AUDIT REPORT

CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
BUREAU OF FINANCIAL AUDIT
WILLIAM C. THOMPSON, JR., COMPTROLLER

Audit Report on the Financial Practices of the New York City Marketing Development Corporation

FM05-121A

April 10, 2006

THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
1 CENTRE STREET
NEW YORK, N.Y. 10007-2341

WILLIAM C. THOMPSON, JR.
COMPTROLLER

To the Citizens of the City of New York

Ladies and Gentlemen:

In accordance with the responsibilities of the Comptroller contained in Chapter 5, § 93, of the New York City Charter, my office conducted an audit to determine whether the New York City Marketing Development Corporation (NYC Marketing) accurately reported revenues and expenses and remitted excess revenue to the City as required with the terms of its agreement with New York City.

Under the City contract, NYC Marketing is to prepare its program budget and financial plan in accordance with procedures and methodology determined by the Mayor's Office of Management and Budget (OMB) so that financial operations can be monitored. The contract also states that NYC Marketing may retain revenues in an amount necessary to meet its cash operating requirements; any excess revenue is to be paid to the City.

The results of our audit, which are presented in this report, have been discussed with officials of NYC Marketing and the Mayor's Office of Management and Budget, and their comments have been considered in preparing this report. Their complete written responses are attached to this report.

I trust that this report contains information that is of interest to you. If you have any questions concerning this report, please e-mail my audit bureau at audit@Comptroller.nyc.gov or telephone my office at 212-669-3747.

Very truly yours,

William C. Thompson, Jr.

WCT/fh

Report: **FM05-121A**
Filed: **April 10, 2006**

Table of Contents

The City of New York
Office of the Comptroller
Bureau of Financial Audit

Audit Report on the Financial Practices of the New York City Marketing Development Corporation

FM05-121A

AUDIT REPORT IN BRIEF

In March 2004, the City entered into a contract to retain New York City Marketing Development Corporation (NYC Marketing) as the City's exclusive marketing and licensing consultant. NYC Marketing is to assist the City in developing, enhancing, and protecting City trademarks, patents, copyrights, and other City assets in order to generate revenues and other resources for the City. NYC Marketing seeks to gain new revenue for the City, to support City agencies and initiatives, and to encourage City growth through economic development and tourism.

Under the City contract, NYC Marketing is to prepare its program budget and financial plan in accordance with procedures and methodology determined by the Mayor's Office of Management and Budget (OMB) so that financial operations can be monitored. The contract also states that NYC Marketing may retain revenues in an amount necessary to meet its cash operating requirements; any excess revenue is to be paid to the City.

This audit determined whether NYC Marketing accurately reported its revenue and expenses, remitted excess revenue to the City in accordance with the City contract, and complied with certain significant provisions of the contract.

Audit Findings and Conclusions

NYC Marketing accurately reported revenue and expenses, and its expenses were valid. However, the City has yet to establish formal procedures and a methodology that would allow it to effectively monitor NYC Marketing's financial activities to ensure that funds in excess of NYC Marketing's cash operating requirements are paid to the City. In fact, for the fiscal year ending June 30, 2005, NYC Marketing reported a cash balance of approximately $1.6 million, but did not remit a portion of the excess cash to the City.

Further, NYC Marketing underpaid the City its full share of the commission from the sale of Snapple beverages sold on City property. Consequently, NYC Marketing owes the City $235,834 in additional commission payments.

Audit Recommendations

To address these issues, we recommend that NYC Marketing:

- Pay the City the full Snapple commission received as of June 30, 2005, (less the seven percent paid to Octagon, Inc., a company retained to develop a vending machine program) and remit the additional commission of $235,834 due the City.
- Pay all subsequent commissions it receives from Snapple to the City.

We recommend that OMB:

- Establish written procedures and a methodology that would enable it to closely monitor NYC Marketing's financial activities to ensure that funds in excess of NYC Marketing's cash operating requirements are paid to the City.
- Develop financial benchmarks to evaluate NYC Marketing's budgetary needs and to ensure that the City receives a portion of the revenues generated by NYC Marketing activities.
- Ensure that NYC Marketing addresses the report's finding and implements the report's recommendation.

INTRODUCTION

Background

NYC Marketing is a local development corporation established by the City of New York in July 2003, pursuant to §1411 of the Not-For-Profit Corporation Law of the State of New York. In March 2004, the City entered into a contract to retain NYC Marketing as the City's exclusive marketing and licensing consultant. NYC Marketing is to assist the City in developing, enhancing, and protecting City trademarks, patents, copyrights, and other City assets in order to generate revenues and other resources for the City.

