE: December 29, 2009

SUBJ: Delaware North Companies Travel Hospitality Services, Inc. Audit Report

Background

On June 27, 1986, CA One Services, Inc (“CA One”) entered into the original Concession Agreement with the Metropolitan Nashville Airport Authority (“Authority”). The Agreement granted CA One the exclusive right, privilege, and obligation to operate all food and beverage services within the Nashville International Airport. The term of the Agreement was for a period of fifteen (15) years.

On January 1, 2005, the Agreement was amended to extend the term of CA One’s Concession Agreement on a month-to-month basis, due to the Terminal Renovation.

On September 13, 2005, CA One changed its name to Delaware North Companies Travel Hospitality Services, Inc. (“DNC”). The modification was a change of name only, and the ownership, management and former employees of the former CA One remained unchanged.

After completion of a formal request for proposal process, DNC entered into a Master Lease and Concession Agreement with the Authority for the operation of Package 1 of the Food and Beverage Concession at the Nashville International Airport, effective October 17, 2006. The term of the Agreement commenced on January 31, 2009, the beginning of the Operational Phase and would continue for eight (8) full lease years (6/30/2017) with two one-year renewal options. The Authority would have the right to exercise the renewal options by providing the Concessionaire with notice of the Authority’s election to renew and extend the Operational Phase not less than one hundred eighty (180) days prior to the expiration of the Agreement.

Concession Package No. 1 consists of the following restaurants, categories of operations, concession locations, and square footage:

Restaurant	Category of Operation	Concession Location	Location within Terminal	Square Footage
Manchu Wok, Villa Pizza & Wendy's	Fast Food	AB-1	Concourse A/B Apex	2,247 sq. ft.
La Hacienda	Locally Themed Cafe/Lounge	A-2	Concourse A	1,620 sq. ft.
Swett's/Whitt's/Tootsie's	Locally Themed Cafe/Lounge	C-3	Concourse C	3,819 sq. ft.
O'Charley's	Casual Dining Restaurant and Lounge	C-7	Concourse C	4,567 sq. ft.
Tootsie's	Locally Themed Cafe/Lounge	PS-1	Pre Security	641 sq. ft.
Total Square Footage of Concession Package No. 1				12,894 sq. ft.

DNC agreed to pay to the Authority the greater of a minimum annual guarantee (“MAG”) of One Million One Hundred Seventy Five Thousand and No/100 Dollars (\$1,175,000) or an amount equal to the applicable percentage of gross receipts from Concession Operations from each concession location. The applicable percentages of gross receipts are as follows:

1. Twelve percent (12%) of Gross Receipts derived from the sale of Food & Non-Alcoholic Beverages at Fast Food shops and Locally Themed Café/Lounges;
2. Fifteen percent (15%) of Gross Receipts derived from the sale of Alcoholic Beverages at Fast Food and Locally Themed Café/Lounges;
3. Ten percent (10%) of Gross Receipts derived from the sale of Food & Non-Alcoholic Beverages at the Casual Dining Restaurant and Lounge;
4. Fifteen percent (15%) of Gross Receipts derived from the sale of Alcoholic Beverages at the Casual Dining Restaurant and Lounge; and
5. Fifteen percent (15%) of Gross Receipts derived from the sale of Related Merchandise at all locations.

Within sixty (60) days after the end of each Lease Year, Concessionaire would provide to the Authority an annual report along with a reconciliation and payment to Authority (if any is due) as follows: (A) a comparison of the MAG for such preceding Lease Year and the percentage of Gross Receipts due to Authority for such Lease Year to determine the total amount owed to Authority by Concessionaire for such preceding Lease Year; and (B) payment of any additional amount owed as Rent for such preceding Lease Year under the terms of the Agreement. In the event that such Annual Report reflects an overpayment by Concessionaire of Periodic Rent for such preceding Lease Year, Concessionaire would receive a credit by Authority for the overpayment with respect to subsequent Periodic Rent due to Authority or a refund, as Authority may determine. However, in no event would the Concessionaire take a credit against any subsequent Periodic Rent owed to Authority for any such overpayment without the prior written approval of Authority.

The Agreement stated that DNC would prepare monthly, quarterly and annual reports of Gross Receipts derived from the Concession Program and separately listing Gross Receipts by Concession Operator, Concession Location and type of Concession Operations. Annually, within ninety (90) days after the end of each Lease Year, Concessionaire would furnish

Authority with audited statements of Gross Receipts derived from the Concession Program certified to by an independent public accounting firm.

DNC agreed to contribute to the Joint Marketing Fund, on a monthly basis, an amount not to exceed three quarters of one percent (0.75%) of all gross receipts derived from Concession Operations within the Premises, effective January 31, 2009. The types of expenses that Authority may pay out of the Joint Marketing Fund include the following:

1. Direct costs associated with marketing and promotional activities (including, without limitation, costs incurred for the purchase of marketing program creative material, costs for special events and/or paid media);
2. Costs associated with marketing program development and the day-to-day coordination of the marketing program;
3. Costs for development and provision of shopping bags to promote Concession Operations;
4. Secret shopping and other inspection programs with respect to Concession Operations;
5. Directory signage within the Terminal relating to the Concession Locations;
6. The preparation of a full-color catalog featuring the Concession Operations, the Concession Locations and the products and services offered by Concession Operators, which may include coupons, and
7. Other programs, such as brochures, common shopping bags, graphics, media promotions, pamphlets and public events, to promote sales through the Concession Program.

