



WENDY GREUEL
CONTROLLER

January 12, 2012

Honorable Antonio R. Villaraigosa, Mayor
Honorable Carmen Trutanich, City Attorney
Honorable Members of the Los Angeles City Council

In December 2001, the City entered into a 20-year street furniture contract with the anticipation of receiving up to \$150 million in revenue. This contract gave CBS Decaux the exclusive right to sell and display advertising on specific items of street furniture and was intended to expand the City's street furniture program by providing modern amenities for transit patrons, while also generating significant revenue for the City. In the audit I am releasing today, I sought to determine whether the City has received all revenues it is entitled to under this agreement.

One thing is certain, the city did not realize the amount of proceeds it was led to believe it would be receiving when the contract was executed. It is clear, however, that this contract was unrealistic in terms of expectations from the very beginning. As a result, what the Council was led to believe would be coming their way in terms of revenue, was not ever likely to occur.

According to the contract, the City could have received at least \$53 million in revenue within the first 10 years; however, from its inception through January 2011, the City only realized \$29.9 million. The \$23.1 million lost through this contract consists of approximately \$8.2 million in revenue due to the methodology used to calculate annual fees paid to the City combined with \$14.9 million for delays in approving site permits.

The contract obliged the City to a rollout schedule of the installation of street furniture with advertisements placed throughout the City that was simply not realistic. With a cumbersome approval process in place, the city was primed for failure to meet the agreed upon schedule from the start, making the possibility of earning the entire \$150 million a non starter. If a contract amendment is not pursued to resolve outstanding issues, \$57 million more could be lost.

Finally, the contract required a six-year review by both parties that still has not happened because of pending contract negotiations that never came to fruition. While

Honorable Antonio R. Villaraigosa, Mayor
Honorable Carmen Trutanich, City Attorney
Honorable Members of the Los Angeles City Council
January 12, 2012
Page 2

this overdue review surely would have revealed the magnitude of the loss of revenue to the city, had it been done timely, the fact remains that it still hasn't been done today.

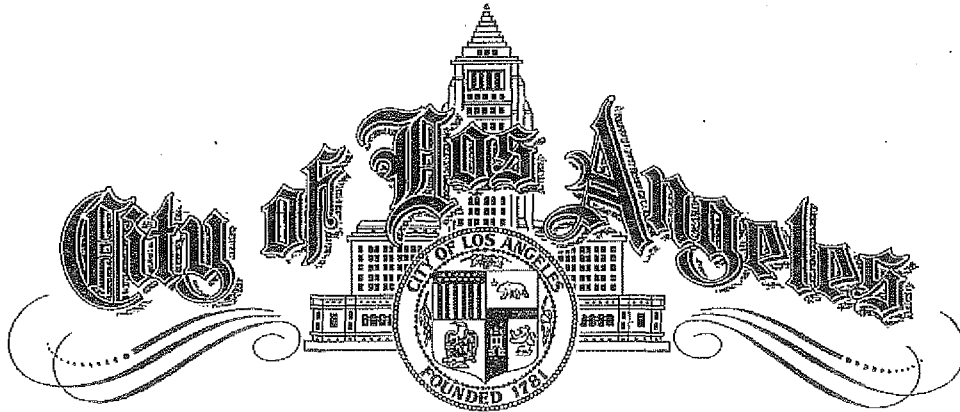
Similar to the recommendations that I made in my audit of Real Property Trust Funds, Street Furniture revenues provide another opportunity to place more money in the City's General Fund, rather than in individual Council district funds. Since 2002, each Council district has received more than \$1 million in funds for community improvements. Given the state of Los Angeles' struggling economy, I am calling on the Mayor and City Council to put 100% of these funds into the General Fund.

Given the high stakes that are at risk in this contract, I urge the Bureau of Street Services and the City Attorney to revisit the terms of this contract to generate as much revenue as possible for the City. Creating a more effective and efficient City requires the assistance of all City entities and we cannot afford any further delays to take action.

Sincerely,



WENDY GREUEL
City Controller



WENDY GREUEL
CONTROLLER

January 12, 2012

Nazario Saucedo, Interim Director
Department of Public Works/Bureau of Street Services
1149 South Broadway, Suite 400
Los Angeles, CA 90015

Dear Mr. Saucedo:

Enclosed is a report entitled, "Audit of the City's Street Furniture Contract with CBS Decaux, LLC." A draft of the report was provided to your Department and comments made by your Department at the August 2, 2011 exit meeting were evaluated and considered prior to finalizing this report. A draft report was also discussed with representatives of the Chief Legislative Analyst, the City Attorney's Office and CBS Decaux during October and December 2011. Comments from these agencies, as well as additional information provided, were considered in finalizing the report.

Please review the final report and advise the Controller's Office by February 10, 2012 on planned actions you will take to implement the recommendations in the report. If you have any questions or comments, please contact me at (213) 978-7392.

Sincerely,

A handwritten signature in black ink, appearing to read 'Farid Saffar'.

FARID SAFFAR, CPA
Director of Auditing

Enclosure

cc: Gaye Williams, Chief of Staff, Office of the Mayor
Andrea A. Alarcon, President, Board of Public Works
Miguel A. Santana, City Administrative Officer
Gerry F. Miller, Chief Legislative Analyst
June Lagmay, City Clerk
Francois Nion, Co-Managing Director, CBS Decaux
Independent City Auditors





**City of Los Angeles
Office of the Controller**

**Audit of the City's Street Furniture Contract
with CBS Decaux, LLC**

January 12, 2012

Wendy Greuel
City Controller

TABLE OF CONTENTS

EXECUTIVE SUMMARY.....1

CONTROLLER’S ACCOUNTABILITY PLAN 8

BACKGROUND, OBJECTIVES, SCOPE AND METHODOLOGY.....9

AUDIT FINDINGS AND RECOMMENDATIONS17

SECTION I. ANNUAL FEE DUE TO THE CITY.....17

SECTION II. SITE/PERMIT APPROVAL PROCESS & PROGRAM REVIEW24

APPENDIX A - RANKING OF RECOMMENDATIONS..... 32

ATTACHMENTS.....33

**AUDIT OF THE CITY'S
STREET FURNITURE CONTRACT WITH CBS/DECAUX, LLC**

EXECUTIVE SUMMARY

BACKGROUND

In 2001, the Board of Public Works (BPW), on behalf of the City, executed a 20-year agreement with a term from January 2002 to December 2021 with Viacom Decaux LLC (now called CBS Decaux LLC) to operate the City's Coordinated Street Furniture Program.

The City contracts with CBS Decaux, LLC (CBS Decaux or the Contractor) to operate a street furniture advertising program on the City's behalf. Under the terms of the agreement, the City anticipated receiving up to \$150 million by giving CBS Decaux the exclusive right to sell and display advertising on specific items of street furniture which are installed and maintained by the Contractor. Because the furniture items are on City property, a permit for each item must be approved by City officials prior to its installation. This revenue goal was contingent upon the City issuing permits for all furniture items as specified in the contract's projected rollout schedule. The contract anticipated that the furniture items, which include automated public toilets; transit shelters; newsstands; and public amenity pillars and kiosks, with a combined total of 3,430 advertising panels, would be permitted within two years of contract approval.

The Contractor covers the cost of installation, maintenance, repair and removal of both the furniture items and advertising panels. The Contractor sells the advertising space to interested parties and retains the majority of the ad revenue. Through this arrangement, residents enjoy the use and benefits of City-approved street furniture and the City receives a minimum annual fee and an opportunity to share in the revenue generated from advertising. The Department of Public Works, Bureau of Street Services (BSS) administers the agreement and performs Contractor oversight.

The primary objective of this audit was to determine whether the City has received all revenues it is entitled to under this agreement. The audit also assessed the City's processes relative to permitting street furniture to identify the reasons for untimely approvals which have impacted the amount of revenue received by the City.

SCOPE AND METHODOLOGY

Our audit was performed in accordance with Generally Accepted Government Auditing Standards (GAGAS) and covered the revenue reported from January 2002 to January

2011. Fieldwork was conducted primarily between February and May 2011, with supplemental review activities conducted from October through December 20, 2011. In conducting our audit, we interviewed CBS Decaux and BSS staff and management; reviewed the contract agreement; and reviewed applicable policies and procedures used by both the City and the Contractor to obtain an understanding of the key agreement provisions and processes for collecting and reporting advertising revenue. We also selected sample records and reviewed key documents such as advertising contracts, advertising posting documents, and customer invoices. In addition, we recalculated annual fees due to the City based on Article 24.3 of the contract, and compared those amounts to the payments received from the Contractor.

SUMMARY OF AUDIT RESULTS

The CBS Decaux contract was intended to expand the City's street furniture program by providing modern amenities for transit patrons, while also generating revenue for the City. Through the first ten years of the agreement, the City could have received at least \$53 million in revenue. However, from inception through January 2011, the City has realized only \$29.9 million.

The primary cause of the lost revenue opportunity was the City's untimely approval of permits. Due to the site approval process required by the City, which includes sign-off by affected council offices, some delays were anticipated. Indeed, a "Remedy for Delay" provision was included in the contract that allows the Contractor to reduce the Minimum Annual Fee when the City has failed to approve all properly requested permit applications for new Ad Panels, as set forth in the proposed rollout schedule.

Even though as of 2009 the City had permitted 69% of the contractual number of ad panels, because both parties had a mutual understanding that the fee adjustment was contingent on the City permitting each specific type of furniture item within a rollout period prior to advancing to the next period, the City is only receiving credit for 12.48% of those panels. The financial effect of this contract interpretation totaled \$8.2 million in lost financial opportunity for the City.

According to the parties involved, regardless of the total number of permits issued, because the City failed to approve permits for pillars at specific locations requested by the Contractor within the projected timeframe, the program has not moved out of the first rollout period (P1), which was anticipated to conclude by September 30, 2002. City officials and the Contractor stated that the approval of pillars within specific council districts during the early rollout periods was necessary to make the program economically viable for the Contractor.

By 2008, the City had finally approved the number of pillar sites that had been projected through P4 of the rollout schedule (noted as Year 1 in the Contract). However, the Contractor indicated it is no longer economically viable to make the capital investment for these structures under the current contract; therefore CBS Decaux has not applied for construction permits to install the pillars. This disagreement has created an impasse

between the parties with respect to whether the City has fulfilled its obligations and should be compensated at the P4 level from 2009 forward.