NYC Marketing generates revenue by entering into agreements with public and private entities seeking to use the City's image and vast resources for various marketing purposes. By developing these partnerships, NYC Marketing seeks to gain new revenue for the City, to support City agencies and City initiatives and to encourage City growth through economic development and tourism. During the period July 10, 2003, to June 30, 2005, NYC Marketing received a loan of approximately $1.2 million from the New York City Economic Development Corporation to cover expenses associated with the development and organization of NYC Marketing; it generated approximately $8.4 million in revenue and spent approximately $8.3 million in operating expenses.

Under the City contract, NYC Marketing is to prepare its program budget and financial plan in accordance with procedures and methodology determined by the Mayor's Office of Management and Budget (OMB) so that financial operations can be monitored. The contract also states that NYC Marketing may retain revenues in an amount necessary to meet its cash operating requirements; any excess revenue is to be paid to the City.

For the period April 23, 2004, to June 30, 2005, NYC Marketing entered into various marketing and licensing agreements (some are multi-year agreements) with a potential value of approximately $159.1 million.[1] Of this amount, approximately $76.1 million consists of cash payments, including $36 million in commissions from the sale of Snapple products on City property, and $83 million in other benefits, such as media and promotional advertising. See Table I, following, for a breakdown of the potential revenue and other benefits negotiated by NYC Marketing on behalf of the City.

[1] Subsequent to the receipt of NYC Marketing's response to this audit and before the issuance of the final audit report, NYC Marketing scheduled a public hearing before the Franchise and Concession Review Committee (FCRC) to request an amendment to its agreement with Snapple Beverage Corporation. The Amendment being submitted to the FCRC for approval includes an agreement by Snapple to reduce the yearly case sale goal, which will result in a revised payment schedule for NYC Marketing. Consequently, the City will receive approximately $33 million in potential revenue and other benefits.

Table I

NYC Marketing Agreements
Revenue and Other Benefits
April 23, 2004, to June 30, 2005

Company	***Terms***	***Cash***	***Non-Cash Benefits (Marketing Initiatives and Media) ****	***Total Anticipated Cash and Non-Cash Benefits Over the Contract term***
Snapple, Inc.- Marketing Initiatives**	5 Yrs	$30,000,000	$60,000,000	$90,000,000
Snapple, Inc.- Vending Commissions**	5 Yrs	$36,000,000	$0	$36,000,000
Octagon, Inc.	5 Yrs	$1,185,000	$0	$1,185,000
The History Channel	4 Yrs	$3,500,000	$16,000,000	$19,500,000
Chevrolet - General Motors	1 Yr	$2,450,000	$0	$2,450,000
Universal Studios	1 Yr	$3,000,000	$7,000,000	$10,000,000
Total Over 5 Years		$76,135,000	$83,000,000	$159,135,000

*Marketing Initiatives and Media consist of non-cash benefits received in addition to cash over the contract term and include advertising, communications, broadcasting airtime, DVD content, and other promotional benefits.
** Both the cash value and non-cash benefits are estimates contemplated in the contract; however, actual amounts are based solely on actual vending sales over the contract term.

Objectives

The objectives of this audit were to determine whether NYC Marketing:

- accurately reported revenue and expenses and remitted excess revenue to the City as required by the City agreement; and
- expenses were valid (i.e., for proper business purposes).

Scope and Methodology

The scope of this audit covered the period July 10, 2003, to June 30, 2005. To achieve our audit objectives, we reviewed and abstracted the relevant terms and conditions of the contract between the City of New York and NYC Marketing. In addition, we interviewed NYC Marketing officials, conducted a walk-through of NYC Marketing operations, and reviewed accounting policies and procedures to gain an understanding of NYC Marketing's operating activities, the controls over its revenue, and its expense reporting processes. We also interviewed officials from the New York City Economic Development Corporation to understand their involvement in the start-up of NYC Marketing, and with officials from OMB to gain an understanding of their role in overseeing the financial activities of NYC Marketing.

To determine whether the revenue and expense amounts were valid (i.e., for proper business purposes) and accurately reported, we reviewed NYC Marketing financial records and traced the financial information from the general ledger to the underlying source documents (i.e., invoices, cancelled checks, and payment vouchers). To determine the accuracy and reliability of the amounts reported on NYC Marketing's financial statements, we traced the recorded revenue and expense amounts from the general ledger to the trial balance and then to the financial statements.