Additionally, DNC would pay to the Authority, on a monthly basis, Common Area Maintenance (“CAM”) Charges in an amount equal to one and twenty-five one-hundredths (1.25%) of the gross receipts from Concession Operations. The CAM charges assessed would be used to reimburse the Authority for expenses incurred to provide general maintenance and upkeep of the Common Areas including cleaning, repair, refurbishment, equipping, furnishing, and replacement of furnishings.

The Disadvantaged Business Enterprise (“DBE”) participation goal for the Agreement was established at fifteen and seven tenths percent (15.7%) or more of total gross receipts from Concession Operations that are attributable to the participation of Authority-certified DBEs in the Concession Program. DNC achieves DBE participation through a sublease agreement with Bridgeman Foods (“Wendy’s”), their DBE partner.

The following are the gross revenues for DNC per the Schedule of Gross Revenues for the Year Ended December 31, 2008, provided by Tronconi Segarra & Associates LLP and Darryl McCormick, PSC (Wendy’s):

2008	Alcoholic Beverages	Alcoholic Beverages	Food & Vending	Wendy's Food & Vending	All Other Retail	O'Charleys Food & Beverage	O'Charleys Alcoholic Beverages	Total
January	\$89,693	\$35,689	\$425,392	\$0	\$125	\$219,714	\$80,668	\$851,281
February	50,472	97,943	396,239	-	694	215,700	68,223	\$829,271
March	33,924	104,044	452,396	40,681	974	223,312	66,599	\$921,930
April	27	123,143	391,258	85,362	1,123	209,743	71,938	\$882,594
May	-	126,285	416,591	92,777	1,048	207,285	71,394	\$915,380
June	-	127,585	411,752	101,517	2,714	214,480	70,120	\$928,168
July	-	113,551	408,766	107,239	2,039	195,300	61,043	\$887,938
August	-	120,158	369,054	97,899	929	171,550	53,790	\$813,380
September	-	114,932	318,527	88,887	1,662	155,378	53,990	\$733,376
October	-	121,764	326,881	100,980	1,279	193,400	61,832	\$806,136
November	-	124,546	327,365	90,889	724	158,440	50,196	\$752,160
December	-	124,678	336,057	97,539	898	162,946	54,596	\$776,714
Total Gross Revenue	\$174,116	\$1,334,318	\$4,580,278	\$903,771	\$14,209	\$2,327,248	\$764,389	\$10,098,329

On January 1, 2008, DNC entered into a Space Lease Agreement with the Authority. The Agreement provided for DNC to lease from the Authority the following 3,947 square feet of support space:

1. First floor level of the Passenger Terminal Building - 1,319 sq ft;
2. Ramp storage space in the "C" Triangle storage area - 1,668 sq ft; and
3. A/B Apex storage area – 960 sq ft.

DNC agreed to pay the Authority annual rental of One Hundred Forty Two Thousand and Ninety Two and 00/100 Dollars (\$142,092), payable in equal monthly installments, based upon \$36 per square foot per annum. The Agreement would automatically renew on a month-to-month basis unless otherwise terminated by either party by giving a thirty (30) day advance written notice.

The First Amendment to the Space Lease Agreement, effective April 1, 2009, provided for: (i) the addition of support space, room T0032 (4,222 sq ft) located on Level I of the main terminal space and S1175 (278 sq ft) located in the "C" Triangle Storage area of the main terminal and (ii) deletion of support space rooms S1175 (1,390 sq ft), N1056E1 (183 sq ft), N1056E3 (103 sq ft), T0035A (125 sq ft), and T0035 (262 sq ft). Delaware North agreed to pay the Authority annual rental of Forty Five Thousand and 00/100 Dollars (\$45,000), payable in equal monthly installments, based upon \$10 per square foot per annum.

Objectives

The objectives of the audit were as follows:

1. Determine the validity of gross revenue amounts reported and fees paid to the Authority;
2. Determine compliance with contract terms and operational requirements; and
3. Document and evaluate existing internal controls.

Testing

In order to satisfy the audit objectives, the following tests were performed:

1. Selected 3 months for detailed testing (January, March, and June 2008). For each month selected, performed the following:
 - a. Obtained the monthly fixed rent invoices from Authority's Accounts Receivable and verified that the invoiced amount agreed to the schedule of rental fees and charges in the Master Lease and Concession Agreements.
 - b. Obtained monthly revenue report and performed the following:
 - i. Reviewed report for mathematical accuracy.
 - ii. Tied amounts per report to amounts reported to the Authority.
 - iii. Verified DNC had not properly calculated the percentage of gross revenue requirements.
 - iv. Verified monthly CAM charges were not equal to 1.25% of the gross receipts from concession operations.
 - c. Obtained a copy of the Tennessee Sales and Use Tax and Alcoholic Beverage and Beer Tax forms.
 - i. Tied revenue amounts per sales tax and alcoholic beverage tax forms to revenue amounts reported to the Authority.
2. Selected 3 months for detailed testing (January, March, and April 2009) of a specific concession location (O'Charleys). For each month selected, performed the following:
 - a. Obtained a copy of general ledger and performed the following:
 - i. Reviewed report for mathematical accuracy.
 - ii. Verified that the revenue amounts reported per the general ledger were consistent with the revenue amounts reported to the Authority.
 - iii. Verified O'Charleys had properly calculated the percentage of gross revenue requirements.
 - iv. Sub selected a week each month and performed the following:
 1. Obtained the Daily Revenue Report for the week selected.
 2. Verified the daily revenue amount agreed to the monthly general ledger report.
 3. Determined that the revenue was properly stated by noting sales receipts per the Daily Revenue Reports contained appropriate information (e.g., sales date, total, method of payment, etc.)
 4. Reviewed the Daily Revenue Reports for any unusual activity.