If the contract is not modified with respect to the Projected Rollout Schedule by furniture type and the resulting impact on the City's Minimum Annual Fee, the impasse between the City and the Contractor will continue. The City could remain in P1-P2 throughout the life of the agreement, resulting in an additional lost revenue opportunity that exceeds \$57 million. We strongly urge City officials to pursue a contract amendment to resolve these issues to the mutual benefit of the City and CBS Decaux.

The following provides a summary of our audit findings. Additional details on the program and these findings are provided in the narrative sections of the report.

- **Although CBS Decaux is entitled to adjust the stated minimum annual fee in the event the City delayed approving the required number of permits, through 2011, the City lost the opportunity to collect \$8.2 million due to the methodology used to adjust annual fees paid to the City.**

The contract states that the City will receive a minimum annual fee, ranging from \$3 million in the early years of the agreement, to \$11.5 million by 2018. However, if the City fails to issue 100% of permits for the required number of advertising panels, the contract terms allow the Contractor to adjust the stated minimum annual fee (MAF) based on the ratio of the number of ad panels on furniture items where permits have been issued, to the contractual number that was expected to have been issued based on the project's rollout schedule. Regardless of the permit approval rate, the City is guaranteed \$2 million per year. According to Article 24.3 of the agreement, to adjust the MAF due to permit delays, the difference between \$2 million and the stated MAF for each year is multiplied by the ratio of the aggregated number of permits for ad panels issued, to what had been requested through December 31st of the concluding year. The adjustment amount is then added to the \$2 million minimum to derive the revised MAF due.

For example, for the 2011 payment, if the City had issued permits for 100% of the contractual sites and related number of ad panels as of December 31, 2010, the City would have received \$7.5 million as the minimum annual fee. However, since records show that through that date, the City had only issued permits for sites with approximately 69% of the contractual number of ad panels, in our opinion, CBS Decaux was entitled to adjust the MAF based on this approval rate. In accordance with the method described in Article 24.3, the MAF for 2011 should have been \$5.8 million. This equates to the \$2 million guaranteed amount, plus \$3.8 million (which is 69% of \$5.5 million, the unadjusted MAF of \$7.5 million less the guaranteed amount of \$2 million).

However, rather than using the 69% compliance rate, CBS Decaux used 12.48%. The Contractor credits the City with only the number of ad panels related to furniture items permitted through the first two measurable time periods of the Project Rollout

Schedule (PRS) defined as P1 and P2, even though the agreement is well into its tenth year. The Contractor's rationale was that the City had failed to issue permits for any pillars, and at least 50 pillar-style amenity kiosks with 200 ad panels should have been approved by P2 per the rollout schedule; therefore, the agreement has not advanced beyond P2.

Based on our discussions with representatives of the Office of the Chief Legislative Analyst (CLA), the City Attorney and the Contractor's representatives, the City had a contractual understanding with CBS Decaux that defined the progression to a subsequent period only when the City had achieved the targeted number of permit approvals for each specific type of furniture item¹. However, we found no evidence demonstrating if the City considered and presented to policy makers how this contractual understanding and interpretation affected the MAF calculation and its significant detrimental financial impact to the City, nor the acceptance of an apparent inconsistent methodology that compared approval numbers through one period that were capped at the targets for that period, against the total targeted approvals for the entire agreement term. This inconsistent methodology is in direct contrast with the terms of the agreement that was executed and agreed to by both parties.

According to this understanding, while the City has issued permits for sites with 2,370 ad panels through December 31, 2010, CBS Decaux credited the City for only 428 panels related to permits issued up to the target for P1-P2, yet it compares that figure to the total 3,430 panels contemplated through P8. This methodology ignores the additional 1,942 ad panels related to permits the City has approved for shelters, newsstands and public amenity kiosks through December 31, 2010, even though these panels have been generating revenue for the Contractor. Even under the rationale that the City remains in P1-P2, if the Contractor had used equivalent periods for both approvals and the target for that period, the adjustment factor would have been comparable.

By calculating the MAFs for 2003 through 2011 based on the Contractor's methodology, the City lost approximately \$8.2 million in potential revenue.

If this continues, whereby the program cannot advance beyond P2 and the MAF adjustment is calculated in the same manner, the City could lose an additional \$57 million in potential revenue over the remaining term of the agreement. Therefore, it is imperative that the City Attorney, in collaboration with the CLA and BSS, work to renegotiate the contract to the mutual benefit of the City and CBS Decaux, and present a contract amendment for Mayor and Council approval.

¹ It should be noted that the contract defines Rollout Period as a three-month period of time, as set forth in the Projected Rollout Schedule (PRS), and further states "there are eight three-month Rollout Periods during Phase I of the PRS". The contract's PRS is included as Attachment I to this report.

- **The Contract's site and permit approval process is very cumbersome and has resulted in the untimely approval of the required number of permits. Consequently, the City has lost approximately \$15 million in potential revenue.**

Based on a sample of sites, our review disclosed that it took an average of 129 days for council offices and all involved departments to approve the sites and permit applications. These untimely approvals have resulted in the City losing approximately \$15 million in potential revenue through 2011. This is in addition to the \$8.2 million previously cited.

The site approval process begins when the Contractor submits a list of proposed sites to the Councilmember(s) of the district(s) where the sites are located. Our review, which analyzed timeframes for a variety of furniture items actually installed, disclosed that council offices took an average of 28 days to approve site applications they received. Once a Councilmember approves a site, the Contractor informs BSS, and a notification is mailed to any property owners who may share a common boundary with the proposed site. If a property owner objects to the placement of a furniture item, the complaint is forwarded to the Board of Public Works for review and resolution. For our sampled sites, it took an average of 12 days from the council offices' approval before notifications were mailed to the property owners.

If no objection is received from the property owners within 15 days, a site approval form is distributed simultaneously to eight task force departments to review the site(s) to ensure conformity to City codes and ordinances. Task force departments took an average of 62 days to approve the sampled sites.

Once a site is approved by the task force, CBS Decaux initiates a request for a final permit and submits design drawings for the specific furniture item, first to the Bureau of Street Lighting and then to the Department of Water and Power. These two departments review the design's electricity requirements. Once they have approved the furniture drawings, the Bureau of Engineering issues a construction permit. Based on our sample of installed furniture items, the final construction permit process involving these three departments took an average of 27 days to complete.

While the Chief Legislative Analyst had previously recommended a contract amendment to address the site approval process, the amendment was never approved by Council. In order to maximize potential revenue under this contract, the City must formally address, along with the previously discussed MAF issue, the need for a more expedited process to approve a site and/or permit relative to the installation of street furniture.

- **The City did not complete the required Year Six Review that was intended to identify unanticipated problems and to develop mutually agreed upon solutions to achieve the revenue and service goals contemplated by the agreement.**

Article 6 of the agreement requires a Year Six program review that would allow the City and the Contractor to identify and discuss any issues and problems that were not originally anticipated, so that both parties could mutually agree on appropriate adjustments and modifications to the program to achieve the service and revenue goals contemplated by the agreement.

On January 15, 2008, the Council adopted a motion instructing the City Attorney, BSS and the CLA to work with CBS Decaux to complete a Year Six review. However the review was never conducted. In April 2008, City officials and the Contractor agreed to forgo the formal Year Six review pending their ongoing contract amendment negotiations. However, the contract was never amended. Though the program is now in its tenth year, there remain issues relative to the program's full implementation that must be addressed. Therefore, it may still be beneficial for the City and the Contractor to conduct such a review, and use the results to develop changes that are necessary to improve the program.

REVIEW OF REPORT

The findings noted by our audit were formally discussed with BSS on August 2, 2011. A draft report was provided to representatives of the Chief Legislative Analyst and the City Attorney's Office on September 22, 2011 and additional information provided in October and November was considered in finalizing the report. We also discussed the contents of the report with CBS/Decaux at an exit conference held on December 12, 2011, and considered their comments in finalizing the report.

BSS' views on the significant findings are as follows:

Finding #1 – Loss of \$8.2 million in potential revenue

BSS stated that, before the agreement had been signed, City officials involved (i.e., representatives of BSS, City Attorney and Chief Legislative Analyst) as well as the Contractor agreed to a mutual understanding that the program would remain in a particular phase (e.g., P1, P2, etc.) until the City had approved the required number of permits for that phase/period for all furniture types, and that the minimum annual fees would be adjusted on that basis. Therefore, the Department believes that the Contractor's methodology for adjusting the minimum annual fees due to the City was appropriate, at least from 2002 to 2008. However, this understanding and agreement was not formally incorporated into the contract executed by both parties. Since then, BSS believes that the City is owed approximately \$4 million in additional revenues due

to a disagreement as to whether the City has now progressed beyond P2, based on site approvals for pillars.

As discussed in the Audit Findings and Recommendation Section of this report, the "Remedy for Delay" provisions in the written contract calls for an adjustment based on an aggregated number of sites and associated ad panels permitted by the end of each calendar year. Therefore, in our opinion, this criterion as stated in the contract should have been used to compute the amount due to the City for each year. City officials should have revised or amended the written contract to clearly reflect such an understanding, as this would significantly reduce the annual amounts due to the City below what was termed the "minimum annual fee" revenues that were initially anticipated.

Finding #2 – Loss of an additional \$15 million in potential revenue

BSS stated that the requirement for council office approvals as the first step for all potential furniture installations led to the majority of delays encountered in implementing the program, and the resulting loss of potential revenue. The Department stated that significant delays occurred at this stage, and numerous site applications were approved or denied only after a considerable period of time, while others were never formally approved or denied. According to BSS, as of the end of November 2011, more than 15% of proposed street furniture sites submitted to council offices had still never been formally approved or denied. BSS disagreed with our audit sampling approach to derive timelines for furniture items that had been installed. BSS believes that an expanded sample that included declined applications and those not acted on by council offices would show that the street furniture site permitting process actually took much longer as a result of council offices' delays.