To determine the reliability of the NYC Marketing's computerized accounting system (Fundware), we reviewed revenue and expense transactions and traced the information from the sources documents (i.e., invoices, cancelled checks, and payment vouchers) to the computerized reports for accuracy and consistency.

For our test of Personal Service expenses, we judgmentally selected six Payroll Reports (July 25, 2003, October 3, 2003, June 11, 2004, June 25, 2004, December 24, 2004, and February 18, 2005). July 25, 2003, was selected because it was the first pay period of NYC Marketing. The remaining five pay periods were selected because they included a significant change in the number of personnel and/or payroll costs covered during our audit period. We then traced the amounts from the Payroll Reports to the each employee's personnel file to determine whether payroll expenses were appropriate and accurately reported. The six payroll periods selected represent 14 percent, or $374,399, of the total of $2.7 million in Personal Service expenses reported during the period July 10, 2003, to February, 28, 2005.

For our test of Other Than Personal Service expenses, we selected all transactions above $2,500, representing 92 percent, or $2.8 million, of the total $3.1 million in expenses reported from July 10, 2003, to February 28, 2005, and traced the amounts recorded in the general ledger to the underling source documents (i.e., invoices and payment vouchers). We also determined whether credit card charges were properly authorized and related to organization purposes.

The results of the above-noted tests of Personal Service and Other Than Personal Service expenses, while not projected to the various populations from which they were drawn, provided a reasonable basis for us to satisfy our audit objectives.

To determine whether NYC Marketing reported all its revenue from sponsorship, marketing, and licensing agreements, we reviewed each agreement and abstracted the relevant terms and conditions, identified all gross revenue, and traced reported sponsorship, marketing, and license revenue to the amounts posted in the general ledger.

To determine whether NYC Marketing accurately paid commissions to the City, we reviewed the financial terms of the Concession Permit between the City's Department of Citywide Administrative Services (DCAS) and NYC Marketing and applicable sections in the contract between the City and NYC Marketing as they relate to the sale of non-carbonated beverages sold in City agencies and on other, City-controlled properties. For the audit period, we traced reported commissions to the amounts posted on NYC Marketing's general ledger to determine whether the correct amounts were paid to the City.

This audit was conducted in accordance with generally accepted government auditing standards (GAGAS) and included tests of the records and other auditing procedures considered necessary. This audit was performed in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

Discussion of Audit Results

The matters covered in this report were discussed with NYC Marketing and OMB officials during and at the conclusion of this audit. A preliminary draft report was sent to these officials and discussed at an exit conference held on February 3, 2006. On February 13, 2006, we submitted a draft report to NYC Marketing and OMB officials with a request for comments. We received written responses from OMB officials on February 24, 2006, and from NYC Marketing officials on February 27, 2006.

In their responses, NYC Marketing and OMB disagreed with the report's findings that the City has yet to establish formal procedures and a methodology that would allow it to effectively monitor NYC Marketing's financial activities. They also disagreed that the City was underpaid its full share of vending commissions. NYC Marketing stated that its "financial operations have been and will continue to be regularly monitored by the City's Budget Office through formal procedures" and that it "distributes vending commissions appropriately." OMB stated that it believes it "has clearly explained to the audit staff the consistent practices which it employs in ensuring the transparency and accuracy of MDC's [Marketing Development Corporation's] financial activities, and in ensuring that funds in excess of NYC Marketing's cash operating requirements are paid to the City."

In its response, OMB acknowledged that it does not have written procedures for monitoring NYC Marketing's financial activities. Nevertheless, OMB stated that it relies "on common practiced methods for financial analysis including human interaction to carry out its mission responsibly and effectively." OMB further stated that "it is prudent management policy that the Corporation always retains sufficient cash to meet one to three months' worth of operating expenses."

NYC Marketing was conceived as a way to generate revenue from public and private entities seeking to use the City's image for marketing purposes. Nevertheless, there is a need to develop and implement procedures and a methodology to ensure that a realistic portion of the revenues generated by NYC Marketing are paid to the City. This will become a paramount concern in the coming years as NYC Marketing expects to receive approximately $76 million in cash benefits from agreements it currently has with Snapple, Inc., and with other entities. One such procedure could be to stipulate a specific percentage of revenue for each marketing venture that would be allocated to the City. Alternatively, OMB could establish a threshold amount in the budget, above which all further revenues would be remitted to the City. In fact, this type of benchmark is included in the City's contract with the Economic Development Corporation (EDC), which requires EDC to remit payment to the City if its current fund balance exceeds a specific threshold amount.