3. Selected 3 months for detailed testing (March, April, and May 2009). For each month selected, performed the following:
 - a. Obtained monthly revenue report and performed the following:
 - i. Determined DNC was contributing 0.75% of monthly gross receipts to the Joint Marketing Fund as of the Commencement Date of January 31, 2009.
 - ii. Verified the Authority was not maintaining the Joint Marketing Fund in a separate account and commingling with other Authority funds.
4. Determined DNC has not reimbursed the Authority for one-half of the cost of the furniture and fixtures used to equip the common seating area.
5. Determined DNC had not met the initial capital improvement costs but submitted certified receipts and lien release for the capital improvements to the Authority.
6. Determined DNC was meeting operational requirements.
 - a. Determined through observations that the Concessionaire's premises was maintained in a First Class Manner.
 - b. Verified Concessionaire was meeting operational hours and staffing requirements.
 - c. Determined Concessionaire's employees were trained to respond to airport customer's request for information.
 - d. Determined Concessionaire was not submitting a quarterly update regarding recent trends or developments in food and beverage concession operations.
 - e. Verified Concessionaire was conducting formal performance audits on a bi-monthly basis.
 - f. Determined DNC was not meeting annual reporting requirements.
 - g. Determined Concessionaire was submitting pricing reports to ensure reasonable pricing was being maintained.
7. Verified Authority personnel were not conducting monthly meetings with Concessionaire to discuss operational issues.
8. Verified Concessionaire has not met the Disadvantaged Business Enterprise ("DBE") Program requirements established in the contract.
9. Determined DNC maintained adequate insurance coverage.
 - a. Obtained a copy of the current certificate of insurance on file.
 - b. Verified that the commercial general liability, property, automobile, and worker's compensation insurance coverage met or exceeded the amounts specified in the contract.
 - c. Verified that the certificate of insurance was current and adhered to all other contract terms.
10. Determined DNC maintained an Irrevocable Letter of Credit ("LOC").
 - a. Obtained a copy of the current LOC.
 - b. Verified that the LOC coverage met or exceeded the amount specified in the contract.
 - c. Verified that the LOC was current and adhered to all other contract terms.
11. Determined Concessionaire's Sublease tenant was meeting contract requirements.
12. Through inquiry and observations, reviewed the existing internal controls in place.

Conclusion

Based upon the audit, the following was determined with respect to the stated objectives:

1. DNC has not been submitting fifteen percent (15%) of gross receipts derived from the sale of related merchandise, as noted in finding #1.
2. DNC has not been submitting to the Authority the gross receipts derived from the sales of catering services, as noted in finding #2.
3. The Authority is not complying with Joint Marketing Fund requirements, as noted in finding #3.
4. DNC has not been invoiced for the cost of the furniture and fixtures used to equip the food and beverage common seating areas, as noted in finding #4.
5. DNC did not meet their capital improvements requirements for the O'Charley's concession location, as noted in finding #5.
6. DNC is not submitting to the Authority a quarterly update regarding recent trends or developments in Airport food and beverage concession operations, as noted in finding #6.
7. DNC was not in compliance with FY 2008 annual reporting requirements, as noted in finding #7.
8. Properties is not conducting monthly meetings with DNC to discuss operational issues, as noted in finding #8.
9. DNC is not achieving the DBE participation goal of 15.7% established in the Master Lease and Concession Agreement, as noted in finding #9.
10. DNC's monthly gross revenue reports submitted to the Authority are not disclosing the required DBE participation information, as noted in finding #10.
11. BDD has not processed Wendy's DBE certification information in a timely manner, as noted in finding #11.

Finding #1

Observation

DNC has not been submitting fifteen percent (15%) of gross receipts derived from the sale of related merchandise.

Background

According to Section 5.1(a. & b.), Periodic Rent, of the Master Lease and Concession Agreement, “During each Lease Year of the Interim Phase and Operational Phase, Concessionaire shall pay Periodic Rent in an amount equal to the greater of (i) the MAG due for such Lease Year as set forth herein or (ii) the applicable percentages of Gross Receipts from Concession Operations for such Lease Year as set forth below:

- i. Twelve percent (12%) of Gross Receipts derived from the sale of Food & Non-Alcoholic Beverages at Fast Food shops and Locally Themed Café/Lounges;
- ii. Fifteen percent (15%) of Gross Receipts derived from the sale of Alcoholic Beverages at Fast Food and Locally Themed Café/Lounges;
- iii. Ten percent (10%) of Gross Receipts derived from the sale of Food & Non-Alcoholic Beverages at the Casual Dining Restaurant and Lounge;
- iv. Fifteen percent (15%) of Gross Receipts derived from the sale of Alcoholic Beverages at the Casual Dining Restaurant and Lounge; and
- v. Fifteen percent (15%) of Gross Receipts derived from the sale of Related Merchandise at all locations.”