Our sample was selected from a database of furniture items installed between 2004 and 2009 and consisted of two installed furniture items per council district. The application process for these locations started between 2002 and 2004. Because a significant proportion of items installed were transit shelters, the sample consisted mostly of shelters. Our objective was to obtain an estimate of how long it took each respective City office/department to provide approvals during the permit process for furniture that had been installed. Therefore, our sample did not include unapproved applications or those that were never acted upon by council offices. Regardless, the issue being raised in this report is that the City's process for approving and issuing permits for street furniture sites is cumbersome, and has contributed to millions of dollars in lost revenue opportunity to the City.

We would like to thank BSS management and staff, representatives of the Chief Legislative Analyst and the City Attorney's Office, as well as CBS Decaux for their cooperation and assistance during the audit.

CONTROLLER'S ACCOUNTABILITY PLAN

RECOMMENDATIONS	PAGE REFERENCE	MAYOR ACTION REQUIRED	COUNCIL ACTION REQUIRED	DEPARTMENT ACTION REQUIRED
<p>1. The City Attorney, in collaboration with the CLA and BSS, should work to renegotiate the contract to the mutual benefit of the City and CBS Decaux, and present any proposed amendments to the Mayor and Council for approval.</p>	23	X	X	BPW BSS City Attorney CLA
<p>2. BSS management, the council offices, all affected departments and the Contractor should mutually develop and include a revised site approval and permit process as part of any future contract amendment. This could include limiting the number of parties involved in the approval process.</p>	29	X	X	BSS CLA BOE BSL BCA LAPD DOT DWP PLANNING
<p>3. BSS management should, in conjunction with the Contractor and other appropriate parties, initiate a comprehensive street furniture program evaluation that complies with the "Year Six review" provision of the agreement.</p>	31			BSS City Attorney

BACKGROUND, OBJECTIVES, SCOPE, AND METHODOLOGY

On December 21, 2001, the Board of Public Works, on behalf of the City, executed an agreement (City contract #C-102477) with a 20-year term extending from January 2002 to December 2021 with Viacom Decaux LLC (now called CBS Decaux) to operate the City's Coordinated Street Furniture Program. CBS Decaux, LLC is a joint venture between CBS Outdoors (a division of CBS Corporation) and JC Decaux North America, Inc. The companies operate similar street furniture programs in many cities around the world.

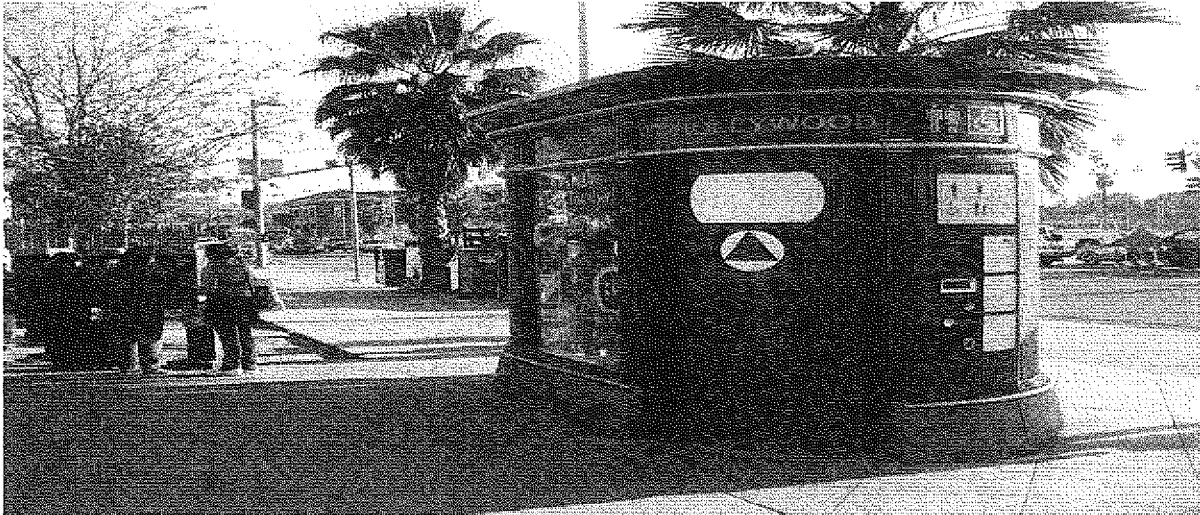
The City contracts with CBS Decaux, LLC (CBS Decaux or the Contractor) to operate a street furniture advertising program on the City's behalf. Under the contract, the City grants CBS Decaux the exclusive right to install and maintain street furniture in exchange for the right to sell and display advertising on the furniture. The contract specified that CBS Decaux would supply, install and maintain the following numbers and types of furniture, which are located adjacent to City streets, generally on City sidewalks: 150 automatic public toilets (APTs), 1,285 new and 900 replacement bus shelters, 315 existing bus shelters, 500 public amenity kiosks (PAKs), 100 pillars and 100 vending or newsstand kiosks.

The Contractor is responsible for the installation, maintenance, repair and removal of street furniture items and advertising panels. The Contractor covers these costs through the sale of advertising space, and shares a proportionate amount of the ad revenue with the City. Through this arrangement, residents enjoy the use of the furniture at no cost to the taxpayer; rather, the City receives a portion of the revenue generated from the advertising, as remitted from CBS Decaux. The Department of Public Works' Bureau of Street Services (BSS) administers and provides oversight over the contract.

The following pages provide brief descriptions of each type of street furniture to be provided by CBS Decaux as part of this agreement:

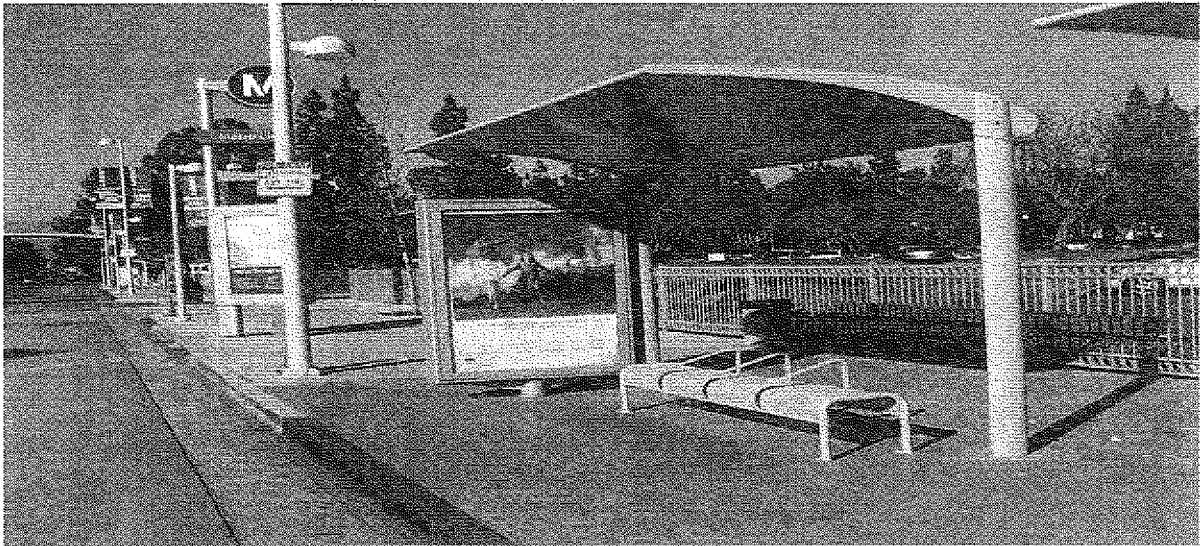
Automatic Public Toilets (APT)

The APT is an enclosed structure containing a self-cleaning automatic public toilet available for use by the general public. They are primarily coin operated or free, and are designed to be accessible to persons with disabilities. All units are self-cleaning, which means that the entire interior of the APT is sanitized after each use. All APTs are serviced and maintained year-round by CBS Decaux. The APTs do not contain ad panels, and therefore are not considered “revenue generating” furniture.



Transit Shelters

These structures provide shelter for transit riders awaiting public transportation. CBS/Decaux makes five different shelter designs available to the City to choose from. Transit shelters may have one or two ad panels.



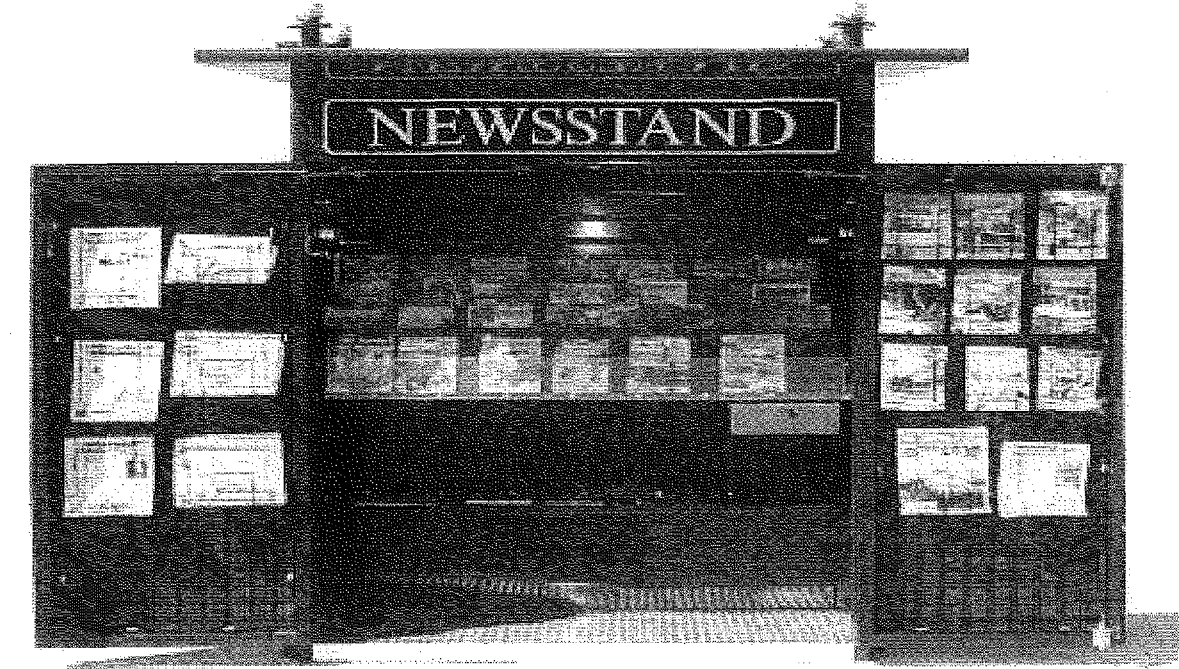
Public Amenity Kiosks (PAK)

This is a free-standing structure that may be two or three-sided, that include panels for both advertising purposes and a public amenity display, such as a local vicinity map, a community poster, or other form of community announcement.