In regard to the underpayment of vending commissions to the City, NYC Marketing was unable to provide us with any written distribution policy. Not only is this payment structure not memorialized under any agreements among the City, Snapple, or NYC Marketing, it is also arbitrary and self-serving. Since the Snapple agreement provides for commission payments to be made to NYC Marketing on behalf of the City, NYC Marketing should remit to the City all commissions it receives from Snapple, less the seven percent due Octagon.

The specific issues raised by NYC Marketing and OMB and our responses are included within the respective sections of this report. The full text of the responses received from NYC Marketing and OMB are included as addenda to this report.

FINDINGS

NYC Marketing accurately reported its revenues and expenses, and its expenses were valid. However, the City has yet to establish formal procedures and a methodology that would allow it to closely monitor NYC Marketing's financial activities to ensure that funds in excess of NYC Marketing's cash operating requirements are paid to the City. In fact, for the fiscal year ending 2005, NYC Marketing reported a cash balance of approximately $1.6 million, but—with the exception of certain commission payments as discussed below—was not directed by the City to remit a portion of the excess cash to the City.

Further, NYC Marketing underpaid the City its full share of the commission from the sale of Snapple beverages sold on City property. Consequently, NYC Marketing owes the City $235,834 in additional commission payments.

These matters are discussed in the following sections of the report.

Inadequate Procedures to Monitor
NYC Marketing's Financial Operation

OMB has not established formal procedures and a methodology that would allow it to closely monitor NYC Marketing's financial activities to ensure that funds in excess of NYC Marketing's cash operating requirements are paid to the City. According to the City contract, NYC Marketing is to prepare a program budget and financial plan in accordance with procedures and methodology determined by the Director of OMB. The contract also requires that NYC Marketing pay to the City, from time to time as the City may direct, revenues in excess of the amount needed to meet its fiscal year cash requirements.

For the period July 10, 2003, to June 30, 2005, NYC Marketing had approximately $9.6 million available to fund its operation and expended approximately $8.3 million. Moreover, NYC Marketing reported an ending Fiscal Year 2005 cash surplus of approximately $1.6 million. However, NYC Marketing was not directed by OMB to make any payment to the City, but was permitted to retain the excess cash to use during Fiscal Year 2006.

Our review of NYC Marketing's 2006 financial records noted that NYC Marketing had anticipated revenue of approximately $2.1 million and expenses of approximately $2.3 million during the first quarter of 2006. If established formal procedures and a methodology were used to review NYC Marketing financial activities, a determination could have been made that NYC Marketing did not need to retain all of the excess cash from 2005 to meet its 2006 cash requirements.

NYC Marketing was created to generate additional revenue and resources for the City. By not formalizing procedures and a methodology, the City has failed to establish effective controls that would allow closer scrutiny of NYC Marketing's cash position and operating needs. The absence of formal procedures and methodology constitutes a lack of effective oversight that would provide proper accountability of City funds.

NYC Marketing Response: "NYC Marketing has an agreement with the City which clearly articulates how the Corporation must operate. The agreement is submitted, approved and registered by the Comptroller annually. As you know, it provides for, among other things, regular financial reporting and correspondence with OMB ensuring their full and complete oversight. NYC Marketing has strictly complied with these provisions since its inception.

"In addition to adhering to the policies in our agreement, NYC Marketing meets with OMB on an ongoing basis to review our progress and business plans in order to further define our business strategy and the oversight of our operations."

Auditor Comment: The primary purpose for which NYC Marketing was created was to generate revenue for the City by tapping into the City's vast marketing potential. Of the $9.6 million, NYC Marketing had available in Fiscal Year 2005, all but $1.6 million was expended to fund NYC Marketing operations. Over the next four years, as reported in this report, NYC Marketing expects to receive approximately $76 million from various sources (i.e., Snapple, Octagon, etc.). Therefore, while we agree that NYC Marketing complied with the agreement's financial reporting requirements, there is a need for formal procedures and financial benchmarks to ensure that the City will receive financial benefits from revenue that NYC Marketing receives in the future.