An objective of the audit was to verify DNC had properly calculated the percentage of gross revenue requirements. Through audit testing, it was determined that DNC has been submitting twelve percent (12%) of gross receipts derived from the sale of related merchandise instead of the contract requirement of fifteen percent (15%). Therefore, DNC owes the Authority for underpayment of rent for related merchandise for 2008, as detailed below:

2008	All Other Retail - 12%	All Other Retail - 15%	Variance
January	\$125	\$125	
February	694	694	
March	974	974	
April	1,123	1,123	
May	1,048	1,048	
June	2,714	2,714	
July	2,039	2,039	
August	929	929	
September	1,662	1,662	
October	1,279	1,279	
November	724	724	
December	898	898	
Total Gross Revenue	\$14,209	\$14,209	
Contractual Percentage Rate	12%	15%	
Calculated Percentage Rent	\$1,705	\$2,131	(\$426)

Recommendation

Properties should require DNC to comply with the Master Lease and Concession Agreement by submitting to the Authority fifteen percent (15%) of gross receipts derived from the sale of related merchandise.

Additionally, Properties should request the Finance Department to invoice DNC for the underpayment of rent for related merchandise in the amount of \$426.

Management Response

Properties will notify DNC to comply with the Master Lease and Concession Agreement by submitting to the Authority fifteen percent (15%) of gross receipts derived from the sale of related merchandise and request that the Finance Department invoice DNC for \$426 representing the underpayment of rent for related merchandise sales.

Finding #2

Observation

DNC has not been submitting to the Authority the gross receipts derived from the sales of catering services.

Background

According to Section 1.1, Definitions, of the Master Lease and Concession Agreement, “Gross receipts means all monies paid or payable, whether in cash, credit or otherwise, for sales made or services rendered at or from a Concession Location regardless of when or where the order therefore is received, or outside such Concession Location if the order is received at the Airport, including, without limitation:

h. Sales of Catering Services.”

An objective of the audit was to determine the validity of gross revenue amounts reported to the Authority. Through audit testing, Internal Audit determined that the sales from catering services were not being included in the gross receipts submitted to the Authority.

Catering sales revenues were included in the gross receipts definition under the previous Concession Agreement and the current Master Lease and Concession Agreement. Both Agreements did not specifically state the percentage payment provisions for catering sales. Therefore, Internal Audit consulted with the Properties Department and based the catering sales percentage requirements on the percentage provisions under the previous Concession Agreement and by concession location for the current Agreement.

Accordingly, DNC owes the Authority for underpayment of rent for catering sales for 2008, as detailed below:

2008	Catering Sales -		Amount Due to Authority
	Old Concession Contract	Catering Sales - O'Charley's	
January	\$783	\$0	
February	316	0	
March	1,183	0	
April	197	0	
May	503	2,145	
June	-	3,069	
July	-	158	
August	-	1,291	
September	-	2,297	
October	-	782	
November	-	527	
December	-	178	
Total Gross Revenue	<u>\$2,981</u>	<u>\$10,447</u>	
Contractual Percentage Rate	12%	10%	
Calculated Percentage Rent	<u>\$358</u>	<u>\$1,045</u>	<u>\$1,402</u>

Recommendation

Properties should require DNC to comply with the Master Lease and Concession Agreement by submitting to the Authority the gross receipts derived from the sales of catering services, based upon concession location percentage requirements.

Additionally, Properties should request the Finance Department to invoice DNC for the underpayment of rent from the sales of catering services in the amount of \$1,402.

Management Response

Properties will notify DNC to comply with the Master Lease and Concession Agreement by submitting to the Authority the gross receipts derived from the sales of catering services, based upon concession location percentage requirements and request the Finance Department to invoice DNC for \$1,402 representing the underpayment of rent from the sales of catering services.

Finding #3

Observation

The Authority is not complying with Joint Marketing Fund requirements.

Background

According to Section 4.8, Marketing and Promotions, of the Master Lease and Concession Agreement, "Authority shall maintain the Joint Marketing Fund in a separate account to be established for this purpose, and the Joint Marketing Fund shall not be commingled with any other funds of Authority."

An objective of the audit was to verify the Authority was maintaining the Joint Marketing Fund in a separate account and not commingled with any other funds. Through audit testing, Internal Audit determined that the Authority was maintaining the Joint Marketing Fund in a separate liability account (261005-00-00). However, the Joint Marketing Funds were being commingled with other Authority funds.

It was determined from the Authority's Properties Department that the requirement to retain the Joint Marketing Fund in a separate account and not commingled with other Authority fund was because the Authority would be serving in a fiduciary capacity in the use of the Joint Marketing Funds to meet marketing and promotional activity needs.

The account balance of the Joint Marketing Fund as of November 30, 2009, was \$327,713 with no joint marketing expenditures recorded to date.

Recommendation

The Finance Department should be complying with the Master Lease and Concession Agreement by ensuring the Joint Marketing Funds are not being commingled with any other funds of the Authority.

Management Response

Finance is requesting that Properties and the Authority's Legal Department coordinate with the Chief Financial Officer and Assistant Treasurer before entering into any contract that requires a new fund or bank account. The contract(s) which call for creation of the Joint Marketing Fund were not vetted with Finance staff, nor was Finance provided a copy of the contract. Finance staff believes the requirement to have a separate account that is not comingled requires additional administrative resources and costs that are not necessary and provide little or no increase of internal controls. Nevertheless, Finance will adhere to the contract terms by opening a new bank account for the Joint Marketing Fund and deposit funds currently identified in account number 261005-00-00 within the next 30 days.