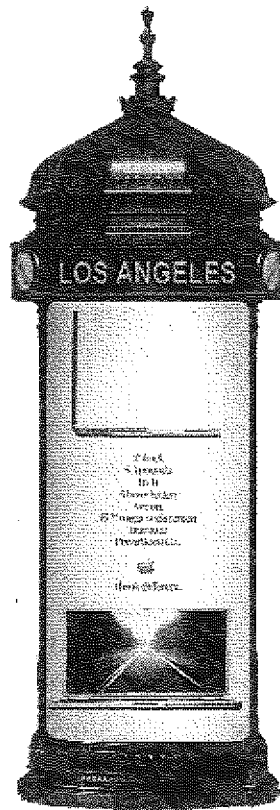
Vendor and Newsstand Kiosks

Vending kiosks are installed by the Contractor for use by City-approved vendors to sell newspapers/magazines as authorized by the City, which may also contain ad panels.



Pillar style- Public Amenity Kiosks (Pillar)

The "Pillar" style Public Amenity Kiosk is an internally-lit columnar structure with three faces - two for commercial advertising and one for a City Amenity Component(s), such as litter or recycling bin, computer terminal, a pay phone or an emergency phone, above ground monument, or a display area for non-commercial posters or services. The Pillar is 4 feet 7 inches in diameter and 14 feet 4 inches in height.



Payment Structure

Pursuant to Article 4.5 of the agreement, over the 20-year life of the contract, the City anticipated receiving up to \$150 million in minimum annual fees (MAF), provided that the City issues related permits that would allow CBS Decaux to install all street furniture and related advertising panels as specified in the project rollout schedule. The MAF was \$3 million in the first year (2002) and it gradually increases to \$11.5 million beginning with the seventeenth year. The MAF is due to the City on the first day of each calendar year. Table 1 shows the stated MAFs during the life of the contract:

Table 1

Annual Fees If the City Approves 100% of Permits In Accordance with the Rollout Schedule

Years	Minimum Annual Fee (MAF) Due Each Year	Total MAF Due
2002, 2003, 2004	\$ 3,000,000	\$ 9,000,000
2005	\$ 5,000,000	\$ 5,000,000
2006, 2007, 2008, 2009	\$ 6,000,000	\$ 24,000,000
2010, 2011, 2012, 2013	\$ 7,500,000	\$ 30,000,000
2014, 2015, 2016, 2017	\$ 9,000,000	\$ 36,000,000
2018, 2019, 2020, 2021	\$ 11,500,000	\$ 46,000,000
Total Amount Anticipated		\$ 150,000,000

Source: Article 4.5 of Contract No. C-102477

The contract also specifies that if, at the end of a program year, twenty percent (20%) of the Contractor's annual gross advertising receipts exceed the annual fee made by the Contractor at the beginning of the year, the City is entitled to the difference between 20% of the gross receipts and the payment made². For example, assume that the Contractor paid a \$3 million MAF on January 1, 2003, and by year-end (December 31, 2003), 20% of the Contractor's annual gross receipts for advertising on City street furniture was \$4 million. In this scenario, the City would be entitled to an additional \$1 million (i.e., the difference between the \$4 million and the \$3 million paid on January 1, 2003). Therefore, the City would receive a total of \$4 million for the year 2003.

However, the contract also states that if the City fails to issue permits for the number of furniture items/ad panels within the timeframe contemplated by the projected rollout schedule, the City's stated MAF would be reduced to \$2 million a year plus a pro-rated amount (based on the number of ad panels permitted) of the difference between \$2 million and the stated MAF.

Because the City has failed to adhere to the rollout schedule, it no longer has the opportunity to earn the \$150 million originally anticipated. The issues related to potential lost revenue due to the City are discussed in greater detail later in this report.

² Gross receipts is defined in the agreement as the total compensation (including in-kind payments) actually received by Contractor for the display of advertising, less a) any agency or broker commissions or similar fees; and b) returned or credited advertising fees.

Contract Deliverables

The original rollout schedule, which formed the basis of the stated minimum payments of up to \$150 million over the 20-year term, is presented as Attachment I of this report. As indicated in Attachment I, with the exception of the automatic public toilets, the City was expected to issue permits for all street furniture items (and their associated advertising panels) as provided in the contract during the eight quarters covered by P1 through P8, or within the first two years of the contract term.

Current Performance Status

As of March 2011, BSS records show that the City had issued permits for 1,727 of the 2,135 (81%) furniture items required by the agreement. However, the City has not issued construction permits for any pillars, the furniture type that both parties agreed had the highest revenue-generating potential. Because of delays in approving the permits, the City has lost millions in potential revenue. In addition, CBS Decaux has slowed down furniture installations. As of March 2011, CBS Decaux had only installed 824 (48%) of permitted structures. The table below shows street furniture statistics as of March 2011:

	Contractual	Permitted	% of Contractual Permitted	Installed	% of Permitted Installed
APTs	150	23	15%	15	65%
Shelters	1,285	1,223	95%	614	50%
Pillars	100	-	0%	0	0%
PAKs	500	431	86%	189	44%
Vending Kiosks	100	50	50%	6	12%
	2,135	1,727	81%	824	48%

Source: BSS Records

Fees Paid to the City

The payments received from CBS Decaux are allocated on a 50-50 basis between the General Fund and the Street Furniture Revenue Fund. The portion of the revenue deposited into the Street Furniture Revenue Fund is equally distributed among the 15 council districts. Although the contract requires at least one-third of all pillars, kiosks and newsstands installed be equitably distributed among all 15 council districts, there is no such proportional requirement for transit shelter installations among council districts. Since the inception of the agreement, each council district has received approximately \$1 million.

According to Administrative Code, council districts may use these funds for expenses related to transit services and equipment, beautification projects, and sidewalk curb improvements to improve conditions for public transit patrons.

Table 3 shows the distribution of payments received under the agreement from 2002 to 2011.

	Total Payment Received		General Fund (50% of Total)	Each Council District (50% of Total Divided by 15)
2002	\$ 3,000,000		\$ 1,500,000	\$ 100,000
2003	\$ 2,590,000		\$ 1,295,000	\$ 86,333
2004	\$ 2,160,000		\$ 1,080,000	\$ 72,000
2005	\$ 2,544,178		\$ 1,272,089	\$ 84,806
2006	\$ 3,145,225		\$ 1,572,613	\$ 104,841
2007	\$ 3,057,676		\$ 1,528,838	\$ 101,923
2008	\$ 3,475,249		\$ 1,737,625	\$ 115,842
2009	\$ 3,493,077		\$ 1,746,539	\$ 116,436
2010	\$ 3,378,990		\$ 1,689,495	\$ 112,633
2011	\$ 3,383,752		\$ 1,691,876	\$ 112,792
	\$ 30,228,147	(1)	\$ 15,114,074	\$ 1,007,605

Source: BSS' Records

(1) -This total includes \$327K in additional payments received as a result of escrow activities in 2003, 2005 and 2006.

OBJECTIVES, SCOPE, AND METHODOLOGY

The primary objective of this audit was to determine whether the City has received all revenues it is entitled to under the contract. The audit also assessed the Street Furniture permitting processes, in order to identify where delays were occurring, since the delays have significantly reduced the amount of revenue received by the City. This audit did not include a review of expenses paid from the Street Furniture Revenue Fund, or other funds received by the City through this agreement.

Our audit was performed in accordance with Generally Accepted Government Auditing Standards (GAGAS) and covered the revenue received by the City since inception of the agreement in 2002 through 2011. The 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.

Fieldwork was conducted primarily between February and May 2011, though additional review activities which focused on the City's contractual understanding related to the Project Rollout Schedule were conducted during September and October 2011. In conducting our audit, we interviewed the City's contract administrator and other staff involved in the program, as well as representatives of CBS Decaux, LLC. We also reviewed applicable policies and procedures to obtain an understanding of the key contract provisions and processes involved in the operation of the program. For example, we:

- Obtained and reviewed the contract agreement between the City and CBS Decaux to understand key provisions related to the project rollout schedule, minimum annual fees, remedies for delay, and contract deliverables.
- Selected sample records and reviewed key documents such as site approvals and permits, contracts and invoices related to advertising revenue, and supporting documentation for advertising payments received by the Contractor.
- Tested sample payments received by the City to ensure that payments were recorded and allocated to the City's accounts accurately.
- Physically inventoried furniture items and compared the results to the City's inventory of furniture to obtain reasonable assurance that the inventory includes all items.
- Reviewed a sample of the minutes of monthly program status meetings between City officials and the Contractor, as well as a sample of monthly maintenance reports prepared by the Contractor showing the level of cleaning and repair activities.
- Recalculated annual fees due to the City based on our interpretation of the "remedy for delay" provisions in Article 24.3 of the agreement for each year since Year 1 of the contract.

The remainder of this report details our findings, comments, and recommendations.

AUDIT FINDINGS AND RECOMMENDATIONS

SECTION I. ANNUAL FEE DUE TO THE CITY

Finding #1: Although the Contractor is entitled to adjust the stated minimum annual fee due to the City in the event the City delayed approving the required number of permits, through 2011, the City has lost the opportunity to collect an additional \$8.2 million due to the methodology used to adjust annual fees due to the City.

Article 4.5.1 of the agreement requires the Contractor to make annual payments to the City on or before January 10th of every year. Other than the \$3 million first year payment, the payment for each subsequent year is contingent upon the City permitting 100% of the contractual number of furniture items with the stated number of ad panels in accordance with the rollout schedule noted in the agreement. If the City fails to approve 100% of permits, the Contractor may adjust the stated minimum annual fee (MAF) based on the ratio of the number of ad panels for furniture permits approved, vis-à-vis the contractual number that should have been approved.