NYC Marketing Underpaid Commissions to the City

NYC Marketing did not fully compensate the City from the sale of Snapple beverages sold on City property. Consequently, NYC Marketing owes the City $235,834 in additional commission payments. Based on the terms of the Snapple agreement, NYC Marketing is to receive, on behalf of the City, a 30 percent commission from the retail sale of Snapple beverages sold on City property. From this amount, NYC Marketing must pay a seven percent commission to Octagon Inc., in exchange for Octagon's services in developing a vending machine program for the City. The remaining balance of the total sales commission should be remitted to the City, which would in turn credit appropriate portions to City agencies and other City properties with Snapple vending machines. However, our review of NYC Marketing's financial reports found that from April 23, 2004, to June 30, 2005, NYC Marketing received $507,171 in commissions from Snapple, paid $35,502 (seven percent) to Octagon, and paid the City $235,835. See Table II below for a breakdown of the Snapple commission.

Table II

Snapple Commission Received and
Disbursed by NYC Marketing
April 23, 2004, to June 30, 2005

Description	Amount
Sales Commission from Snapple	**$507,171**
Less:	
7 % Commission Paid to Octagon	($35,502)
Balance	**$471,669**
Commission Paid to City	$235,835
Amount Retained by NYC Marketing	$235,834

The Snapple agreement clearly states that NYC Marketing will receive the commission from Snapple "on behalf of the City." However, according to NYC Marketing officials, once a payment of seven percent is paid to Octagon, the remaining amount is divided evenly between NYC Marketing and the City. This payment structure was not established under any agreements among the City, Snapple, or NYC Marketing. This method of compensation was determined by NYC Marketing and is arbitrary and self-serving. Since the Snapple agreement provides for commission payments to be made to the City, NYC Marketing should remit to the City all commissions it receives from Snapple, less the seven percent due Octagon.

NYC Marketing Response: "Working together with input from City Agencies and OMB, NYC Marketing created a policy for the distribution of half of the vending commissions. This distribution policy, adopted by OMB, sought to replace previous vending revenue and provide an ongoing incentive for City agencies. This policy strictly adheres to NYC Marketing's agreement with the City."

Auditor Comment**:** We disagree. The agreement does not permit NYC Marketing to create its own "policy" for distributing vending commissions. As stated above, the Snapple agreement clearly states that NYC Marketing will receive the commission from Snapple "on behalf of the City." Therefore, NYC Marketing should immediately remit all funds obtained from vending commissions.

RECOMMENDATIONS

NYC Marketing should:

1. Pay the City the full Snapple commission received as of June 30, 2005, (less the seven percent paid to Octagon) and remit the additional commission of $235,834 due the City.

***NYC Marketing Response:* "**NYC Marketing respectfully disagrees with this recommendation and will continue with its current distribution policy."

2. Pay all subsequent commissions it receives from Snapple to the City.

***NYC Marketing Response:* "**NYC Marketing respectfully disagrees with this recommendation and will continue with its current distribution policy."

Auditor Comment: As previously noted, the Snapple agreement clearly states that NYC Marketing will receive the commission from Snapple "on behalf of the City." Moreover, the agreement does not permit NYC Marketing to make its own policy for distributing vending commissions. Therefore, NYC Marketing's "current distribution policy" is not only arbitrary, it is clearly unauthorized. Accordingly, NYC Marketing should reconsider its position with regard to Recommendations #1 and #2 and remit the additional $235,834 commission to the City.

OMB should:

3. Establish written procedures and a methodology that would enable it to closely monitor NYC Marketing's financial activities to ensure that funds in excess of NYC Marketing's cash operating requirements are paid to the City.

OMB Response: "Although OMB may issue written directives and enter into written agreements that provide for specific financial reporting, OMB does not have written procedures for monitoring financial activities. OMB routinely relies on common practiced methods for financial analysis including human interaction to carry out its mission responsibly and effectively.

"At the beginning of each fiscal year MDC submits to OMB a preliminary budget for analysis and approval. OMB is further provided, on a quarterly basis, current and projected revenues, expenses and cash position which are subject to a careful review by assigned staff and compared against adopted budget. OMB and MDC further engage in on-going dialogue in order to identify circumstances that could significantly alter the approved budget. Given that MDC is a new and novel enterprise, OMB has determined that careful long-term cash planning is crucial. Until such time as MDC's operations become consistent and predictable, it is prudent management policy that the Corporation always retain sufficient cash to meet one to three months' worth of operating expenses.