Finding #4

Observation

DNC has not been invoiced for the cost of the furniture and fixtures used to equip the food and beverage common seating areas.

Background

According to Section 5.5, Reimbursement for Food and Beverage Common Seating Areas, of the Master Lease and Concession Agreement, "Within thirty (30) days after receipt of an invoice from Authority therefore, Concessionaire shall reimburse Authority for one-half of the cost of the furniture and fixtures used to equip and furnish the Food and Beverage Common Seating Areas; provided, however, that such reimbursement shall not exceed One Hundred Thousand and No/100 Dollars (\$100,000)."

An objective of the audit was to determine DNC reimbursed the Authority for one-half of the cost of the furniture and fixtures used to equip the common seating area. Through audit testing, it was determined that DNC has not been invoiced for the cost of the furniture and fixtures used to equip the food and beverage common seating area.

With the assistance of the Authority's Director of Construction, Bell & Associates Construction contractors were able to provide Internal Audit with the following furniture and fixtures cost for the Common Seating Areas:

Furniture Type	Cost
Banquette Seating	\$30,375
Chair 1 (café)	\$86,127
Table 1 (24" x 30" vinyl edge)	\$25,725
Table 2 (36" diameter vinyl edge)	\$5,989
Table 3 (24" x 30" wood edge)	\$20,973
Table 4 (30" diameter wood edge)	\$6,268
Total Furniture and Fixture Costs	\$175,458
DNC applicable percentage (one-half)	50%
DNC applicable Cost	\$87,729

Accordingly, DNC owes the Authority \$87,729 for one-half of the cost of food and beverage common seating area furniture and fixtures.

Recommendation

Properties should request the Finance Department to invoice DNC in the amount of \$87,729 for the cost of food and beverage common seating area furniture and fixtures.

Management Response

Properties will request the Finance Department to invoice DNC in the amount of \$87,729 for one-half of the cost of the furniture and fixtures used to equip and furnish the food and beverage common seating areas.

Finding #5

Observation

DNC did not meet their capital improvements requirements for the O’Charley’s concession location.

Background

According to Section 10.2, Initial Capital Improvements, of the Master Lease and Concession Agreement, “The Initial Capital Improvements to be constructed, equipped and installed in each Concession Location shall require an expenditure by Concessionaire and/or the applicable Concession Operator of not less than Four Hundred Twenty One Dollars (\$421) in Eligible Costs per square foot of such Concession Locations.

DNC's concession locations as specified in the Master Lease and Concession Agreement are identified below:

Restaurant	Category of Operation	Concession Location	Location within Terminal	Square Footage
Manchu Wok, Villa Pizza & Wendy's	Fast Food	AB-1	Concourse A/B Apex	2,247 sq. ft.
La Hacienda	Locally Themed Cafe/Lounge	A-2	Concourse A	1,620 sq. ft.
Swett's/Whitt's/Tootsie's	Locally Themed Cafe/Lounge	C-3	Concourse C	3,819 sq. ft.
O'Charley's	Casual Dining Restaurant and Lounge	C-7	Concourse C	4,567 sq. ft.
Tootsie's	Locally Themed Cafe/Lounge	PS-1	Pre Security	641 sq. ft.
Total Square Footage of Concession Package No. 1				12,894 sq. ft.

DNC provided the Authority with certified receipts and lien release for the capital improvements expenditures by concession location, which are detailed below:

Concession Location	Concession Location	Concession		Required Expenditure	Actual Expenditure	Amount Over/(Under) Required	Actual Expenditure / sq ft	Amount /sq ft Over/(Under) required
		Required Amount/sq ft	Location sq ft					
AB-1	Manchu Wok	\$421	666	\$280,386	\$478,903	\$198,517	\$719.07	\$298.07
AB-1	Villa Pizza	421	797	335,537	494,120	158,583	619.98	198.98
AB-1	Wendy's	421	784	330,064	361,395	31,331	460.96	39.96
	Total	\$421	2,247	\$945,987	\$1,334,419	\$388,432	\$593.87	\$172.87
A-2	La Hacienda	421	1,620	682,020	888,002	205,982	548.15	127.15
C-3	Swett's/Whitt's/Tootsie's	421	3,819	1,607,799	1,660,302	52,503	434.75	13.75
PS-1	Tootsie's PS1	421	641	269,861	412,590	142,729	643.67	222.67
C-7	O'Charley's	421	4,567	1,922,707	1,440,067	(482,640)	315.32	(105.68)
Total Capital Improvements		\$421	12,894	\$5,428,374	\$5,735,380	\$307,006	\$444.81	\$23.81

As noted above, DNC met their initial capital investment requirements in total; however, the Agreement required DNC to expend \$421 per sq ft for each concession location and the O'Charley's concession location did not meet their capital requirements.

According to Section 10.4, Certification of Construction Expenditure, of the Master Lease and Concession Agreement, "Concessionaire shall provide Authority with certified receipts and lien releases for the Initial Capital Improvements and Midterm Renovations to a Concession Location required hereunder within ninety (90) days after the completion thereof in detail acceptable to Authority to enable Authority to verify compliance with the requirements of this Agreement. In the event that such certified receipts indicate that Eligible Costs incurred with respect to the Initial Capital Improvements or Midterm Renovations required hereunder are less than required under the terms and provisions of this Agreement, Concessionaire shall pay to Authority one hundred ten percent (110%) of the difference between the amount required to be spent and the Eligible Costs actually incurred by Concessionaire and/or Concession Operator as indicated by such certified receipts.