Both the City and the Contractor appear to have anticipated permit delays and agreed on procedures for remedies. In fact, Article 2.1 of the agreement states, that,

"In the event the City is unable, notwithstanding its good faith efforts, to approve permits to install the number of ad panels in the agreement, the City shall not be in default of its obligations and Contractor's sole remedies shall be as set forth in the Agreement."

Article 24 (Remedy for Delay) describes the procedure for making necessary annual adjustments. Specifically, Article 24.3 states that, regardless of the permit approval rate, the City is guaranteed \$2 million per year. It further states

"To determine the MAF Adjustment for each new year, the total number of properly requested permit applications for new Ad Panels issued, as of December 31 of the concluding year shall be divided by the lesser of i) the total number of properly requested Ad Panel permits; or ii) the total number of new Ad Panels (the "PRS Target Panels") contemplated to have been issued by December 31 of the concluded year as set forth in the Projected Rollout Schedule."

The resulting percentage is then multiplied by the amount of the stated MAF for the new year, which is above the \$2 million base threshold amount. The adjustment amount is then added to the \$2 million minimum, to derive the revised MAF due.

For example, if the Project Rollout Schedule (PRS) provided that the City should have permitted 200 new ad panels by the end of Year 2 and the Contractor properly requested 200 new ad panel permits, but the City only permitted 150 new ad panels (75%), the annual fee that the Contractor would pay in January of Year 3 is determined as follows: The \$2 million minimum, plus 75% of the MAF above the \$2 million base threshold (i.e. \$1.0 million, since the contract specifies the MAF for Year 3 is \$3 million). Thus, \$2.75 million (\$2 million plus \$750,000) would be paid to the City by January 10th of Year 3.

Because permits have not been approved in accordance with the timeframe anticipated by the PRS, the Contractor has adjusted the stated MAF every year since 2003 (Year 2) using Article 24.3 as a basis. Discussed below is the methodology used by CBS Decaux for adjusting the MAF due to the City for 2011, compared with an estimated amount that should have been payable to the City based on the language of the contract's "remedy for delay" provisions.

AUDITOR'S ESTIMATED 2011 MINIMUM ANNUAL FEE

According to CBS Decaux's records, as of December 31, 2010, excluding APTs³, the City had issued permits for approximately 86% of the contractual number of sites, which equated to 69% of associated ad panels (Table 4 below). Attachment II shows the number of sites that were permitted from 2002 through 2010 as reflected in CBS Decaux's records.

Table 4

Sites Permitted as of December 31, 2010			
	Actual	Contractual	Compliance %
Shelters	1,223	1,285	95%
PAKs	431	500	86%
Pillars	-	100	0%
Vending Kiosks	50	100	50%
Total	1,704	1,985	86%
Ad Panels Related to Sites Permitted as of December 31, 2010			
	Actual	Contractual	Compliance %
Shelters	1,592	1,770	90%
PAKs	728	1,000	73%
Pillars	-	400	0%
Vending Kiosks	50	260	19%
Total	2,370	3,430	69%

Source: CBS Decaux's Records and Project Rollout Schedule

³ APTs have no associated ad panels.

If the City had issued permits for 100% of the contractual number of sites and related ad panels, the City should have received \$7.5 million (the stated MAF for 2011 from Table 1). However, since only 69% of the anticipated ad panels had been permitted as of December 31, 2010, the Contractor was entitled to adjust the stated MAF to reflect this approval rate. In our opinion, based on Article 24.3 of the agreement, the City is entitled to the guaranteed \$2 million plus 69% of \$5.5 million (\$7.5 million MAF noted in the contract for 2011, minus the \$2 million guaranteed threshold amount). This equates to \$5.8 million (\$2 million plus \$3.8 million).

CBS DECAUX'S 2011 MAF CALCULATION

CBS paid the City \$2.6 million as the MAF for 2011. Rather than using the 69% compliance rate, which considers the cumulative number of permitted panels through December 31, 2010, CBS Decaux used only 12.48% in its calculation for the adjustment. The Contractor credits the City with only the number of ad panels permitted through the first two measurable time periods of the PRS, defined as P1 and P2, even though the agreement is well into its 10th year.⁴

According to the Contractor's representatives, since the City failed to approve permits for any pillars, and at least 200 pillar ad panels should have been approved by P2 per the rollout schedule, they believe the program is still in the P1-P2 phase and the City should only be credited for the ad panels approved through those periods, and only up to the target stated for that period.

Therefore, while the City had approved 2,370 panels as of December 31, 2010 (as noted on Table 4), the Contractor credited the City with only 428 panels permitted through P2 as of that date. However, CBS used as the denominator the total 3,430 contractual ad panels, which considered the ad panel target for the entire contract that were anticipated to be installed through P8. The following table illustrates how the Contractor derived the percentage.

⁴ P1 and P2 represent the first two quarters of the first year (2002) of the contract.

Table 5

	Ad Panels Related to Sites Permitted in P1-P2			Contractual #s of Ad Panels (P1-P8)	P1/P2 Actual as % of Contractual Total
	Actual	Target	Compliance %		
Shelters*	138	138	100%	1,770	8%
PAKs	240	240	100%	1,000	24%
Pillars	-	200	0%	400	0%
Vending Kiosks*	50	52	96%	260	19%
Total	428	630	68%	3,430	12.48%

Source: CBS Decaux's Records

*Ad Panel #s for Shelters and Vending Kiosks are not specifically defined by quarter (P1 through P4). Totals for Year 1 were evenly divided, and targets noted for P1-P2 represent 50% of the Year 1 Total.

The Contractor's methodology excluded the effect of 1,942 (2,370 minus 428) ad panels relating to the additional permits for shelters, vending kiosks and PAKs approved by the City since 2002, even though the Contractor has had the opportunity to both install the panels and receive advertising revenue for them. This calculation methodology significantly limited the City's potential revenue.

Article 24.3 specifically requires the Contractor to **aggregate** the number of panels as of December 31 of the concluding year. It states:

"CONTRACTOR shall be entitled to recalculate the MAF at the beginning of any year of this Agreement when CITY has failed to approve all properly requested permit applications for new Ad Panels set forth in the Proposed Rollout Schedule aggregated through December 31 of any year..."

In our opinion, this would imply that the MAF for 2011 should be based on the aggregated number of panels the City permitted through December 31, 2010 regardless of categories by furniture type. However, even if the program was still considered to be in the P1-P2 phase, the actual ad panels permitted through these periods should have been compared to the targeted amount for those same periods. As Table 5 shows, as of December 31, 2010 the City had approved 428 out of a targeted 630 ad panels through P1 and P2, which equates to a compliance ratio of 68% for P1-P2. Therefore, even under the limited P1-P2 scenario, we believe CBS Decaux should have used a 68% compliance ratio to compute the amount due to the City.

The Contractor cited Article 4.2.9 (a) of the agreement to support the methodology for its calculation. According to this article, street furniture shall be **installed** in the quantities set forth on the PRS subject to the provisions of the agreement. Further, it states that Rollout Period I shall commence sixty (60) days after the City has approved the applications for permits for the first two rollout periods. The Contractor believes that because the City did not issue permits for any pillars, rollout Period I has yet to

commence. However, this article only discusses the anticipated installation schedule, and not MAF adjustments. As described above, Article 24.3 requires the MAF adjustment to be calculated based on the number of permits the City issues regardless of whether those furniture items were installed or not.

Further, CBS Decaux argued that the City's failure to approve requested permits, particularly by council offices' rejections of high revenue types of furniture and high revenue locations, could constitute an act of Force Majeure which would have entitled the Contractor to compensation in excess of \$8.2 million cited in our calculation. Article 24.2 also states that any MAF reduction due to Force Majeure should be calculated using the MAF adjustment described in Article 24.3, the criteria that we used for our calculation.

CITY'S HISTORICAL ACCEPTANCE OF CONTRACTOR'S METHODOLOGY

The Bureau of Street Services has historically accepted the MAF adjustment methodology as calculated by CBS Decaux. BSS representatives stated they understood and accepted the Contractor's position that the projected rollout schedule was contingent upon the City's reaching the numbers of approved permits by type of structure. BSS stated that this was a mutual understanding between the Contractor and City officials, which included the Chief Legislative Analyst and City Attorney, whose offices played key roles in negotiating the contract agreement. Our discussions with those offices during this audit confirmed that understanding. However, there is no written correspondence that memorializes this contractual understanding, nor evidence showing how the City may have considered how this interpretation would significantly reduce the MAF due to the City.

Under the contractual understanding, the program would remain in a particular phase (e.g., P1, P2, etc.) until the City had approved the required number of permits for that phase/period for all furniture types. For example, according to the PRS, there should be a total of 300 permits approved by the end of P2, as follows:

- ❖ APTs – 10 items⁵
- ❖ Transit Shelters – 100 items
- ❖ Pillars – 50 items
- ❖ Kiosks – 120 items
- ❖ Vendor and Newsstand Kiosks – 20 items

According to BSS staff, certain furniture items (e.g., pillars) generate more advertising revenue than other types of items. This was one factor considered by City staff underlying the contractual understanding with the Contractor, that the City would need to approve the required number of permits for each furniture type noted for a given period in order to "move out" of that period. Although we noted that the Contractor's advertising billings under this agreement were based on market area without respect to the specific type of furniture, BSS stated that, had the Contractor installed pillars, which

⁵ APTs do not contain advertising panels, and therefore are not considered "revenue generating".

contain bigger ad panels in their anticipated high revenue locations, CBS Decaux would have sold ad spaces for higher fees and generated increased revenues.

CBS Decaux also indicated that during contract negotiations the parties discussed that installation of pillars was essential to the economic viability of the program. For example, the Contractor stated that "a tall Pillar Ad in a dense commercial district commands more advertising revenue than a shelter ad in an outlying low population neighborhood." It appears that due to this mutual understanding, City officials have historically accepted CBS Decaux's MAF calculation, which only considers permits approved through P1-P2 up to the stated target for those periods, measured against the total permits for all furniture types that was to be installed throughout the contract term. However, none of these understandings and agreements were formally incorporated into the contract.