"OMB is very cautious in determining when and if MDC is in a position to remit monies to the City. The audit report claims that at the end of FY 2005 the Corporation held cash of $1.6 million. However the report fails to correctly clarify that this cash balance was not a result of MDC's operating activities from fiscal year, but was mostly attributable to a $1.2 million loan provided by the NYC Economic Development Corporation in FY 2004. In FY 2005 MDC remitted a payment to this entity in the amount of $103,258 and has, since then, been making consistent monthly payments towards the expiration of this loan—currently anticipated for the end of this fiscal year. Based on discussions with MDC and careful evaluation of its operations, it became apparent that MDC expenses in the beginning months of FY 2006 would exceed its revenues, thus precluding it from remitting monies to the City. In fact, MDC's cash balance at the end of FY 2006's first quarter had dropped to $361,244."

Auditor Comment: OMB officials stated that "OMB has determined that careful long-term cash planning is crucial," and that "it is prudent management policy that the Corporation always retain sufficient cash to meet one to three months' worth of operating expenses." We believe that these are the types of practices that should be the basis for establishing formal written policies and procedures to monitor NYC Marketing's financial activities. In fact, contract agreement §3.04(b) stipulates that "the Corporation shall prepare a financial plan *in accordance with procedures and methodology determined by the Director of Management and Budget*." (Emphasis added.) Implementing formal procedures is an important internal control to ensure that all funds that exceed NYC Marketing's operational needs are paid to the City. The lack of such procedures makes the process by which funds are remitted to the City arbitrary.

OMB asserts that NYC Marketing's ending cash balance for Fiscal Year 2005 was mostly attributable to a $1.2 million loan provided by the NYC Economic Development Corporation. However, the "loan" was never recorded as cash on NYC Marketing's financial statements. Instead, the loan was only recorded as a current liability on NYC Marketing financial statements. Therefore, this loan did not impact NYC Marketing's fiscal year ending cash balance.

4. Develop financial benchmarks to evaluate NYC Marketing's budgetary needs and to ensure that the City receives a portion of the revenues generated by NYC Marketing activities.

OMB Response: "Since MDC began its operations in July of FY 2004, OMB has played an active role in the development, approval and timely oversight of its budget. In this effort, OMB employs the same principles and practices it undertakes in oversight of other agencies and/or covered organizations. OMB engages in standard and consistent methods when evaluating the financial activities of MDC and makes use of any resource necessary to ensure that the objectives set forth in the City contract are fully complied with. The

Corporation’s activities will continue to be subject to OMB’s careful scrutiny to ensure the appropriateness and timely remittal of revenues to the City.”

Auditor Comment: OMB officials assert that “OMB employs the same principles and practices it undertakes in oversight of other agencies. . . . OMB engages in standard and consistent methods when evaluating the financial activities of MDC.” While these principles and practices may be sufficient when evaluating the financial activities of City agencies, we do not believe they are adequate as far as NYC Marketing is concerned.

NYC Marketing was conceived as a way to generate revenue from public and private entities seeking to use the City’s image for marketing purposes while operating free of the restrictions imposed upon municipal agencies. Because of the limited oversight of NYC Marketing, there is a greater need for the development of creative financial benchmarks in determining a realistic budget for NYC Marketing to accomplish its mission rather than the application of standard OMB practices. One such benchmark could be to stipulate for each marketing venture a specific percentage of revenue that would be allocated to the City. Alternatively, the City could require NYC Marketing to include a threshold amount in its budget above which all further revenues would be remitted to the City. In fact, this type of benchmark exists with respect to the City’s contract with EDC, which requires EDC to remit payment to the City if its current fund balance exceeds a specific threshold amount. Therefore, the City needs to develop the type of financial benchmarks that will ensure that the City receives an adequate portion of revenues generated by NYC Marketing activities. In addition, the City must include the necessary provisions, within its agreement with NYC Marketing, requiring NYC Marketing to adopt these financial benchmarks in preparing its annual budget.

5. Ensure that NYC Marketing addresses the report’s finding and implements the report’s recommendation.

OMB Response: “OMB will continue to apply its experience and judgment in ensuring that MDC’s budget is leveraged to yield the most benefit to the Corporation and the City.”

Auditor Comment: As discussed in this report, the need for formal procedures will become even more crucial in the coming years, as NYC Marketing’s potential for generating revenue for the City continues to grow. Therefore, we strongly urge OMB to ensure that formal procedures are developed so that NYC Marketing’s financial activities can be closely monitored.

NYC MARKETING
New York City Marketing Development Corporation

February 27, 2006

Gayle M. Horwitz
Deputy Comptroller and Chief of Staff
Office of the Comptroller
One Centre Street
New York, New York 10007

Dear Ms. Horwitz,

We appreciate the opportunity to respond to the February 13, 2006 draft audit of NYC Marketing's financial and operating practices.