Accordingly, DNC owes the Authority \$530,904 which is 110% of the difference between the amounts required to be spent for the O’Charley’s concession location and the eligible costs actually incurred by DNC, as calculated below:

<u>Location</u>	<u>Required Amount/sq ft</u>	<u>Concession Location sq ft</u>	<u>Required Expenditure</u>	<u>Actual Expenditure</u>	<u>Amount Over/(Under) Required</u>	<u>Actual Expenditure /sq ft</u>	<u>Amount /sq ft Over/(Under) required</u>	<u>Amount due to Authority (110%)</u>
O’Charley’s	\$421	4,567	\$1,922,707	\$1,440,067	(\$482,640)	\$315.32	(\$105.68)	(\$530,904)

Recommendation

Properties should request the Finance Department to invoice DNC for not meeting their capital improvements obligations for the O’Charley’s concession location in the amount of \$530,904.

Management Response

Properties staff has recommended that, because DNC exceeded the overall proposed capital expenditures, the funds identified in this finding be spent as additional capital expenditures to re-concept the Manchu Wok location. The Authority’s President and CEO was consulted with regard to this recommendation and agreed to the proposed resolution to this finding, provided that DNC is in compliance with all other aspects of their contract requirements.

Finding #6

Observation

DNC is not submitting to the Authority a quarterly update regarding recent trends or developments in Airport food and beverage concession operations.

Background

According to Section 4.2 (k), Concession Management, of the Master Lease and Concession Agreement, “Concessionaire shall perform the following duties, subject to the terms and provisions of this Agreement:

- k. Remain current with all trends in Airport food and beverage operations and provide to Authority a quarterly update regarding recent trends or developments in Airport food and beverage concession operations.”

An objective of the audit was to determine Concessionaire was submitting a quarterly update regarding recent trends or developments in food and beverage concession operations. Through

audit testing, it was determined that DNC was not submitting to the Authority quarterly updates regarding recent trends or developments in Airport food and beverage concession operations.

Recommendation

Properties should require DNC to comply with the Master Lease and Concession Agreement by submitting to the Authority quarterly updates regarding recent trends or developments in Airport food and beverage concession operations.

Management Response

Properties will request DNC to submit reports regarding trends and developments in food and beverage concession operations henceforth. Properties will also establish trigger dates for periodic report requirements in the Properties Management suspense system.

Finding #7

Observation

DNC was not in compliance with FY 2008 annual reporting requirements.

Background

According to Section 4.6, Annual Reporting, of the Master Lease and Concession Agreement, "Concessionaire shall submit within sixty (60) days after the end of each twelve (12) month period or portion thereof during the Interim Phase, and within sixty (60) days after the end of each Lease Year (and at one other time during each Lease Year if desire by Concessionaire or if requested by Authority), a report that shall contain the following:

- a. A review of the performance of Concession Operations for such prior twelve (12) month period, Lease Year, or other applicable period, as the case may be, including, without limitation, Concession Operator's achievement of sales projections, financial results and other goals and objectives;
- b. The establishment of new operational goals and objectives for the forthcoming Lease Year, including projections, for each Concession Location, of sales per square foot, sale per Enplaned Passenger and payments to Authority for the forthcoming Lease Year;
- c. Identification of Concession Operations that either will or might be replaced during the forthcoming Lease Year, along with photos, drawings, etc., of proposed replacement concepts and the reasons for such recommended changes;

- d. A discussion of Concession Operator's customer service improvements, initiatives and activities, including, without limitation, information on surveys, secret shopper programs, incentives, etc;
- e. Any planned expenditures or investments for improvements in the Concession Locations;
- f. Any changes or improvements in Concession Operations anticipated in the forthcoming Lease Year, such as marketing efforts, training or services at Concession Locations by Concession Operators;
- g. Copies of any consumer surveys completed by a Concession Operator and other industry trend studies;
- h. A review of customer service issues, a complaint summary and how complaints were handled during such prior twelve (12) month period, Lease Year or other applicable period, as the case may be, with respect to Concession Operations;
- i. An updated listing of Concession Locations, including, without limitation, names, types and square footage of Concession Locations;
- j. A listing of any problems encountered during such prior twelve (12) month period, Lease Year or other applicable period, as the case may be, and/or improvements to operations to enhance customer service, sales or other aspects of Concession Operations that might reasonably be completed by Authority in concert with Concessionaire; and
- k. Any other information reasonably requested by Authority."

An objective of the audit was to determine DNC was complying with annual reporting requirements. Through audit testing, it was determined that DNC had not submitted their FY 2008 annual reporting to the Authority. DNC's General Manager started in January 2009 and was not aware of the annual reporting requirements specified in the Master Lease and Concession Agreement. However, through the course of the audit, the General Manager was able to produce and submit the annual reporting information for FY 2008.

Recommendation

Properties should be monitoring the Master Lease and Concession Agreement to ensure DNC is complying with the annual reporting requirements by formally notifying DNC to submit their annual reporting within sixty (60) days after the end of the Lease Year and reviewing the report for compliance purposes.