Citing section 4.2.9 of the contract, Installation of Street Furniture, CBS Decaux argues that P1 and P2 did not commence until the required approvals were obtained for each type of structure; yet they have voluntarily paid the MAF as if P1 and P2 had been completed despite the lack of permits for pillars and newsstands. While this section defines the periods as a schedule for furniture installation, it makes no reference to the Remedy for Delay provisions and its effect on the MAF. Rather, that section states that at the end of Rollout Period 4, Contractor and BSS shall review the number of City approvals compared to the number contemplated by the PRS, in order to establish a revised schedule.

FINANCIAL IMPACT OF THE CITY REMAINING IN P2 FOR THE CONTRACT TERM

Based on our interpretation of the "Remedy for Delay" calculations, for the period 2003 through 2011, the City lost the opportunity to receive \$8.2 million in potential revenue. Attachment III details our year-by-year computation based on the number of aggregated permitted ad panels as of December 31st of each year, the adjustment to the MAF based on our interpretation of Article 24.3 of the agreement, and the effect of the 20% of gross receipts for each year.

The City Attorney's Office stated that our interpretation of the contract for how the MAF should be calculated is a reasonable interpretation, but that there may be others. The City Attorney also stated that the MAF adjustment has been calculated in accordance with the intent of the parties to the agreement. Therefore, we acknowledge that these funds are not recoverable due to the mutual understanding between City officials and CBS Decaux.

It should also be noted that beginning in April 2008, a disagreement arose between BSS and CBS Decaux regarding the number of approved/permitted sites. In January 2009 the City claimed that it had reached P4 levels while CBS Decaux claimed it was still at P2 of the rollout schedule, since the construction permits for implementing furniture on those sites were not pursued. In March 2009, the City issued a "breach of contract" letter to CBS Decaux with regards to how it affected the MAF due to the City; however, the City informally suspended its pursuit of the matter pending the outcome of

renewed talks to craft a contract amendment. As of our audit fieldwork date, this impasse regarding the City receiving credit for P4 numbers has not yet been resolved.

Regarding the impasse, the Contractor stated that because of City delays in approving permits for pillars, it is no longer economically feasible to install pillars given the remaining number of years left in the agreement. In addition, the Contractor provided evidence showing that since 2007, there were numerous attempts to renegotiate the contract, whereby the Contractor proposed removing pillars from the agreement in exchange for other contract modifications. In a July 2010 letter, BSS notified the Contractor that it is in the best interest of the City to continue with the contract as it is currently written.

At a minimum, we believe that the "Remedy for Delay" provisions should be amended to clearly reflect the understanding of both parties with respect to the MAF adjustment. Contract renegotiation would also help resolve the current impasse between the City and the Contractor so the program can continue to move forward. If the contract is not modified, the impasse will likely continue and the City would continue to remain in P2 throughout the life of the agreement. This situation will result in an additional lost revenue opportunity that could exceed \$57 million. Because of the significance of this potential revenue loss, this matter requires immediate consideration by City officials.

Recommendation:

- 1. The City Attorney, in collaboration with the CLA and BSS, should work to renegotiate the contract to the mutual benefit of the City and CBS Decaux, and present any proposed amendments to the Mayor and Council for approval.**

SECTION II. SITE/PERMIT APPROVAL PROCESS AND PROGRAM REVIEW

SITE AND PERMIT APPROVAL PROCESS

Finding #2: The Contract's site and permit approval process is very cumbersome and has resulted in significant delays in approving the required number of permits. Consequently, the City has lost almost \$15 million in additional potential revenue.

Even though the City was expected to have approved 100% of contractual sites and ad panels by the end of Year 2 of the program, the City had only permitted furniture items with 69% of the contractual number of ad panels as of March 2011 (Year 10 of the agreement).

In order to determine how long the City was taking to approve sites/permits, and to identify where bottlenecks were occurring, we selected 30 sites for detailed review of approval timelines. Our sample was selected from a database of furniture items that were installed between 2004 and 2009, and consisted of two installed furniture items per council office. Because a significant proportion (approximately 75%) of items that had been installed was transit shelters, the sample consisted mostly of shelters. Our objective was to determine an average timeframe of how long it took each City offices/department(s) in their process to approve permits for furniture that had been installed. Therefore, our sample did not include unapproved applications or those that were never acted upon by council offices, since these did not go through the entire process. BSS believes that additional significant delays were due to the applications that were denied or never acted on by council offices. Also, in evaluating our sample results, we excluded one item (from our sample of 30) because it was for a replacement location that did not go through the entire approval process.

For each site, we obtained the date that each council office and appropriate departments approved the location for the site/permit. We also obtained the dates that the Contractor subsequently submitted design documents to the Bureau of Engineering (BOE), Bureau of Street Lighting (BSL), and the Department of Water and Power (DWP). We also recorded the date that BSS notified the adjacent property owner, the date BSS issued a notice to proceed to the Contractor, and the date that the final permit was issued for each location. We then computed how long it took each responsible party to approve the application, and the average number of days for the sample.

We found that it took the City an average of 129 days to approve sites and permits.⁶ It is not surprising that there were delays in approving permits because the Contract's approval processes are very cumbersome. Discussed below are steps the Contractor

⁶ Throughout this section of the report, in deriving averages, we used the median as opposed to the arithmetic mean. In many instances, using the arithmetic mean would skew the average because a few sites took an excessive number of days to approve.

must follow to obtain a permit to install street furniture, and how long each step took to complete based on our sample of 30 sites.

Council District Office

The site approval process begins when the Contractor develops and submits a list of proposed sites to the Councilmember(s) of the district(s) where the sites are located. A Councilmember may request the Contractor to make presentations about the proposed furniture locations to his/her office and/or to any neighborhood council, community or business group, before approving the site(s). The Councilmember may then approve the proposed site, or may request the Contractor to provide alternative site(s).

There were some considerable delays by the council offices during this process, especially during the early years of the program. For our sample of installed locations, our analysis found that council districts took an average of 28 days to approve site applications that came through their offices. Of the 30 sampled sites, 40% took 50 or more days to approve the application.

Delays also would have occurred on site applications that were denied and on those that were not acted upon by council districts. When a site is rejected by a council office, an alternative site is proposed, and the Contractor must submit a new site application which further delays the site and permit approval process. According to BSS, as of the end of November 2011, more than 15% of proposed street furniture sites submitted to council offices had never been formally approved or denied, even though very few sites were forwarded to council offices for approval since 2008.

Adjacent Property Owner Notification

Once a Councilmember approves a site, the Contractor informs BSS, and a notification is mailed to any property owners who may share a common boundary with the proposed site. If a property owner objects to the placement of a furniture item, the complaint is forwarded to the Board of Public Works for review and resolution. For our sampled sites, it took an average of 12 days from the council districts' approval dates before notifications were mailed to the property owners.

Street Furniture Task Force

If no objection is received from the property owners within 15 days, a site approval form is distributed simultaneously to task force departments to review the site(s) to ensure conformity to City codes and ordinances. The Street Furniture Task Force consists of representatives from the Bureaus of Street Services, Engineering, Street Lighting and Contract Administration, the Los Angeles Police Department, the DWP, the Department of Transportation (DOT) and the Department of City Planning (Planning). Each department reviews a site for different reasons. For example, Planning ensures that the proposed site will not violate a specific plan area, while Bureau of Street Lighting (BSL) ensures there is an accessible power source at the proposed location.

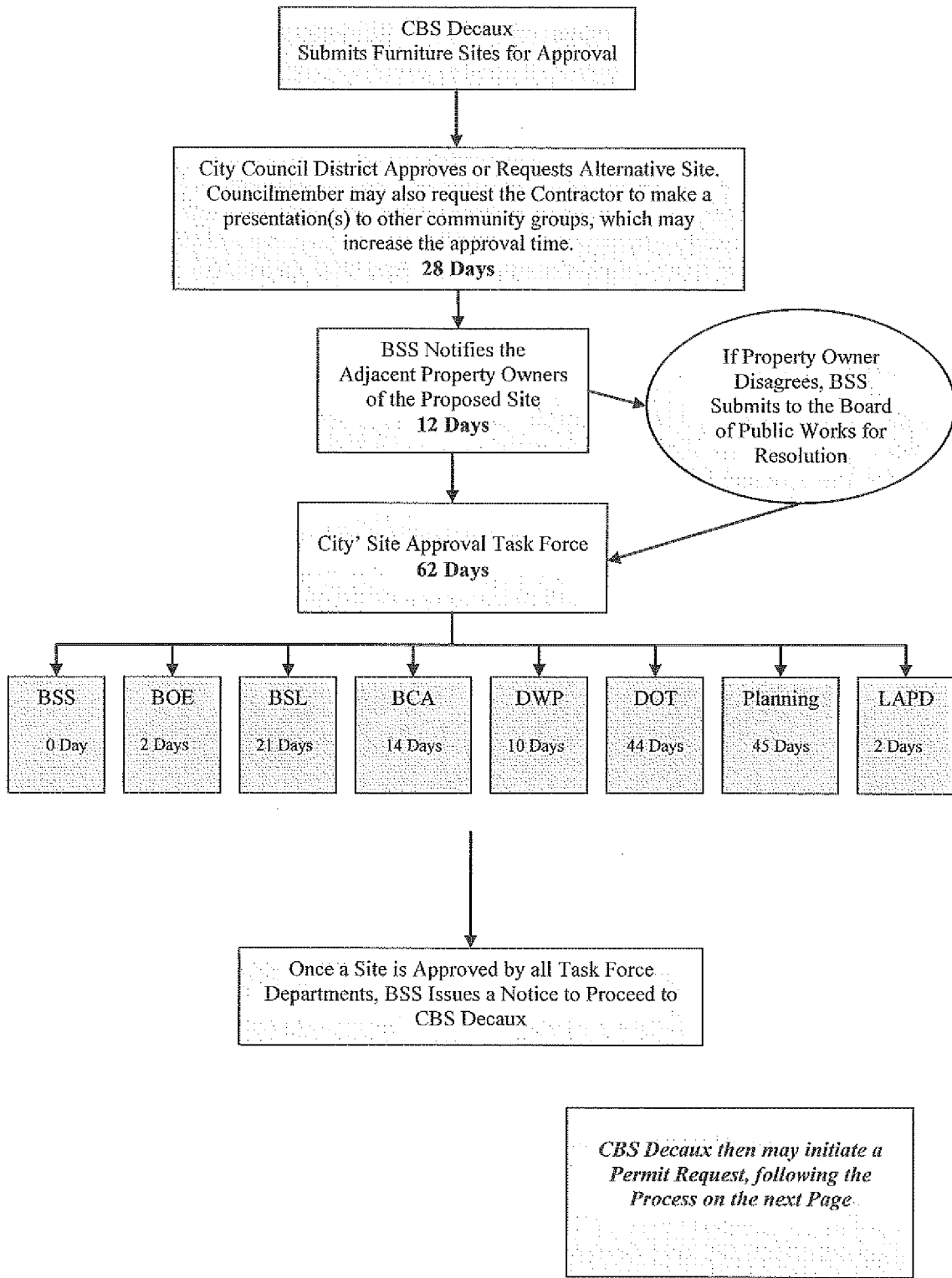
The City does not have an expedited approval process in place, and task force departments often do not prioritize approving these street furniture sites. Our sample disclosed that it took the task force an average of 62 days to approve the site. We found that two task force departments, DOT and Planning, took the longest time to approve sites. DOT took an average of 44 days, while Planning took an average of 45 days. Planning staff indicated that the delays were because site approval forms were typically sent out to field supervisors with direct knowledge of proposed individual locations. Waiting to hear back from different individuals often took some time because it was not a high priority for staff. DOT did not provide explanations for their delays. Since BSS will only move an application forward after all eight task force departments have approved a site, a delay by one department will hold up the entire process. BSS attributed delays by task force departments to the fact that dedicated resources were not allocated to these departments to accommodate the program's needs.