We are pleased with your conclusion that all of NYC Marketing's expenses were valid and that we accurately reported our revenue and our expenses. As we enter our third year of operations, we are very proud of our progress and appreciate the time your staff spent with our group. However, we respectfully disagree with your two condensed findings.

NYC Marketing's financial operations have been and will continue to be regularly monitored by the City's Budget Office through formal procedures. These procedures are clearly articulated in our agreement with the City which the Comptroller has approved and registered. NYC Marketing closely follows these procedures. Additionally, while the audit correctly noted that NYC Marketing had a cash balance of $1.6 million at the end of the audit period, it failed to acknowledge that NYC Marketing also had $1.7 million in outstanding bills immediately coming due. It is reasonable and prudent to retain enough cash to fund our ongoing operations. All of this information was provided to your staff during the year-long audit and should be fully covered in your final report.

NYC Marketing distributes vending commissions appropriately. Together with City agencies and OMB, NYC Marketing created a policy to distribute half of the vending commissions to the City's budget office. This distribution policy, adopted by OMB, replaces previous vending revenue and provides an ongoing incentive for City agencies. This policy strictly adheres to our agreement with the City.

As your staff noted, NYC Marketing has quickly developed from an idea, to a start-up organization, to a full-fledged working business that has and will continue to deliver valuable new benefits to the City. As it continues to grow, we acknowledge that our agreement with the City may require adjustments to manage such growth. We look forward to making any needed adjustments and view such as a sign of our continuing success.

Please find attached a detailed response to each of your NYC Marketing recommendations. We are grateful for the time and consideration afforded to us by your audit staff. We look forward to continuing to work with your office and help build on our current progress. Thank you again for your ongoing support.

Sincerely,

Kevin A. Booth
Chief Financial Officer

NYC Marketing's Responses to the Findings

Response to Audit Report (FM05-121A) of New York City Marketing Development Corporation

This attachment contains NYC Marketing's response to the two condensed findings and two recommendations made by the Audit Report (FMO5-121A).

Response to Finding I Regarding Financial Oversight

OMB Properly Oversees NYC Marketing's Finances
NYC Marketing has an agreement with the City which clearly articulates how the Corporation must operate. This agreement is submitted, approved and registered by the Comptroller annually. As you know, it provides for, among other things, regular financial reporting and correspondence with OMB ensuring their full and complete oversight. NYC Marketing has strictly complied with these provisions since its inception. NYC Marketing's regular reporting to OMB includes:

1) an annual budget to OMB for their approval;
2) regular progress reports including a statement of sources and uses of funds and a balance sheet;
3) a regular forecast of revenue, expenses, and monthly cash balances;
4) regular variance reports as needed.

In addition to adhering to the policies in our agreement, NYC Marketing meets with OMB on an ongoing basis to review our progress and business plans in order to further refine our business strategy and the oversight of our operations.

Comptroller's Financial Snapshot Fails To Acknowledge Planned Expenses in Future Months
Your financial snapshot failed to acknowledge large expenses coming due in the immediate months following the end of the fiscal year. While the audit correctly noted that NYC Marketing had a cash balance of $1.6 million it failed to acknowledge that NYC Marketing also had $1.7 million in outstanding bills due in the immediate coming months.

These imminent expenses included payments for our start-up loan and significant bills coming due in July and August primarily related to underwriting the cost of recruiting the Country Music Awards to New York. In fact, our cash balance three months later (August 15, 2005) was $313,097. All of this data was provided to your staff and we're unclear why these details were not fully noted in the draft audit.

Response to Finding 2 Regarding Vending Commissions

NYC Marketing Distributes Vending Commissions Appropriately
Working together with input from City agencies and OMB, NYC Marketing created a policy for the distribution of half of the vending commissions. This distribution policy, adopted by OMB, sought to replace previous vending revenue and provide an ongoing incentive for City agencies. This policy strictly adheres to NYC Marketing's agreement with the City.

Response to Recommendation 1:
NYC Marketing respectfully disagrees with this recommendation and will continue with its current distribution policy.

Response to Recommendation 2:
NYC Marketing respectfully disagrees with this recommendation and will continue with its current distribution policy.

The City of New York
Office of Management and Budget
75 Park Place • New York, New York 10007-2146
Telephone: (212) 788-6013 • Fax: (212) 788-6548

Mark Page
Director

Mark Montgomery
Associate Director

February 24, 2006

Ms. Gayle M. Horwitz
Deputy Comptroller & Chief of Staff
Office of the Comptroller
1 Centre Street
New York, New York 10007-2341

Re: Audit of the Financial Practices of the New York City Marketing Development Corporation FM05-121A.