Management Response

Properties will request DNC to submit the aforementioned reports relative to their food and beverage concession operations henceforth. Properties will also establish trigger dates for periodic report requirements in the Properties Management suspense system.

Finding #8

Observation

Properties is not conducting monthly meetings with DNC to discuss operational issues.

Background

According to Section 4.2 (dd), Concession Management, of the Master Lease and Concession Agreement, “Concessionaire shall perform the following duties, subject to the terms and provisions of this Agreement:

- dd. Participate in weekly meetings with Authority staff representatives during the Pre-Occupancy and Interim Phases, and monthly meetings with Authority staff representatives during the Operational Phase, to discuss operational issues.”

An objective of the audit was to verify Authority personnel were conducting monthly meetings with Concessionaire to discuss operational issues. Through audit testing, it was determined that Properties was not conducting monthly meetings with the food and beverage concessionaire’s operating at the Airport.

Recommendation

Properties should be complying with contract requirements by conducting monthly meetings with DNC to discuss operational issues and to enhance the Authority’s commitment to providing the Nashville Airports Experience to its business partners and customers.

Management Response

Properties will comply with contract requirements by formalizing and documenting monthly meetings held with DNC to discuss operational issues and to enhance the Authority’s commitment to providing the Nashville Airports Experience to its business partners and customers.

Finding #9

Observation

DNC is not achieving the DBE participation goal of 15.7% established in the Master Lease and Concession Agreement.

Background

According to Section 7.2, DBE Participation Goals, of the Master Lease and Concession Agreement, “To provide a fair opportunity for DBE participation in the Concession Program, Authority requires that Concessionaire make good faith efforts, as described in 49 C.F.R. Section 23.95(i), to provide for a level of Authority-certified DBE participation in the Concession Program that results in the generation of fifteen and seven tenths percent (15.7%) or more of total Gross Receipts from Concession Operations that are attributable to the participation of Authority-certified DBEs in the Concession Program; provided, however, that Gross Receipts derived from in-flight Catering Services shall not be included in Gross Receipts for purposes of calculating the percentage of DBE participation in the Concession Program.”

An objective of the audit was to verify DNC was meeting the DBE Program requirements established in the Master Lease and Concession Agreement. DNC’s DBE participation goal was 15.7% of total gross receipts and DNC achieves DBE participation through a sublease agreement with Wendy’s, their DBE partner. Through audit testing it was determined that for 2008 DNC achieved a DBE participation level of 8.95%, which is detailed below.

Wendy's Total Gross Receipts	DNC Total Gross Receipts	DBE %
\$903,771	\$10,098,329	8.95%

On June 19, 2009, the Authority’s Director of Business Diversity Development (“BDD”) sent a letter notifying DNC of their non compliance in meeting the DBE participation goal of 15.7% and requested a meeting between DNC, BDD, and Properties to discuss possible remedies. A meeting was conducted on August 11, 2009, and several possible remedies were discussed. On August 15, 2009, DNC sent the Director of BDD a letter summarizing the meeting and provided an update on DNC’s recent efforts towards achieving more DBE participation, which is detailed below:

1. DNC will provide MNAA with all purchases to date for Kijiji Coffee. Update; Kijiji Coffee represents approximately .30% of total revenues for 2008.
2. DNC will meet with David Swett and explore ACDBE certification. Update; Met with David Swett on August 11, 2009. David Swett is currently not interested in becoming ACDBE certified.
3. DNC will meet with Salvador Guzman and explore ACDBE certification. Update; Salvador Guzman expressed interest in becoming ACDBE certified and will request required documents from MNAA. DNC will also explore the possibility of purchasing produce from Mr. Guzman.
4. DNC will continue to explore other reasonable options to resolve its non-compliance.

DNC should continue to make good faith efforts towards achieving more DBE participation.

Recommendation

Properties should ensure DNC is continuing to make good faith efforts toward achieving the DBE contract participation goal of 15.7% and updating the Authority's Director of BDD with such efforts.

Management Response

Properties will ensure DNC is continuing to make good faith efforts toward achieving the DBE contract participation goal of 15.7% and coordinate with the Authority's Director of BDD regarding such efforts.

Finding #10

Observation

DNC's monthly gross revenue reports submitted to the Authority are not disclosing the required DBE participation information.

Background

According to Section 5.1, Periodic Rent, of the Master Lease and Concession Agreement, "Concessionaire shall submit, on or before the twentieth (20th) day of each month, (i) a Concession Location Sales Report in the form of the Exhibit H hereto that details the total Gross Receipts for such preceding month from the Concession Program and a breakdown of such Gross Receipts by Concession Location, and (ii) DBE utilization reports in a form acceptable to Authority."

According to Section 7.2, DBE Participation Goals, of the Master Lease and Concession Agreement, "To determine compliance with such DBE participation goal, Authority requires that Concessionaire submit certified monthly reports indicating the Gross Receipts of all Concession Operations and the Gross Receipts of all DBEs participating in the Concession Program as described in this Section 7.2."

An objective of the audit was to verify DNC was meeting the DBE Program requirements established in the Master Lease and Concession Agreement. Through audit testing, it was determined that DNC was submitting monthly concession location sales reports utilizing the Exhibit H form and Wendy's was submitting the required gross receipts information. However, the Authority revised the Exhibit H form to better capture the gross receipts of all DBEs participation in the Concession Program by requiring the Concessionaire to disclose the DBEs gross sales and percentage of total gross sales on a monthly basis. DNC has not been utilizing the revised forms. An example of the revised form is provided below.