Final Permit Issuance

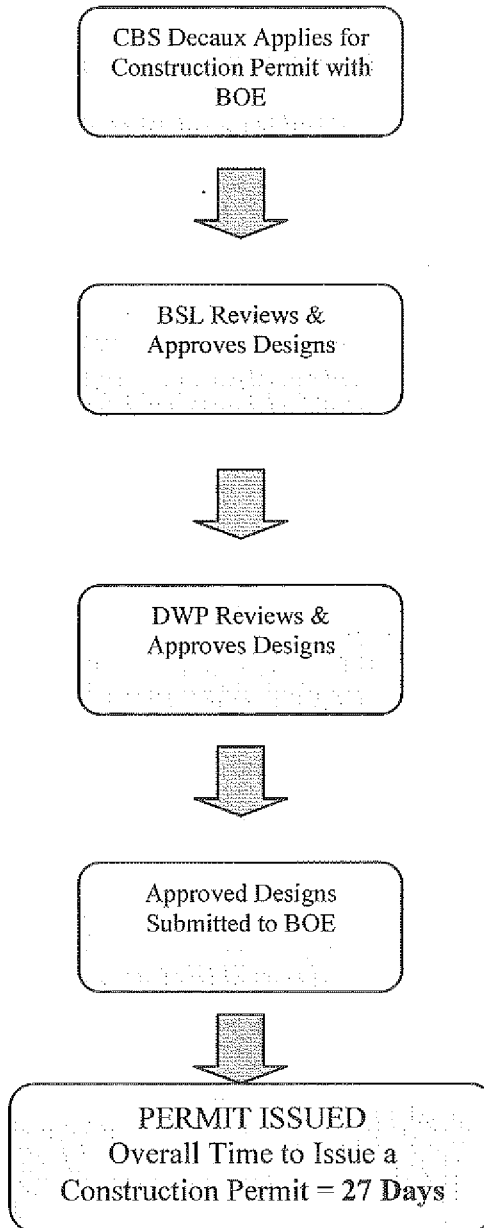
Once a site is approved by the task force, BSS issues a notice to proceed (NTP) to the Contractor. CBS Decaux then initiates a request for a final permit and submits design drawings for the specific furniture item, first to the BSL and then to DWP⁷. These two departments review the specific furniture drawings, designs, and electricity requirements. Once they have approved the particular furniture drawings, the BOE issues a construction permit. Based on our sample, the final permit process involving the three departments took an average of 27 days to complete. The diagram on the next two pages shows the entire site and permit application process.

⁷ For the sample sites reviewed, CBS Decaux took an average of 118 days between the dates it received a NTP from BSS to when it submitted engineering drawings to the BSL. We did not include this number in our computation of the total number of days it took the City to issue a permit because our objective was to determine how long City departments/offices took to process each request from the Contractor.

STREET FURNITURE SITE APPROVAL PROCESS



**FINAL PERMIT APPROVAL
AND
ISSUANCE**



Overall, our sample results show that the City took an average of 129 days (28 +12 + 62+ 27) to approve a site/permit.

Because of the City's inability to approve (or deny) a significant number of proposed sites in a timely manner, and therefore approve permits in accordance with the agreement's anticipated project rollout schedule, it is entitled to only \$38.1 million of the potential \$53 million for the first ten years of the contract. This equates to a \$14.9 million loss in potential revenue. This amount is exclusive of the \$8.2 million cited in Finding #1.

Prior Effort to Streamline the Process through Contract Amendment

It should be noted that City officials recognized a problem with the site approval and permitting delays several years ago. In 2005, BSS and the Chief Legislative Analyst (CLA) attempted to revise the permitting process for street furniture, after it was discovered that some council districts and departments were taking longer than originally anticipated to approve site requests. The CLA reported that a number of council districts did not act in a timely manner on proposed site applications submitted by the Contractor, with numerous site applications over three years old at the time of their report. The CLA's 2005 report noted that the City had issued final permits to install only 490 (24% of 2,068) items. In an attempt to minimize revenue loss, the Council directed BSS and the CLA to recommend a revised permitting process for council offices with approval rates below 75% of the applications submitted by the Contractor.

In early 2007, the CLA recommended that Council approve a contract amendment that incorporated maximum time periods by which the council offices, Contractor and BSS staff would be required to respond. For example, the revised process would have required that, within 15 days of receiving a site request, a council district must either approve the site as requested or request alternative sites and/or further presentation from the Contractor. Discussions went on, but the amendment was never approved by Council. However, these discussions appear to have helped increase the approval rate. As Table 4 shows, 86% of contractual sites (excluding APTs) had been permitted through December 31, 2010.

BSS also indicated that in 2008, it proactively enforced a 30-day response policy for task force members to approve a site. If BSS did not receive a response from a task force department after 30 days, the site is deemed approved and the process moves ahead. BSS believes this action has reduced application processing time. Nevertheless, in order to increase the City's share of revenues under this contract, the City must formally address, along with the previously discussed MAF issue, the need for improving the site and permit approval process.

Recommendation:

- 2. BSS management, the council offices, all affected departments and the Contractor should mutually develop and include a revised site approval and permit process as part of any future contract amendment. This could include limiting the number of parties involved in the approval process.**

PERIODIC PROGRAM REVIEWS

Finding #3: The City has not completed the required Year Six review that was intended to identify unanticipated problems and to develop mutually agreed upon solutions to achieve the revenue and service goals contemplated by the agreement.

Article 6 of the agreement requires that the Council, BSS and the City Attorney complete an annual review of the Contractor's compliance with maintenance standards designated in the contract.

In addition, the agreement requires that, at the end of Year Six (2008), the Council, BSS, City Attorney and Contractor review the operation of the program, taking into account the following:

- The amount of street furniture installed and the actual timetable on which permits were approved.
- The level of services which are being provided by the Contractor relative to program goals and public needs.
- The revenues generated, including the relationship of the location of ad panels and the street furniture to the amount of revenue.
- The level of maintenance relative to program goals and actual site conditions.
- The impact of personal property taxes or possessory interest taxes, if such taxes have been imposed.

The six-year review was intended to allow the City and Contractor to discuss any issues and problems that were not originally anticipated, so that both parties could mutually agree on appropriate modifications to the program in order to achieve the service and revenue goals contemplated by the agreement. The review would also allow Council to consider appropriate remedial actions.

On January 15, 2008, the Council instructed the City Attorney, BSS and the CLA to work with CBS Decaux to complete a Year Six review. However the review was never conducted. The agreement prohibits changes as a result of any review unless they are mutually agreed to by both parties in a written amendment.


In April 2008, City officials and the Contractor agreed to forgo the formal Year Six review pending their ongoing contract amendment discussions, which sought to streamline the permit approval process. However, the contract has not yet been amended, and the issues regarding site/permit approval process and the MAF have not been resolved.

BSS stated that, although neither the annual reviews nor a Year Six review were conducted, program progress, service and maintenance levels were discussed during their regular monthly meetings with the Contractor representatives. Though the program is now in its tenth year, it may still be beneficial for the City and the Contractor to conduct a formal review, and use the results to develop mutually agreed upon solutions to improve the program.

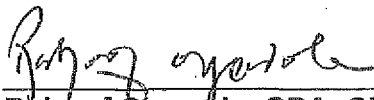
Recommendation:

3. BSS management should, in conjunction with the Contractor and other appropriate parties, initiate a comprehensive street furniture program evaluation that complies with the "Year Six review" provision of the agreement.

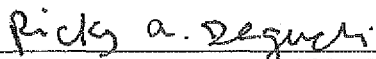
Respectfully submitted,



Eren Sanchez, CPA
Internal Auditor I



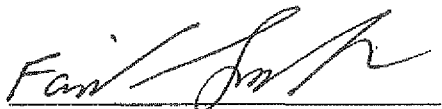
Rahoof Oyewole, CPA, CIA, CISA
Internal Auditor IV



Ricky Deguchi, CPA, CIA, CISA
Chief Internal Auditor



Siri Khalsa, CPA
Deputy Director of Auditing



Farid Saffar, CPA
Director of Auditing

December 20, 2011

**OFFICE OF THE CONTROLLER
AUDIT OF THE CITY'S STREET FURNITURE
CONTRACT WITH CBS DECAUX, LLC**

Ranking of Recommendations

Finding Number	Description of Finding	Ranking Code	Recommendations
SECTION I. MINIMUM ANNUAL FEE DUE TO THE CITY			
1.	Although the Contractor is entitled to adjust the stated minimum annual fee due to the City in the event the City delayed approving the required number of permits, in our opinion, through 2011, the City has lost the opportunity to collect an additional \$8.2 million due to the methodology used to adjust annual fees due to the City.	U	1. The City Attorney, in collaboration with the CLA and BSS, should work to renegotiate the contract to the mutual benefit of the City and CBS Decaux, and present any proposed amendments to the Mayor and Council for approval.
SECTION II. SITE/PERMIT APPROVAL PROCESS AND TIMELINE			
2.	The City's site and permit approval process is very cumbersome and has resulted in the untimely approval of the required number of permits. Consequently, the City has lost almost \$15 million in additional potential revenue.	U	2. BSS management, the council offices, all affected departments and the Contractor should mutually develop and include a revised site approval and permit process as part of any future contract amendment. This could include limiting the number of parties involved in the approval process.
3.	The City has not completed the required Year Six review that was intended to identify unanticipated problems and to develop mutually agreed upon solutions to achieve the revenue and service goals contemplated by the agreement.	N	3. BSS management should, in conjunction with the Contractor and other appropriate parties, initiate a comprehensive street furniture program evaluation that complies with the "Year Six review" provision of the agreement.