Dear Ms. Horwitz:

Thank you for the opportunity to respond to the draft Audit Report on the Financial Practices of the New York City Marketing Development Corporation (MDC), dated February 13, 2006.

OMB is pleased that the audit found MDC's revenue and expenditures accurately reported. However the finding that there are "inadequate procedures to monitor NYC Marketing's financial operation" misstates the extent of our role in the active oversight of MDC's budget.

The report further claims that "the City has yet to establish formal procedures and a methodology that would allow it to effectively monitor NYC Marketing's financial activities to ensure that funds in excess of NYC Marketing's cash operating requirements are paid to the City." OMB has clearly explained to your audit staff the consistent practices which OMB employs in ensuring the transparency and accuracy of MDC's financial activities, and in ensuring that funds in excess of NYC Marketing's cash operating requirements are paid to the City. OMB shares with the Comptroller's Office a commitment to ensure that the Marketing Development Corporation conducts its operations with accountability, according to OMB policies and directives, and ultimately to the City's benefit.

Please find attached a detailed response for each of your recommendations pertaining to OMB. We are grateful for the time and consideration afforded to us by your audit staff throughout the course of their endeavors.

Sincerely,

Mark Montgomery

Recommendation #3: *Establish written procedures and a methodology that would enable it to closely monitor NYC Marketing's financial activities to ensure that funds in excess of NYC Marketing's cash operating requirements are paid to the City.*

OMB Response:
Although OMB may issue written directives and enter into written agreements that provide for specific financial reporting, OMB does not have written procedures for monitoring financial activities. OMB routinely relies on commonly practiced methods for financial analysis including human interaction to carry out its mission responsibly and effectively.

At the beginning of each fiscal year MDC submits to OMB a preliminary budget for analysis and approval. OMB is further provided, on a quarterly basis, current and projected revenues, expenses and cash position which are subjected to a careful review by assigned staff and compared against the adopted budget. OMB and MDC further engage in on-going dialogue in order to identify circumstances that could significantly alter the approved budget. Given that MDC is a new and novel enterprise, OMB has determined that careful long-term cash planning is crucial. Until such time as MDC's operations become consistent and predictable, it is prudent management policy that the Corporation always retain sufficient cash to meet one to three months' worth of operating expenses.

OMB is very cautious in determining when and if MDC is in a position to remit monies to the City. The audit report claims that at the end of FY 2005 the Corporation held cash of $1.6 million. However the report fails to correctly clarify that this cash balance was not a result of MDC's operating activities from the fiscal year, but was mostly attributable to a $1.2 million loan provided by the NYC Economic Development Corporation in FY 2004. In FY 2005 MDC remitted a payment to this entity in the amount of $103,258 and has, since then, been making consistent monthly payments towards the expiration of this loan—currently anticipated for the end of this fiscal year. Based on discussions with MDC and a careful evaluation of its operations, it became apparent that MDC's expenses in the beginning months of FY 2006 would exceed its revenues, thus precluding it from remitting monies to the City. In fact, MDC's cash balance at the end of FY 2006's first quarter had dropped to $361,244.

Recommendation #4: *Develop financial benchmarks to evaluate NYC Marketing's budgetary needs and to ensure that the City receives a portion of the revenues generated by NYC Marketing activities.*

OMB Response:
Since MDC began its operations in July of FY 2004, OMB has played an active role in the development, approval and timely oversight of its budget. In this effort, OMB employs the same principles and practices it undertakes in oversight of other agencies and/or covered organizations. OMB engages in standard and consistent methods when evaluating the financial activities of MDC and makes use of any resource necessary to ensure that the objectives set forth in the City contract are fully complied with. The Corporation's activities will continue to be subject to OMB's careful scrutiny to ensure the appropriateness and timely remittal of revenues to the City.

Recommendation #5: *Ensure that NYC Marketing addresses the report's findings and implements the report's recommendations.*

OMB Response:
OMB will continue to apply its experience and judgment in ensuring that MDC's budget is leveraged to yield the most benefit to the Corporation and the City.

cc: Mark Page, OMB
Stuart Klein, OMB
Yvonne Quintian, OMB
Michelle Levine, OMB
Howard Friedman, LAW
George Davis III, MOO
Susan L. Kupferman, MOO
Joseph Perello, NYCMDC
Kevin Booth, NYCMDC