Concessionaire Report of Gross Sales

**Please email this report to finance@nashintl.com
no later than the 15th of the following months activity**

Send Payment to:

Metropolitan Nashville Airport Authority
P O Box 440302
Nashville, Tennessee 37244-0302

Concessionaire Information:

Contact:

Reporting Month/Year _____

Gross Sales						
Revenue Type ----->	Alcohol	Food & Bev	Retail		Total Sales	Total Transactions
Percentages Due	12%	15%	15%	0%		
January					0.00	0
February					0.00	0
March					0.00	0
April					0.00	0
May					0.00	0
June					0.00	0
July					0.00	0
August					0.00	0
September					0.00	0
October					0.00	0
November					0.00	0
December					0.00	0
Total	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0</u>

Gross Sales Percentages Due	12%	0.00
	15%	0.00
	15%	<u>0.00</u>
Total Percentage Due		0.00
Less: Monthly Minimum Guarantee		0.00
Additional Revenue due to MNAA		<u>0.00</u>

Portion of DBE Gross Sales	\$ _____	DBE % of total Sales	% _____
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I certify this report to be a true and accurate summary of all operations required to be reported under the terms of the concession agreement with Metropolitan Nashville Airport Authority.

Company Representative:

Recommendation

Properties should require DNC to submit the monthly concession location sales reports utilizing the revised Exhibit H form to ensure compliance with contract terms and to assist the Authority in monitoring DNC’s monthly DBE participation levels.

Management Response

Properties will notify DNC to submit the monthly concession location sales reports utilizing the revised Exhibit H form to ensure compliance with contract terms and to assist the Authority in monitoring DNC’s monthly DBE participation levels.

Finding #11

Observation

BDD has not processed Wendy's DBE certification information in a timely manner.

Background

According to Section II, Number 4, Annual Renewal of Certification, of the DBE and SMWBE Policy and Process Manual, "The DBE(s) must provide a completed TNUCP Renewal Application to MNAA every year on the anniversary date of their initial certification. This application must include the following documents as listed on the Disadvantaged Enterprise Renewal Application letter:

- a. Copy of most current corporate tax returns with all attached schedules.
- b. Copy of most current personal tax returns with all attached schedules.
- c. Completed Renewal Application, signed by applicant(s) and notarized."

An objective of the audit was to verify DNC was meeting the DBE Program requirements established in the Master Lease and Concession Agreement including Wendy's annual renewal of certification. Through audit testing, it was determined that the Authority issued Wendy's DBE certification on March 31, 2006 with an expiration date of March 30, 2009. Wendy's submitted the required 2007 annual renewal of certification information to the Authority. However, BDD did not request the 2008 annual recertification information from Wendy's because BDD required all Airport Concession Disadvantaged Business Enterprise ("ACDBE") to complete the full DBE certification process again, due to a recommendation from an outside DBE consultant to the Authority.

On June 2, 2009, the Authority's Certification Specialist sent a letter to Wendy's requesting the submittal of a new Uniformed Certification Application, Personal Financial Statement, and business and personal federal tax returns for the 2006 through 2008 tax years. It should be noted that BDD did not request Wendy's 2008 DBE certification information until June 2, 2009, approximately 95 days after the anniversary date of the initial certification. Wendy's had 30 days to submit the requested documents.

The Authority's certification process consists of the following four stages:

1. Preliminary Review – Submitted documents are checked for completeness. Applications that do not contain the required notarized and signed documents will be returned.
2. Desk Audit – Supporting documents are reviewed and additional information may be requested.
3. Site Visit – BDD will arrange for and conduct an on-site visit at the business location. If the firm has had a site visit from another TNUCP agency, the Authority will request the on-site visit report from that agency. If the firm is not located in the State of

Tennessee and the home state certifying agency has conducted a site visit, the Authority will request the on-site visit report from that agency.

4. Final Decision – A final decision to approve or deny a firm's ACDBE certification is made after a thorough review of the application and submitted documents.

Wendy's submitted to the Authority the required application and documents within 30 days. A letter dated July 1, 2009, was sent to Wendy's confirming the Authority had received the application and supporting documents. However, as of November 18, 2009, BDD had not completed processing Wendy's certification information and was in the process of reviewing supporting documents, performing an on-site visit, and issuing a final decision.

According to BDD, due to the complexity in determining certification requirements, the Authority engages the services of a consulting firm to complete pending certifications and re-certifications.

Recommendation

BDD should make certain ACDBE annual recertification information is sent prior to the anniversary date of the initial certification; supporting documentation is thoroughly reviewed; and a final determination is made in a timely manner for all ACDBE certifications and annual re-certifications.

Management Response

BDD is in agreement with the recommendation. BDD made a decision to engage the assistance of a consulting firm with expertise in ACDBE program evaluation and effectiveness due to changes and new requirements in the federal regulations 49 CFR part 23 for ACDBEs. The funds to accomplish this were budgeted in the 2009 fiscal year. Bridgeman Foods, Inc. and all ACDBEs are undergoing an extensive in depth certification review to ensure compliance with the federal regulations. Once completed BDD will request the abbreviated re-certification documents on an annual basis in accordance with its procedures.