Description of Recommendation Ranking Codes

U- Urgent-The recommendation pertains to a serious or materially significant audit finding or control weakness. Due to the seriousness or significance of the matter, immediate management attention and appropriate corrective action is warranted.

N- Necessary- The recommendation pertains to a moderately significant or potentially serious audit finding or control weakness. Reasonably prompt corrective action should be taken by management to address the matter. The recommendation should be implemented within six months.

D- Desirable- The recommendation pertains to an audit finding or control weakness of relatively minor significance or concern. The timing of any corrective action is left to management's discretion.

STREET FURNITURE PROJECT ROLLOUT SCHEDULE

	PHASE I											PHASE II			
	YEAR 1					YEAR 2				CUMULATIVE TOTAL (YEARS 1 & 2)	YEAR 3	YEAR 4	YEAR 5	GRAND TOTAL	
	P1	P2	P3	P4	TOTAL	P5	P6	P7	P8						
Automatic Public Toilet (APT)	# of furniture items (1)	5	5	5	5	20	7	7	8	8	50	33	33	34	150
	# of Ad Panels		-		-	-		-		-				-	-
Transit Shelter	# of furniture items	30	70	140	160	400	215	210	230	230	1,285				1,285
	# of Ad Panels					550					1,770				1,770
Pillar	# of furniture items	25	25	-	-	50	25	25			100				100
	# of Ad Panels	100	100			200	100	100			400				400
Public Amenity Kiosks (PAK)	# of furniture items	60	60	60	60	240	65	65	65	65	500				500
	# of Ad Panels	120	120	120	120	480	130	130	130	130	1,000				1,000
Vending and Newsstand Kiosks	# of furniture items	10	10	10	10	40	15	15	15	15	100				100
	# of Ad Panels					104					260				260
Contractual Total	# of furniture items					750									2,135
	# of Ad Panels					1,334					3,430				3,430

(1) The first APT's shall be installed irrespective of when Rollout 1 commences for all other OSF.

Source: Appendix 2 of the Contract

CUMULATIVE NUMBER OF SITES AND ADVERTISING PANELS PERMITTED BY FURNITURE CATEGORY AND BY YEAR

	Shelter		PAK		Vending Kiosk		Pillar (1)		Total Permitted as of Dec 31st of Each Year		Contract Requirement (Attachment I)		Ad Panels- Compliance % as of Dec 31st of Each Year
	Sites	Ad panels	Sites	Ad panels	Sites	Ad panels	Sites	Ad panels	Sites	Ad panels	Sites	Ad panels	
	A	A1	B	B1	C	C1	D	D1	E	E1	F	F1	G=(E1/F1)%
2002	0	0	0	0	0	0	0	0	0	0	730	1334	0.0%
2003	152	262	60	97	34	34	0	0	246	393	1985	3430	11.5%
2004	315	438	86	124	37	37	0	0	438	599	1985	3430	17.5%
2005	932	1284	226	410	42	42	0	0	1200	1736	1985	3430	50.6%
2006	1075	1390	254	449	44	44	0	0	1373	1883	1985	3430	54.9%
2007	1083	1446	254	445	45	45	0	0	1382	1936	1985	3430	56.4%
2008	1205	1588	338	573	45	45	0	0	1588	2206	1985	3430	64.3%
2009	1224	1594	431	727	50	50	0	0	1705	2371	1985	3430	69.1%
2010	1223	1592	431	728	50	50	0	0	1704	2370	1985	3430	69.1%

A, B,C, & D represent the cumulative number of sites permitted for shelters, PAKs, vending kiosks and pillars at the end of each year.

A1, B1,C1, & D1 represent the corresponding cumulative number of ad panels permitted for shelters, PAKs, vending kiosks and pillars at the end of each year.

E - Aggregate total number of sites permitted for all furniture types at the end of each year.

E1 - Aggregate total number of ad panels permitted for all furniture types at the end of each year. This number is used to compute the City's compliance ratio in G.

F - Aggregate total number of contractual ad panels at the end of each year. The contract's first full year was 2002.

F1 - Aggregate contractual total number of ad panels at the end of each year. This number is used as a denominator to compute the City's compliance ratio in G.

G - City's ad panel compliance % for each year based on E1 and F1. This % is calculated by dividing E1 by F1. This % is used in Column D in Attachment III.

(1) According to BSS, as of April 2008, the City had approved 80 Pillar sites and issued a notice to proceed to CBS Decaux to request construction permits for those sites. However, CBS Decaux has elected not to request permits for these items. We did not credit the City with any pillars on this schedule because Article 24.3 of the agreement requires that MAF adjustments be made based on the number of permitted items.

CALCULATION OF ANNUAL FEE DUE TO THE CITY FROM THE STREET FURNITURE PROGRAM OPERATED BY CBS DECAUX

	Contractual MAF(Assuming 100% Compliance)	Guaranteed Amt	Amt Subject to Delay Adjustment (MAF - Guaranteed Amt)	Compliance % Based on Ads Permitted by Dec 31st of Prior Year	City's Portion of Adjustment Based on Compliance %	APT Connection Costs Claimed by CBS Decaux	Advance Annual Fee Due to the City (January Payment)	Gross Revenue Reported by CBS Decaux	20% of Revenue	Amount Paid	Potential Loss
	A	B	C (A-B)	D	E (C*D)	F	G {(B+E) - F}	H	I (20% of H)	J	K (G or I - J)
Jan-11	\$ 7,500,000	\$ 2,000,000	\$ 5,500,000	69.1%	\$ 3,800,500	\$ 111,307	\$ 5,689,193			\$ 2,574,990	\$ 3,114,203
Jan-10	\$ 7,500,000	\$ 2,000,000	\$ 5,500,000	69.1%	\$ 3,800,500	\$ -	\$ 5,800,500	\$ 17,495,291	\$ 3,499,058	\$ 3,495,058	\$ 2,305,442
Jan-09	\$ 6,000,000	\$ 2,000,000	\$ 4,000,000	64.3%	\$ 2,572,000	\$ 376,473	\$ 4,195,527	\$ 15,929,936	\$ 3,185,987	\$ 2,809,514	\$ 1,386,013
Jan-08	\$ 6,000,000	\$ 2,000,000	\$ 4,000,000	56.4%	\$ 2,256,000	\$ -	\$ 4,256,000	\$ 20,580,992	\$ 4,116,198	\$ 4,116,198	\$ 139,802
Jan-07	\$ 6,000,000	\$ 2,000,000	\$ 4,000,000	54.9%	\$ 2,196,000	\$ 152,258	\$ 4,043,742	\$ 18,128,783	\$ 3,625,757	\$ 3,473,499	\$ 570,243
Jan-06	\$ 6,000,000	\$ 2,000,000	\$ 4,000,000	50.6%	\$ 2,024,000	\$ -	\$ 4,024,000	\$ 15,270,891	\$ 3,054,178	\$ 3,054,178	\$ 969,822
Jan-05	\$ 5,000,000	\$ 2,000,000	\$ 3,000,000	17.5%	\$ 525,000	\$ -	\$ 2,525,000	\$ 13,490,896	\$ 2,698,179	\$ 2,698,179	\$ -
Jan-04	\$ 3,000,000	\$ 2,000,000	\$ 1,000,000	11.5%	\$ 115,000	\$ -	\$ 2,115,000	\$ 11,813,797	\$ 2,362,759	\$ 2,389,169	\$ (26,410)
Jan-03	\$ 3,000,000	\$ 2,000,000	\$ 1,000,000	0.0%	\$ -	\$ -	\$ 2,000,000	\$ 10,345,830	\$ 2,069,166	\$ 2,290,000	\$ (220,834)
Jan-02	\$ 3,000,000	\$ 3,000,000	\$ -		\$ -	\$ -	\$ 3,000,000	\$ 7,463,330	\$ 1,492,666	\$ 3,000,000	\$ -
	\$ 53,000,000	\$ 21,000,000	\$ 32,000,000		\$ 17,289,000	\$ 640,038	\$ 37,648,962	\$ 130,519,746		\$ 29,900,786	\$ 8,238,281

A - This is the stated minimum annual fee in Article 4.5 of the agreement. However, the City is only entitled to this amount if it approves 100% of permits in accordance with the program rollout schedule.

B - This amount is guaranteed regardless of how many permits the City approved.

C - This is the amount of A in excess of B that is subject to adjustment based on the number of permits the City approved.

D - This represents the City's compliance ratio based on the number of ad panels permitted vis-a-vis the number that should have been permitted by December 31st of the concluding year.

E - This represents the amount of C that the City is entitled to based on compliance ratio in D.

F - The contract provides that the City pays for APT connection costs in excess of a certain threshold. CBS claimed these amounts.

G - Total due to the City in January of the new year based on B, E and F.

H - Gross revenue reported by the contractor at the end of the year.

I - 20% of gross revenue reported in H. This amount is compared to amount in G. The City is entitled to the higher amount for the year.

J - CBS Decaux paid the City these amounts. We excluded an additional \$327K escrow payment made by the contractor because escrow provides the City an opportunity to earn some of the lost revenue from the prior year if it approves more permits by April 30th. However, escrow does not affect regular amount due.

K - This amount, calculated based on G, I and J, represents the potential revenue loss to the City through January 2011 based on our interpretation of the remedy for delay provisions of the agreement.